TOAGOSEI

Maximizing Efficiency, Driving Performance

Annual Report 2005

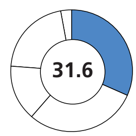
Toagosei's Business Domains

Business Segment

Commodity Chemicals

Sales by Segment

(%)



	Millions of yen		
	2005	2004	2003
Sales	¥47,892	¥46,271	¥44,536
Operating Income	4,026	3,319	3,015

Description

Toagosei manufactures a wide variety of inorganic industrial chemicals, notably caustic soda, as well as fertilizers, metal degreasing and cleaning agents, and ultra-pure chemicals and silicon based specialty gases for the semiconductor industry.

Main Products and Applications

Caustic soda:
Chemical fibers, pulp, dye, and pharmaceuticals

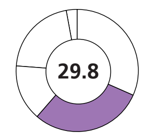
Oxygen:
Combustion enhancing gas for welding and cutting, combustion enhancing gas for steel making process, oxygen inhalation (and high pressure oxygen treatment) for medical use, oxygen aeration for wastewater treatment, oxygen-based pulp bleaching, and fermentation in biotechnology

Sulfuric acid:
Fertilizers, synthetic fibers, and inorganic chemicals

Trichloroethylene:
Metal degreasing and cleaning, solvents, and raw materials for hydrofluorocarbon

Business Segment

Acrylic Products



	Millions of yen		
	2005	2004	2003
Sales	¥45,111	¥41,926	¥41,307
Operating Income	5,344	3,269	375

The Toagosei Group produces the whole range of acrylic monomers, including acrylic esters, which we were the first to produce commercially in Japan, and their derivatives such as acrylic polymers. Acrylic polymer flocculants have proven effective in the purification of sewage and industrial wastewater. In the civil engineering and construction fields, acrylic polymer resins make ideal water-resistant coatings for roofs, external walls and so on. The Toagosei Group offers an integrated service from material production to on-site application.

Acrylic esters:
Acrylic fibers, fiber processors, paints, pressure sensitive and other adhesives, leather processors, paper processors, and acrylic rubber

Acrylic acid:
Nonwoven cloth binders, flocculants, dispersants, paper processors, superabsorbent resin, and detergent builders

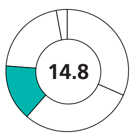
Polymer flocculants:
Treatment of various kinds of wastewater and dehydration of sludges

Construction materials:
One-pack waterproof spray materials, decorative waterproof wall materials, permeable type water-absorption preventive agents, chemical grouts, and earth resistance reducing agents

The catch phrase on the cover, "Maximizing Efficiency, Driving Performance" expresses the core concept behind our medium-term management plan for fiscal 2005-2007. It was printed using ink made from our popular UV/EB-curable acrylic product *Aronix*.

Business Segment

Specialty Chemicals



	Millions of yen		
	2005	2004	2003
Sales	¥22,351	¥20,645	¥14,707
Operating Income	3,234	2,882	2,520

Toagosei has developed and commercialized a long list of unique and high-value-added products for both industrial and consumer use. These include the cyanoacrylate instant adhesive *Aron Alpha* (sold under the name *Krazy Glue* in the U.S.), as well as the silver-based antimicrobial agent *Novaron*. The UV-curable resin *Aronix* has become widely used in paints, inks, and as surface coatings for cell phones, compact discs and many other applications.

Special monomers and oligomers:
Raw material for paints, printing inks, coatings, and adhesives

Cyanoacrylate instant adhesives:
For bonding rubber, plastic, metal, and wood in industrial and consumer uses

Silver-based antimicrobial agents:
For kitchen and bathroom equipment, building materials, and textiles

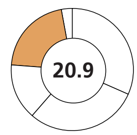
Antifungal agents:
For kitchen equipment, home appliances, and paints

Heat-resistant adhesives:
For bonding metal and ceramics used in high-temperature environments

Hot melt adhesives:
For bonding plastics, metals, and textiles For bonding difficult-to-bond plastics like polyethylene, polypropylene polyester, and nylon

Business Segment

Plastics



	Millions of yen		
	2005	2004	2003
Sales	¥31,655	¥30,656	¥27,373
Operating Income	3,302	3,897	2,609

Our subsidiary, Aron Kasei is developing products in four principal areas:
1) pipes and couplings for water supply and for sewerage use, 2) protective casings for electric power and telecommunications lines, 3) garbage reduction and recycling systems to address environmental preservation needs, and 4) nursing care products.

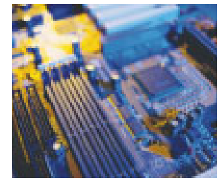
Pipes & couplings:
Rigid PVC pipes

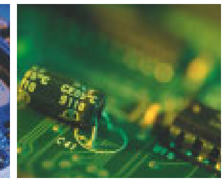
Environmental products:
Trash receptacles

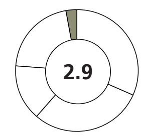
Nursing care products:
Portable toilets, nursing care bath products

Business Segment

Other Businesses







	Millions of yen		
	2005	2004	2003
Sales	¥4,433	¥4,784	¥4,530
Operating Income	(670)	(758)	(568)

To make our dreams of the future come true, we are putting our efforts into developing products that facilitate harmony between human activities and the natural environment. In the electronics field, our high-purity ethylene carbonate, and our TRIES silane chemicals for CVD (chemical vapor deposition) processing, are attracting attention from makers of LCDs and semiconductor devices. At Toagosei, we will continue to develop products that meet user needs and are in tune with the times.

Notes 1 : Segmentation in the above table is by product category. Segmentation shown on pages 8 to 17 is according to organizational structure.

2 : Product category realignment
Segmentation in the above table is by product category. Segmentation shown on pages 8 to 17 is according to organizational structure. During the reporting term, Toagosei spun off the functional materials section of its Acrylic Products Department to create the newly independent Functional Materials Department. With effect from the reporting period (2005), the Company reclassified its products in line with this reorganization, whose purpose was to clarify product segmentation. Figures for the previous business term (2004) shown here have been recalculated in line with the new classification.

Financial Highlights

Toagosei Co., Ltd. and Consolidated Subsidiaries

Years ended December 31, 2005, 2004 and 2003

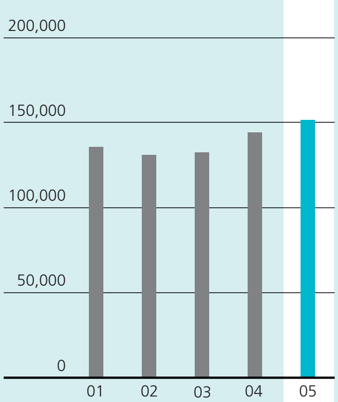
	Millions of yen			Thousands of U.S. dollars (Note 1)	05/04
	2005	2004	2003	**2005**	Change (%)
Net sales	¥151,443	¥144,283	¥132,455	$1,282,657	5.0
Operating income	15,236	12,611	7,951	129,046	20.8
Income before income taxes and minority interests	16,846	10,321	6,125	142,682	63.2
Net income	12,131	8,996	1,719	102,750	34.8
Per share of common stock (in yen and dollars):					
Net income (Note 2)	46.31	34.38	6.57	0.39	34.7
Cash dividends applicable to the year	7.50	6.00	3.00	0.06	25.0
Total assets	186,521	174,766	166,005	1,579,755	6.7
Shareholders' equity	99,501	83,513	74,476	842,734	19.1

Notes 1: U.S. dollar amounts are translated from yen, for convenience only, at the rate of ¥118.07 = $1.00.

2: Beginning with the term ended December 31, 2003, earnings per share are calculated based on the average number of ordinary shares outstanding during the term after deduction of the average number of shares in treasury in accordance with revised accounting standards. For the previous terms, relevant figures were calculated based on the average number of ordinary shares during the term in question.

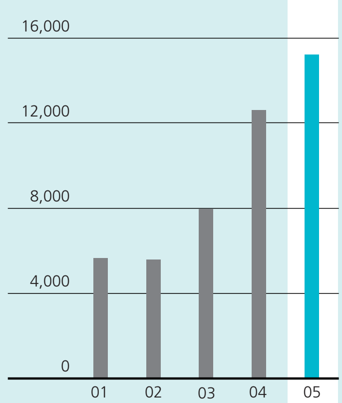
Net sales

(Millions of yen)



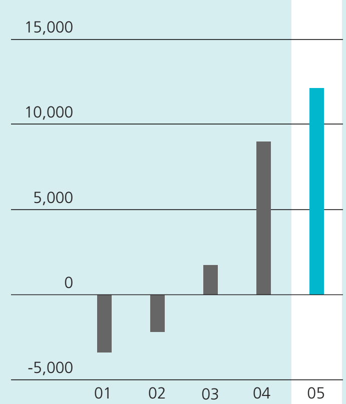
Operating income

(Millions of yen)



Net income (loss)

(Millions of yen)



Interview with President Yamadera

Aiming at sustainable growth, leveraging the strong management and financial base resulting from the bold restructuring of our business portfolio

Record profits on a consolidated basis

Q Your fiscal 2005 business term was the first year of your new three-year medium-term management plan. Could you give us your opinions on the Company's 2005 business performance?

A During the past year, we have reaped the fruits of our efforts to reform our corporate governance system in such fields as cost-efficiency and the integration of management at the consolidated group level.

We were also fortunate with regard to the business environment, as demand for our products on the market exceeded supply up to September, in addition to which we were successful in translating the high price of raw materials into higher product selling prices.

In the October-December fourth quarter, however, our profitability came under pressure as market prices in Southeast Asia began declining. For the full term, ended December 31, 2005, operating income on a consolidated basis surpassed the target figure to record an all-time high, with the ratio of operating income to sales reaching 10.1%, not far off the ultimate target of 10.4% under the current three-year business plan.

Generally speaking, I believe that we have made good progress in attaining our goals under the medium-term plan – in a qualitative sense as well as in terms of the figures posted. Our stated policy is to focus management resources on our areas of core competence (including promising businesses that require restructuring) while downsizing our operational scale in (or withdrawing from) areas deemed unlikely to become profitable. We have virtually completed our business portfolio realignment in line with this policy. In our core businesses, we aim not to be like a department store, trying to maintain as extensive a product lineup as possible, but to selectively focus our management resources on those products and services in which we have, or expect to have, a competitive edge, and which promise to deliver a high profit margin. Toagosei and all the members of its group will exert their full efforts in the creation of a high-value-added, high-profit business structure.

Reinforcing the Group's international production network for priority businesses

Q What progress is being made in developing Toagosei's three priority businesses – photocurable resins, adhesives, and high-purity inorganic chemicals – which the Company hopes will be its main future engines of growth?

A All three businesses are proceeding according to schedule. UV-curable resins have excellent prospects of developing into a profitable business in the future, and an independent business unit – the UV-Curable Resins Group – was set up in 2005 to handle these materials. The Toagosei Group already enjoys a 40% share of the Japanese market and a 10% share of the world market for these materials, and demand is expanding, particularly for the screens used in the displays of PCs, cell phones, and many other electronic appliances. For this reason, we started operation at a new production plant in China in September of 2005, and we also expanded the production capacity of our Nagoya Plant. With this, we have a strong production network for UV-curable resins encompassing facilities in Japan, Taiwan, and China, and we confidently expect this business to make a significant contribution to our earnings in the near future.

Regarding adhesives, consumer-use instant adhesives sold well during the reporting period, garnering an 80% share of the Japanese market and an estimated 50%-60% share of the U.S. market. In the world market, industrial adhesives makers are embroiled in overcompetition, but in the niche markets of photocurable adhesives and hot-melt adhesives, which are among Toagosei's special strengths, we aim to raise our global market presence still further.

In response to rising market demand for high-purity inorganic chemicals, we are currently constructing facilities for the production of high-purity liquefied hydrogen chloride at our factory in Tokushima (construction should be completed in November this year). We have already expanded our production capacity for high-purity hydrochloric acid and high-purity caustic soda. As demand is particularly strong in Korea and Taiwan, over the near future we will be collaborating with our group member Tsurumi Soda Korea, and will be putting extra emphasis on sales promotion targeting overseas manufacturers in the information technology sector.

Nurturing new businesses to serve as growth drivers

Q What are your operational strategies for 2006, the middle year of the current three-year management plan? Also, please give the readers your projections for the Company's business performance in 2006.

A I believe that 2006 will be a year that will bring out the true enterprise value of the Toagosei Group. To ensure continued growth, we must nurture new businesses to the point where they can stand on their own feet, and for this purpose, in 2006 we plan to invest a total of ¥11.1 billion in existing and new-venture businesses.

We intend to speed up the process of reinforcing our acrylic product operations. Specifically, in the field of flocculants, we plan to establish a joint venture with Mitsui Chemicals Aquapolymer, Inc., which is scheduled to start operations in October 2006. We envisage this company making full use of the fact that its parent companies are able to supply the required high-quality raw materials,

Akihiko Yamadera
President

thus achieving a considerable synergistic advantage.

In addition, to expand our downstream acrylics operations, we are developing new value-added products, with work currently proceeding on approximately 20 new items.

With effect from fiscal 2006, three new Chinese companies – TOA-DIC Zhangjiagang Chemical Co., Ltd., Toagosei Hong Kong Ltd., and Toagosei (Zhuhai) Ltd. – have been included in the scope of consolidation.

Turning to our prospective business performance on a consolidated basis in fiscal 2006, in view of the continuing high price levels of raw materials and fuels, and the slight weakening of demand in East Asian markets, we are forecasting sales of ¥154 billion, recurring profit* of ¥14.8 billion, and net income of ¥7.6 billion. These are somewhat conservative projections, and there is plenty of room for an upward revision of earnings in the event of a recovery in market demand/prices.

* Due to reclassification, recurring profit does not appear on the income sheet.

Strengthening Toagosei's internal control to fulfill its corporate social responsibilities

Q Strong pressure, such as the enactment of the new Corporate Law in May, is being exerted on companies to bolster and modernize their corporate governance systems. How is Toagosei responding to these circumstances? I am sure the readers would also like to hear about your dividend payment policy and your long-term management vision.

A We have put considerable work into strengthening the Company's management supervising functions and the degree of our compliance with laws and ethical standards. On April 1, 2006 we set up the Internal Control Section as a first step toward ensuring that the Company fully meets international standards of compliance, which are soon to be codified in Japan with the enactment of a local version of America's Sarbanes-Oxley Act and the new ISO 2700-series of information security standards. It is the earnest desire of the management of Toagosei that we proactively and unreservedly fulfill our corporate social responsibilities.

Regarding the return of profits to our shareholders in the form of dividends, as our business performance for FY2005 was favorable, we raised our annual per share dividend payment by ¥1.50 to ¥7.5 per share. For the foreseeable future, we hope to stabilize the minimum dividend payment at ¥6 per share, while raising the payout on a case-by-case basis whenever the Company's business performance is particularly good.

The present business environment does not warrant an optimistic attitude, but we believe that, by making the best use of our expertise and putting forth our full effort, we have every chance of attaining our medium-term management plan targets of ¥163 billion in sales and ¥17 billion in operating income. This will mark an end to our period of conservative management and put us solidly on the path to sustained growth.

In conclusion, and on behalf of the entire management of the Toagosei Group, I look forward to the continued support and encouragement of our shareholders.

Toagosei's R&D is making great strides toward the development of next-generation products and technologies

Q What sort of achievements did you record in the field of R&D during the first year of the present medium-term management plan? Please first tell the readers about your "Policy No. 1" – developing next-generation core products.

A Overall, things are going according to plan. The Electronics Group is engaged in developing materials for use in semiconductors, flat panel displays, and other opto-electronic applications. Our high-purity ethylene carbonate for use in cleaning LCD substrates to remove resist residues has been chosen by a major LCD maker, and user demand is expanding at a brisk pace. Additionally, our special silicon material has been adopted by major Japanese semiconductor makers as a raw material for the manufacture of resists. Demand for our high-purity silicon hexachloride (for use in making nitride films for semiconductor circuit protection) is rising on a global scale, and we have begun mass production. We will also be starting mass production of solder resist film for hard disk drives in the latter half of 2006.

Under the policy of winnowing down the business portfolio to allow focus on core competencies, the Life Science Group has sold off its ecologically friendly agrochemicals business, and has reorganized itself as a unit specializing in fuel-cell batteries and medical diagnostic and testing agents. We have succeeded in developing fuel-cell membranes with an effective lifespan of 7,000 hours, and this product has drawn considerable attention at recent international trade shows. We plan to actively ship samples to domestic and overseas manufacturers in 2006, and will be making fullscale efforts to put this business on a viable commercial footing. As for medical diagnostic and testing agents, three diagnostics for auto-immune system diseases underwent clinical trials during the term, one of which has already proved efficacious, enabling us to register it as a diagnostic.

An electric motor-driven miniature car powered by a direct methanol fuel-cell battery utilizing pore-filling electrolyte membranes

Hideki Kato,
Director and General Manager of Corporate R&D Department

Q What success have you had in following your Policy No. 2 – Acquiring Future Core Technologies?

A Progress has been achieved in the fields of holographic data storage materials, in initiatives together with the Technology Research Association for Advanced Display Materials (TRADIM), and in the bioinformatics technology field. Our research partner Optware Corp. is developing a holographic material for optical disks, and hopes to announce pilot production of a material in September of this year.

The partners of TRADIM are pursuing a joint development project targeting plastic substrates for use in ultra-thin liquid crystal displays using roll-to-roll processing. Toagosei's contribution is the development of an adhesive required for the interior of the film's structure. From 2006, as the second stage of the project, we will be working on the development of an adhesive to join together the components.

In the field of bioinformatics, in jointly-pursued development efforts, we have elucidated the DNA sequences for certain newly identified peptides (obtained from the cells of adipose tissue) which have the capacity to cause the regeneration of nerve cells. We have completed filing for the acquisition of patents on these peptides, and following this, we intend to tackle the development of an anti-viral agent.

Q What likely developments are there in store for you with respect to your Policy No. 3 – Realizing More Effective R&D?

A To raise the efficiency and practical effectiveness of our research and development activities, we plan to invest even more management resources than hitherto in analysis, evaluation of the properties of materials, acquisition of intellectual property, and the investigation of new technologies and new materials. Last year, we set up the Material Properties Group, which draws its members from all divisions of the Company. To ensure a higher level of technical expertise among members of the Group, we are sending research staff on study courses at major Japanese universities.

Guided by its three basic policies, the Toagosei Group will continue to develop new businesses and bring to market high-quality, innovative products – both of which are essential drivers of future growth.

Commodity Chemicals

Reorganizing existing businesses and bolstering our business base by enhancing capabilities in high-purity inorganic chemicals

Earnings improve thanks to growth in shipment volume and price raises

We enjoyed favorable shipments of caustic soda and high-purity inorganic chemicals in the 2005 business term. Moreover, we were able to pass on to our customers the increased prices of our raw materials and fuel. As a result, sales posted year-on-year growth. Sales of high-purity inorganic chemical products for semiconductor manufacturers were particularly strong, against the background of an expansion in the information technology market. There was a decrease on a volume basis in shipments of inorganic chlorides and organic solvents (chlorinated solvents), and sales of both categories recorded a slight year-on-year decline. Shipments of sulfuric acid and industrial-use gases held firm, securing a year-on-year growth in sales.

As a result of the above, total sales of the Commodity Chemicals business, on a consolidated basis, registered year-on-year growth of 3.5%, to ¥47.9 billion, exceeding the targeted figure of ¥47.2 billion by approximately ¥700 million.

Restructuring existing businesses and enhancing capabilities in high-purity inorganic chemicals

Last year, we set out the restructuring of our existing businesses and the enhancing of our capabilities in high-purity inorganic chemicals as priority goals. This was part of an overall clarification of the status of each of our businesses, which were put into one of two categories: businesses to be nurtured and reinforced, and businesses to be downscaled, or even withdrawn from completely. In this way, we have radically overhauled our portfolio of businesses.

This was performed in stages. Firstly, approximately 70% of a concrete action plan was implemented. During the current year, we intend to complete the remaining 30%. Among existing businesses, the most urgently pressing issue we face at the moment is to devise and push through a radical restructuring plan for the organic chlorides business, which has been suffering from worsening profitability owing to a larger-than-projected falloff in demand. As the first steps toward this objective, we will be taking various measures to make the operations of our electrolysis plant more adaptable to declines in market demand. Principally, the plant currently relies on an in-house power generator, and the running costs of this generator are excessively high because the plant is not operating at anywhere close to full capacity utilization. We therefore intend to

Household products including soap are made from caustic soda.

Welding process employing shield gas made by Toa Techno-Gas Co., Ltd.

switch back to buying power from utilities companies.

We are continuing to expand the production capacity of our top-priority inorganic high-purity chemicals business. At our plant in Tokushima, we have begun construction of the No. 2 production complex for high-purity liquefied hydrogen chloride. The complex is scheduled to be completed in the latter half of 2006.

At our Nagoya Plant, where we have concentrated all our electrolysis operations, we are in the process of expanding production facilities for high-purity caustic potash for CMP (chemical mechanical polishing) and for solutions of sodium hypochlorite with low concentrations of bromine. Demand for both these products is expected to increase, and we are planning to bring them to market as soon as possible. Additionally, we are constructing additional facilities for the production of high-purity chlorine by refining the gaseous chlorine obtained from the electrolysis process. Such high-purity chlorine is in strong demand from manufacturers of semiconductors and optical fiber. From this spring up to the latter part of the year, these production lines currently under construction will be successively coming on stream, and we are confident that this will effect a positive turnaround in the profitability of our business portfolio, leading to an improvement in business performance.

Putting greater focus on products for growth markets, particularly the IT field

Toagosei's medium-term management plan places emphasis on products for the information technology field, which is experiencing strong growth. Particular focus is being put on semiconductors, LCDs, and plasma displays. With respect to the Company's high-purity inorganic chemicals, we have set a sales target for 2007 of twice the ¥2.1 billion recorded in 2004. To attain this, we must not only develop attractive new products and bolster our production capacity, we must also enhance our marketing capabilities and speed up our efforts to satisfy our customers across the total spectrum of their needs, including product quality and reliability of supply.

Meanwhile, we plan to reinforce our collaboration with our wholly owned subsidiary Tsurumi Soda, which operates a plant in South Korea, with the aim of increasing our sales to IT-sector companies overseas.

Acrylic Products

Expanding downstream acrylic operations by carefully selecting promising business fields, and exploiting the possibilities of our unique proprietary technologies

Improving profitability in downstream products

We enjoyed strong demand in fiscal 2005 for polymer products and flocculants. Along with the recovery of monomer markets, total sales posted a large year-on-year increase. Profitability showed a marked improvement, especially in downstream products, as we withdrew from unprofitable operations and brought new products to market. Powder products and construction materials, both of which were incorporated into the Acrylic Products business, marked steady sales.

Selecting promising business fields

Fiscal 2005 was the first year of our current (2005-2007) medium-term management plan, and we pursued a number of action plans in line with the basic aim of the Acrylic Products business – to expand downstream derivative product operations. The top-priority task was to carefully select promising business fields.

We completely withdrew from unprofitable business fields such as superabsorbent resins, and concentrated management resources on the development of new products such as special dispersants and high-performance retention aids for paper industries, which make full use of Toagosei’s proprietary technological expertise.

Regarding existing products, we made further progress in the development of new production methods to raise productivity, and of higher-grade products by adding our proprietary resources. Overall, these action plans were successful, helping us to achieve the first-year goals under our medium-term management plan.

Acrylic fibers with various value-added properties

Aron Tac adhesives have a wide range of applications, including adhesives tapes and labels.

Raising the level of our elemental technologies

In the current term, fiscal 2006, we will continue to work toward the achievement of the final targets under our present medium-term management plan, especially with respect to further accelerating the development of downstream acrylic derivative product businesses. The main driver behind this speed-up process will be the further upgrading of the technologies that distinguish us from our rivals, and the creation of combinations of various elemental technologies. We will further exploit our precision polymerization and special cross-linking technologies to continue bringing new products to market, especially in the electronics sector. In combination with these efforts, we will conduct a rigorous review of costs at all our production facilities to identify ways of lowering total costs, thus giving us an extra edge in cost-competitiveness in this business.

Topics

On February 8, 2006, Toagosei, Mitsui Chemicals, Inc. (MCI) and Mitsui Chemicals AquaPolymer, Inc. (MAP) reached a basic agreement on proceeding with talks to integrate the polymer flocculant businesses of Toagosei and MAP.

Toagosei, MCI and MAP intend to operate production, sales and R&D comprehensively and to transform the business to cope with anticipated severe competition and expanding markets worldwide.

Adhesives

Concentrating management resources on product research and production technology, and shortening development lead times

Adhesives domain established, sales and profits rise

To reflect the status of adhesives within Toagosei's total product lineup as a top-priority product category, with effect from fiscal 2005 we created the Adhesives Department with the intention of further strengthening our adhesives operational structure. Previously, the adhesives business was handled by the Functional Products Department, and the remaining portion of the old department has been renamed the Functional Materials Department.

In the Japanese market, sales of both consumer adhesives (known as *Aron Alpha*) and industrial adhesives reached our planned targets. In the latter category, sales were particularly brisk to customers in the automotive and electronics industries.

In the U.S. market, our consumer-use cyanoacrylate instant adhesive (known as *Krazy Glue*) posted a strong increase in sales.

On a consolidated basis, the adhesives business registered both revenues and earnings in excess of the targeted levels.

Marketing and product development initiatives in FY2005

In the field of consumer adhesives on the domestic market, during the reporting period, to raise the recognition profile of new products among the buying public, we made aggressive use of sales aids that help field sales personnel to make sales presentations to customers, and carried out a sales campaign featuring cash prizes for purchasers of *Aron Alpha*.

In industrial adhesives, we positioned UV-curable acrylic resin-based adhesives, hot-melt adhesives, and reaction adhesives as priority products, and worked to develop adhesives specifically tailored to the requirements of customers in growth markets such as automotive components and electric appliances. Having determined that UV-curable adhesives was an important product category where Toagosei could effectively showcase its superiority in acrylic resin polymers and related technologies, we devoted considerable effort to product development in this area. Our efforts were rewarded with a strong increase in demand for our adhesives from automakers for use in filters.

PES hot melt adhesives are used for smart cards.

Toagosei's famous consumer-use *Aron Alpha* instant adhesives (known as *Krazy Glue* in the United States) are sold all over the world. They boast the top market share not only in Japan but also in the U.S.

In the fields of hot-melt adhesives and reaction adhesives, we enjoyed a steady uptrend in demand for these adhesives for use in the production of IC cards and IC substrates.

We took a number of steps during the term under review to improve the production yield and product quality of our mainstay instant adhesives. For the foreseeable future, we will be concentrating efforts on raising product quality as well as on developing new and more effective specialized products, as a means of increasing the value-added of this business.

In the U.S. market, we launched a series of new products to reinforce the whole *Krazy Glue* brand name. In industrial adhesives, as in Japan, we focused on developing products tailored to the specific application requirements of individual industrial niches.

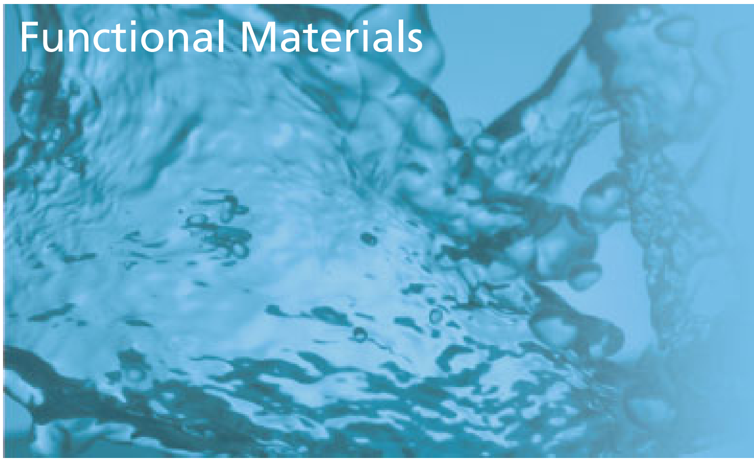
Medium-to-long-term outlook and strategies

For consumer adhesives on the Japanese market, our efforts will continue to be focused on speeding up the development of products and on reinforcing sales promotion campaigns to raise the recognition of our products.

In the Japanese market for industrial adhesives, we are making steady progress in establishing and leveraging a system for developing products that are tailored to the specific requirements of particular customers or customer categories. We intend to be highly selective, both in terms of the product categories to which we assign high priority, and in terms of approaching potential customers. Through concentration of management resources on product research and on production technology, we aim to shorten development lead times and bring new items to market as quickly as possible.

On overseas markets, we plan to expand sales of instant adhesives in China and European markets. We also have plans to develop new industrial applications for our adhesives in the U.S. market.

Functional Materials



Accelerating development of optical materials and other products for cutting-edge industries

Sales grow thanks to specialization in FPDs

At the beginning of fiscal 2005, the Functional Materials Department was separated from the Acrylic Products Department and set up as an independent entity focusing on high-performance, high-value-added materials, particularly the UV/EB-curable resin *Aronix* and the inorganic ion-exchanger *IXE*. By making the department into an independent entity, its business performance has become easier to evaluate, and its specialization in advanced functional materials has won greater trust from our customers.

The Functional Materials Department's No.1 product, *Aronix*, is available in two series: the M Series consists of raw materials for the manufacture of compound products, and the UV Series comprises finished compound products. We are particularly investing resources in strengthening the UV Series, which are high-value-added products selling at premium prices. We are putting special emphasis on materials for flat panel display (FPD) components, shipments of which, on a volume basis, rose strongly during the reporting period.

We also boast a range of unique and highly functional inorganic materials, notably the inorganic ion-exchanger *IXE*. We will continue to focus energy and resources on marketing as well as research into more advanced and specialized material functions, so as to open up and exploit new markets for higher grade products.

Production plant network covering Japan, Taiwan, and China facilitates reliable supply to customers

A major strategic development in fiscal 2005, which is the first year of our current three-year medium-term management plan, was the start-up of a UV/EB-curable resin manufacturer in China – TOA-DIC Zhangjiagang Chemical Co., Ltd., a joint venture with Dainippon Ink and Chemicals. Commercial production began in July of 2005, later than originally scheduled, but smooth progress has been made in establishing an efficient product quality management system.

With full-fledged operations at the plant scheduled in FY2006, we will have an ideal three-base production and supply system encompassing Japan, Taiwan, and China, and are pushing ahead with a plan to further open up the East Asian market for our products, primarily utilizing our production foothold in China.

In addition to its mainstay field of application in printing inks, *Aronix* is also used as a coating agent in the manufacture of optical disks.

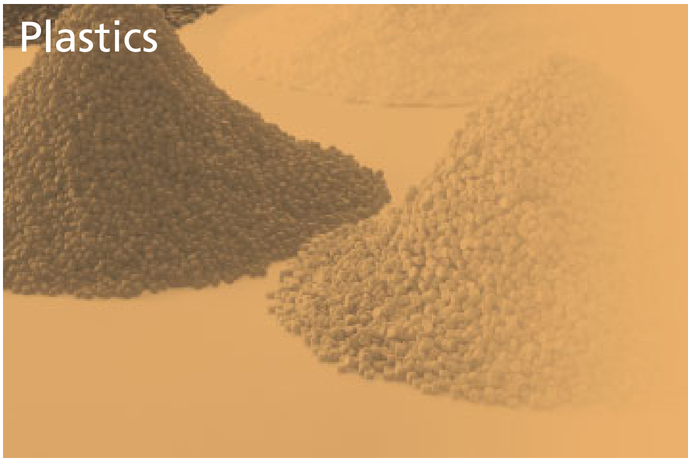
Novaron is a high-performance antimicrobial agent employed in the molding of a wide range of plastic products for everyday use.

In the UV Series, we are putting effort into developing new products in the field of FPDs, and are focusing on creating new products that will hopefully become our main earnings drivers in the category of UV-curable resins. Toagosei already enjoys the top market share in East Asia for this category of product. We are currently studying the feasibility of constructing another plant in one of the countries in the region, as a follow-up to our successful Chinese foothold.

Creating and nurturing potential blockbuster products

As a member of the Technology Research Association for Advanced Display Materials (TRADIM), where work is proceeding on the development of display materials for use in next-generation cell phones and other mobile terminals, Toagosei has made a number of significant breakthroughs in technological development. Project 1, which involved basic research, will be completed by the end of 2007, and we will commence research under Project II, which concerns the development of a commercially practicable product.

Our unique new UV/EB-curable material *Oxetan* has received considerable praise for its safety, high curability, and other features, and we have commenced shipments to makers of paints for cans, ink for ink-jet printers, and ink used in printing notices on food wrappings. We have already acquired patent rights (both the basic patent and applications) in Japan, the United States, and Europe, and *Oxetan* has tremendous potential for future sales.



Plastics

Moving into the growing business field of nursing care through development of distinctive products

Revenues up in FY2005, although short of target

Our subsidiary Aron Kasei, which is engaged in processed resin product operations, once again faced severe business conditions in fiscal 2005, owing to a decline in public sector demand (for use in sewer pipes and so on) and rising prices of raw materials. However, this was offset by a recovery in private-sector demand, and total sales of this product category, on a consolidated basis, rose 2.9% year-on-year in fiscal 2005, to ¥31,961 million, slightly below our target figure.

In a breakdown by product category, our mainline pipes and couplings edged up slightly, while everyday sundry goods, such as nursing care products, recorded an increase in sales as expected. Regarding compound plastics for molding, order-made molded products registered strong sales, but sales of raw plastic compound materials were down from the previous year's level, owing to weaker demand from makers of containers and packaging for foodstuffs.

At the profit level, we raised the selling prices of our own products to pass on increases in raw material prices, but the price of raw materials subsequently rose yet again. Moreover, we were also faced with the need to streamline our production processes by purchasing new production equipment and repairing existing facilities, and as a result, operating income registered a year-on-year decline.

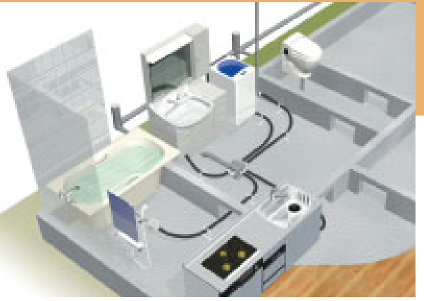
Expanding lineup of processed resin products, and increasing marketing efforts

As far as progress under the current medium-term management plan is concerned, we are seeking out potential needs in the five priority areas of pipes and couplings for sewerage use, protective casings for electric power and telecommunications cables, nursing care products, environmental preservation products, and plastic compounds, and are investing in more aggressive marketing campaigns to increase sales. In the field of nursing care products, we are focusing sales efforts on new products to meet the needs of this market, which has great growth potential.

We are also making progress in restructuring our production system. We closed one of our two plants in the Nagoya area and transferred part of the operations formerly conducted there to the remaining plant, where a new building was constructed to house plastic compound operations. Not only is this new production

Consumer needs for nursing care products such as portable toilets are growing and diversifying in parallel with the graying of society, and Aron Kasei is constantly widening its lineup of products to address their needs.

Aron Kasei has developed a centralized drainage system for single-family houses in which wastewater from the kitchen, washbasin, and bath is channeled through one pipe under the floor of the house. This reduces labor costs associated with installation as well as maintenance, and improves the system's efficiency.



line highly automated and thus more efficient, its production capacity is 50% higher than the previous facilities. Meanwhile, we are working on the development of new applications for plastic compounds in the fields of information technology, medical care, and packaging and containers for foodstuffs.

Addressing five priority management issues

Under our current medium-term management plan, we will continue in fiscal 2006 to address the following five management issues on a priority basis.

1. Developing new products based on close observation of market needs in the above-mentioned five priority areas (while simultaneously taking steps to improve the cost-competitiveness of existing products)
2. Rigorously enforcing cost-cutting in all departments to improve earnings
3. Further reinforcing our quality management system to ensure that our products fully meet our customers' exacting quality standard requirements
4. Pressing forward with the planning and development of new businesses with the aim of bringing them to the commercialization stage by the end of FY2007, the third and final year of our present management plan
5. Creating a new corporate culture through staff training and reeducation, and ensuring that our corporate culture is constantly renewed to meet the changing circumstances of the external environment

By tackling these issues head-on, rejecting half-measures and compromise solutions, we hope to make steady but sure progress toward reaching our goal of ¥35,500 million in total annual sales for fiscal 2007.

Toward Sustainable Growth

In its new medium-term management plan started in fiscal 2005, the Toagosei Group clearly spelled out its policy of putting top management priority on environmental protection by defining as a priority task the reduction and reinforced management of the environmental load caused by the Group's business operations. At the same time, the management of the Group takes its corporate social responsibility very seriously. In line with this stance, we are strengthening our compliance system and also making renewed efforts to ensure that we pay due attention to the rights of the individual, and that we practice no discrimination on the grounds of gender, ethnicity, age, etc. in our staff promotion, compensation and hiring activities.

Responsible Care – the Fundamental Stance of the Toagosei Group

The Toagosei Group is committed to working to ensure the safety of its products, and to reducing the impact on the environment of these products and their manufacturing processes, at all stages from development through use to final disposal.

Environmental management by setting specific targets

The Toagosei Group has determined three priority issues within its overall environmental protection activities – promoting energy saving, reducing the volume of industrial waste generated by the Group's operations while promoting reuse and recycling; and reducing emissions of substances harmful to the environment. Specific numerical targets have been set, and all employees of the Group are working toward their attainment.

Regarding environmental management, inspections for conformity with the standards of the ISO 14001 international environmental management systems certification are carried out every year. To realize a continuous cycle of improvement in our environmental management activities, we effectively employ the Deming, or PDCA (plan, do, check, act) Cycle, and this is reflected in the environmental protection initiatives described below.

We adopted the environmental accounting system in fiscal 2000 to make our environmental preservation measures more widely known among our customers and stakeholders. It also allows us to obtain a more precise grasp of the cost-effectiveness of our environmental activities, enabling us to find ways of pursuing them more efficiently.

In addition, we are putting even more effort into a wide range of environmental and social contribution activities, including education for our staff in environmental matters, the development of environmentally friendly technologies, afforestation programs, and cleanup initiatives in the local communities where we operate.

Environmentally friendly technology

Development of electrolysis using gas diffusion electrodes

Caustic soda production is a classic example of an energy-intensive industry. Toagosei is taking part in a joint project to develop an electrolysis method using gas diffusion electrodes that could result in as much as a 40% saving in power consumed. We are conducting development work on the application of this technology at the commercial level at our Nagoya Plant. The technology is attracting considerable attention as an effective method of retarding the global warming process in line with the goals of the Kyoto Protocol.

Achievements in tackling priority issues (as of FY2005)

1 Energy conservation	We reduced energy intensity at our work places in fiscal 2005 by 1.3% compared with the previous business term. Carbon dioxide emissions were also cut by 3.8% year-on-year.
2 Reduction of industrial waste	Thanks to progress made in the reuse of resources, the volume of waste subject to final disposal declined by 74% from 1,850 tons to 467 tons.
3 Cutting emissions of environmental load substances	We took steps to address this problem from two perspectives: installing new facilities (and bolstering the capacities of existing facilities) for the removal of substances that cause environmental load from the smoke, gas, or industrial waste water emitted by our plants; and strengthening our management of such substances, replacing them with environmentally harmless substitutes wherever possible. As a result, emissions in fiscal 2005 by the Group's factories decreased by 49% year on year from 87 tons to 44 tons.

Corporate Social Responsibility and Compliance

Fulfilling our responsibilities to all our stakeholders

The Toagosei Group has issued to all its executives and employees the Group's Code of Conduct and the Manual of Behavioral Standards. We are also pursuing a compliance-focused style of management, centered on the Compliance Committee, which includes outside members. Additionally, to identify and remedy problems at an early stage, we have set up two whistle-blower "help lines," one within the Company and one outside it operated by a legal firm, to enable staff to report on suspected illegal or unethical behavior by conventional mail, e-mail, or telephone. Our most recent initiative in this field was the establishment in April 2006 the Internal Control Section to perform the twin function of strengthening the Group's compliance and corporate governance.

Regarding respect for individual rights, particularly the avoidance of discrimination, in our hiring practices, we take great pains to ensure that hiring, job assignment, and pay & promotion are all conducted with full respect for fairness and the rights and dignity of the individual. In particular, we conduct education sessions targeting our male staff regarding the need to conform to the provisions of the Equal Employment Opportunity Law, and to ensure that no sexual harassment takes place within Group companies.

In our relationships with our customers, we take great care to observe the stipulations of the Personal Information Protection Law, which came into full effect in April 2005, and have drafted our own Personal Information Protection Policy. We also take fully into consideration the legal and ethical requirements relating to consumer protection and product safety. Other social contributions by the Group include providing support for local sports events near our plants, giving guided tours of our plants to local people, and participating in community events and other social activities. In these and other ways, the Toagosei Group cultivates a harmonious and friendly relationship with the local communities of which it is a corporate member.

Board of Directors and Corporate Auditors

Shigehisa Hibino Hideki Kato Manabu Terao Bunshiro Fukuzawa Akihiko Yamadera Akio Arisawa Katsutoshi Yamada Jun Kuboyama

Chairman
Bunshiro Fukuzawa

President
Akihiko Yamadera

Directors
Manabu Terao
Akio Arisawa
Hideki Kato
Katsutoshi Yamada
Shigehisa Hibino
Jun Kuboyama

Senior Executive Officers
Yasushi Funaki
Toyohiko Kitano
Yoshinobu Yamashita
Hisanori Abe
Suemori Takashima

Executive Officers
Kunio Sato
Yasutaro Yasuda
Futoshi Hashimoto
Shigeo Suzuki
Masaharu Matsubara
Masakazu Ishii
Shinichiro Otani
Kenji Sugishita
Norihiko Ono
Shoji Kawamura

Corporate Auditors
Hirotada Ito
(Standing)
Takeyoshi Ono
Shou Sato
Masao Numata
Fumihiro Hanada

(As of March 31, 2006)

Eight-Year Selected Data

Toagosei Co., Ltd. and Consolidated Subsidiaries

Years ended December 31

	Millions of yen (except per-share data)							
	2005	2004	2003	2002	2001	2000	1999	1998
For the fiscal year:								
Net sales	**¥151,443**	¥144,283	¥132,455	¥131,092	¥135,583	¥145,246	¥150,822	¥145,896
Income (loss) before income taxes and minority interests	**16,846**	10,321	6,125	1,198	(3,540)	2,927	5,552	2,690
Net income (loss)	**12,131**	8,996	1,719	(2,195)	(3,384)	(247)	2,069	254
Per-share data:								
Per share of common stock:								
Net income (loss)	**46.31**	34.38	6.57	(8.37)	(12.72)	(0.93)	7.75	0.95
Cash dividends applicable to the year	**7.50**	6.00	3.00	3.00	6.00	6.00	6.00	6.00
At year-end:								
Total assets	**186,521**	174,766	166,005	165,838	177,148	187,923	196,289	203,788
Shareholders' equity	**99,501**	83,513	74,476	71,648	75,175	80,268	81,731	80,664
Number of employees	**2,523**	2,597	2,735	2,792	2,872	3,097	3,341	3,387

Contents

Management's Discussion & Analysis

Overview of Fiscal 2005

The Japanese economy staged a moderate recovery during the reporting period, ended December 2005, with corporate earnings improving, capital investment rising, and consumer spending holding firm.

In the chemical industry, the business environment remained generally as predicted up to mid-term, but a slump in market prices overseas in the second half of the year, combined with the high price of raw materials and fuels, exerted considerable pressure on corporate earnings.

Amid these circumstances, the management of the Toagosei Group pushed ahead with measures dictated by the basic strategies spelled out in its new three-year business plan commenced from fiscal 2005, i.e. speeding up the development and expansion of priority businesses, and restructuring existing businesses. Specifically, we started operations of our newly-constructed production facilities in China for UV-curable resins, and sold off our agrochemicals business. We also took vigorous steps to pass on increases in raw material and fuel costs to our customers, and to cut back on fixed expenses.

As a result of our efforts, net sales on a consolidated basis for the reporting period rose by ¥7,160 million, or 5.0%, to ¥151,443 million (US$1,284 million).

Thanks to increased marketing efforts and rationalization initiatives, as well as a recovery in the market prices of commodity products, operating income posted a year-on-year growth of ¥2,625 million, or 20.8%, to ¥15,236 million (US$129 million). Net income rose ¥3,135 million, or 34.9%, to ¥12,131 million (US$102 million).

Sales by Segment

Commodity Chemicals

The Group enjoyed brisk shipments of caustic soda and high-purity inorganic chemical products, and we were able to pass on to our customers some of the prices increases in raw materials and fuel. Thanks to these factors, sales posted strong growth over the previous term.

Shipment volumes of inorganic chlorides remained low as a result of a falloff in demand for ferric chloride from major manufacturers, and total sales thus declined slightly from the previous year.

Demand for organic chlorinated solvents was slack in both the Japanese and overseas markets, with the resultant low shipment volume leading to a slight year-on-year fall in sales.

Shipments of sulfuric acid held firm, with sales posting a year-on-year gain.

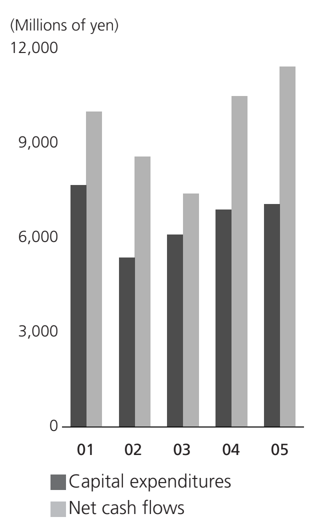
Sales of industrial gases recorded a slight year-on-year growth, thanks to steady shipments.

As a result of the above, total sales for the commodity chemicals segment came to ¥47,892 million, up ¥1,621 million, or 3.5%, over the previous term.

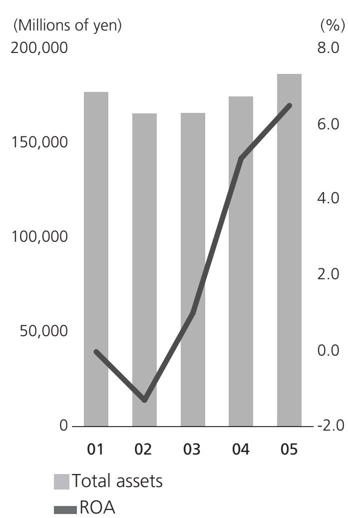
Acrylic Products

Market prices of acrylic acid and acrylic esters staged a recovery on both the domestic and overseas markets during the year. Moreover, thanks to our success in persuading customers to accept price increases to partially compensate for the increased costs of raw materials and fuel borne by the Group, we were able to record a substantial year-on-year increase in sales.

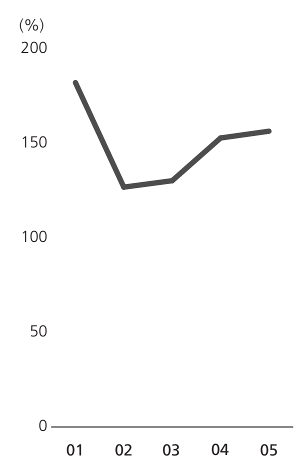
Capital expenditures & net cash flows



Total assets & ROA



Current ratio



We undertook aggressive marketing initiatives in the field of acrylic polymers, including the launching of new products. However, we were obliged to halt production of certain unprofitable products, and other factors were unable to compensate for the resultant decline in sales. Total sales therefore registered a slight year-on-year decline.

In the field of products for the construction and civil engineering sectors, solid shipments were seen in building repair products such as Aron Wall, a water-repellent coating material for concrete walls. This good performance, however, was insufficient to offset the decline in sales of other products. Total sales of this category were consequently down by a small margin from the previous year.

Shipments of polymer flocculants were firm to customers in Japan, and thanks to improved profitability following sales price hikes on certain products, total sales of this product category posted a marked increase over the previous year.

As a result, total sales of the acrylic products segment registered a year-on-year growth of ¥3,184 million, or 7.6%, to ¥45,111 million.

Specialty Chemicals

Vigorous sales promotion campaigns for our new consumer-use adhesives launched last year proved effective, with shipment volumes following a firm trend in line with our projections. As a result, sales were up slightly over the previous term. In industrial adhesives, favorable shipments were recorded for UV-curable and hot-melt-type products, thanks to which sales were up somewhat over the previous term.

The acrylate oligomer Aronix recorded favorable shipments due to the expansion of its use by makers of displays, and sales rose sharply year-on-year.

Regarding in-house-developed products, shipments of inorganic ion-exchangers were adversely affected by inventory adjustments by the electronic materials industry, and sales posted a year-on-year decrease.

As a result of the foregoing, total sales of the specialty chemicals segment rose ¥1,705 million year-on-year, or 8.3%, to ¥22,351 million.

Plastics

Shipments of piping materials were firm, and as we achieved partial success in raising product prices to reflect higher raw material and fuel costs, sales posted a slight rise over the previous year.

Among general consumer-use products, shipments of nursing care products were favorable, with total sales of this category posting year-on-year growth.

Shipments of raw material compounds for the production of molded plastics suffered from weak demand from makers of food containers, and sales were down slightly from the previous year.

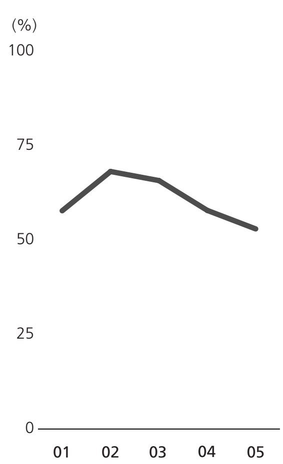
As a result, total sales of the plastics segment came to ¥31,655 million, a year-on-year increase of ¥999 million, or 3.3%.

Other Businesses

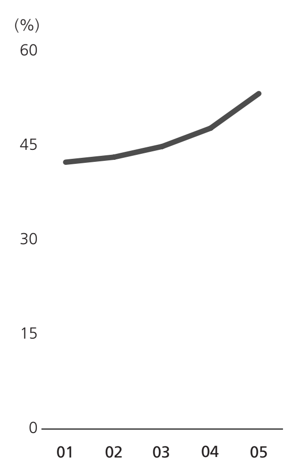
Revenue from facility construction and repair work declined by a small margin from the previous year, while revenue from transportation services also registered a year-on-year decrease.

As a result, total sales of the other businesses segment came to ¥4,433 million, for a year-on-year decline of ¥351 million, or 7.3%.

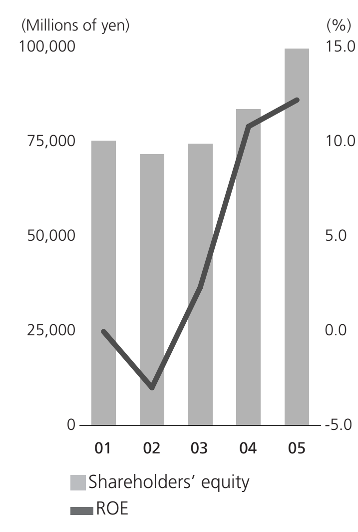
Ratio of property, plant & equipment to long-term capital



Ratio of shareholders' equity to total assets



Shareholders' equity & ROE



Cash Flows

In spite of an increase in inventory assets, net cash provided by operating activities posted a year-on-year increase of ¥3,468 million, to ¥18,380 million (US$155 million), mainly due to higher income before income taxes and minority interests.

Net cash used in investing activities declined by ¥2,580 million year-on-year, to ¥6,889 million (US$58 million), owing to a decrease in expenditure for the acquisition of investment securities.

Net cash used in financing activities increased by ¥8,394 million to ¥10,711 million (US$90 million), as a result of a decline in proceeds from the issuance of commercial paper.

As a result of the foregoing, the balance of cash and cash equivalents at the reporting term-end stood at ¥11,440 million (US$97 million), an increase of ¥940 million over the previous term-end.

Business Performance Prospects for Fiscal 2006

Extrapolating from the business performance for fiscal 2005, described above, we estimate sales at ¥154,000 million and net income at ¥7,600 million for fiscal 2006, both on a consolidated basis.

Cash Flow Prospects for Fiscal 2006

Net cash provided by operating activities is projected at ¥15,000 million, as a result of a decline in income before income taxes and minority interests.

Net cash used in investing activities is projected at ¥11,000 million, as a result of increased expenditures for the acquisition of property, plant and equipment.

Net cash used in financing activities is projected at ¥4,000 million, as a result of the Group's efforts to reduce interest-bearing debt.

Material risks to which we are exposed

(1) Cost competition

In the case of many product categories, there is considerable difficulty for the Group in creating products that differ substantially in nature and/or performance from those of our competitors. As a consequence, there is the possibility that we may become embroiled in fierce price competition, and, despite vigorous efforts to revitalize our marketing activities and lower production costs, we may find our product prices undercut by rival manufacturers. In such situations, the Group may not able to maintain its market share in the face of the severe competition, leading to negative impacts on the business performance and financial position of the Toagosei Group.

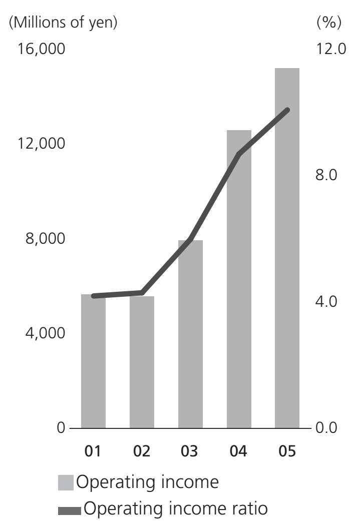
(2) Changes in the price of crude oil and naphtha

The average price of the principal raw materials purchased by the Toagosei Group is strongly and directly affected by changes in the market prices of crude oil and naphtha. In certain cases, the Group may be unable to fully pass on to its customers the increased cost of production of its products resulting from such rises in the prices of the said raw materials, and such situations will naturally exert an adverse impact on the Group's business performance and financial position.

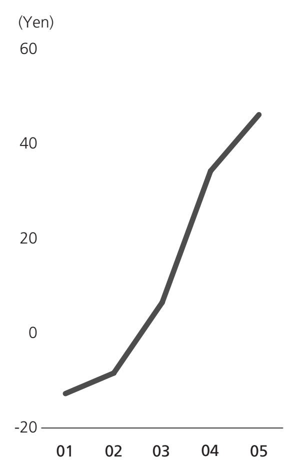
(3) Product liability

In spite of all our efforts to ensure a high level of product quality, there is always the possibility that, as a result of unforeseeable events or factors, a customer or a third party may suffer harm of some kind caused by the use of a product manufactured and sold by the Group. There is, further, the possibility that the resulting financial compensation for which the Group may be liable will exceed the amount covered by the product liability insurance plans into which it pays. In such cases, the

Operating income & ratio as a percentage of net sales



Net income (loss) per share



resulting additional extraordinary expenditure would have an adverse impact on the Group's business performance and financial position.

(4) Earthquakes and other natural disasters

The production plants of the Toagosei Group are located mostly in the Tokai Region of Japan, and in the event of the occurrence of a major earthquake in that region, which is, historically, prone to major earthquakes, the Group is liable to suffer damage including, but not limited to, the forced temporary suspension of production operations. Such an eventuality would, of course, have a significant adverse impact on the Group's business performance and financial position. The possibility cannot be ruled out that these plants may also suffer damage from typhoons or tsunamis.

(5) Major litigation

Although there are no lawsuits currently pending or in process, the possibility cannot be dismissed that Group may become involved in important litigation in the future as a result of its business activities: such lawsuits could result in an adverse impact on the Group's business performance and/or financial position.

(6) Deferred tax assets

Deferred tax assets are recorded in the amount deemed realizable, based on the Group's estimate of future taxable income. In the event of a substantial difference being recognized between the estimate and the actual figure, unrealized deferred tax assets may have a negative effect on the Group's business results and financial position.

(7) Changes in foreign currency exchange rates

For the reporting period, overseas sales by the Group accounted for 14.5% of total sales. Moreover, the Group includes five overseas consolidated subsidiaries, and one overseas affiliate accounted for by the equity method. For these reasons, major changes in foreign exchange rates would have a significant effect upon the Group's business performance and financial position.

(8) Changes in interest rates

The Toagosei Group is working earnestly to reduce its interest-bearing debt burden so as to improve its financial balance, but increases in interest expenses would have an adverse effect on the Group's business performance and financial position.

(9) Application of impairment accounting to fixed assets

With effect from the business term under review, the Toagosei Group has adopted the accounting standards for the impairment of its fixed assets. As a result, future significant changes in current market prices of landholdings, or significant changes in the Group's operating environment that lead to declines in the value of production-related assets, would have a greater adverse effect than hitherto upon the Group's business performance and financial position.

Estimates or projections included in this report are based on facts known to the Company's management as of the time of writing, and actual results may therefore differ substantially from such statements.

Consolidated Balance Sheets

Toagosei Co., Ltd. and Consolidated Subsidiaries

December 31	Millions of yen		Thousands of U.S. dollars (Note 3)
	2005	2004	**2005**
Assets			
Current assets:			
Cash and cash equivalents	**¥ 11,440**	¥ 10,500	**$ 96,896**
Securities (Notes 4 and 8)	**—**	141	**—**
Notes and accounts receivable	**47,926**	45,926	**405,913**
Inventories (Note 5)	**14,377**	12,718	**121,768**
Short-term loans receivable	**8,993**	9,152	**76,174**
Deferred tax assets (Note 10)	**601**	564	**5,093**
Other current assets	**1,563**	1,346	**13,240**
Allowance for doubtful receivables	**(3,378)**	(4,105)	**(28,614)**
Total current assets	**81,524**	76,244	**690,473**
Property, plant and equipment (Note 8):	**244,189**	244,588	**2,068,175**
Accumulated depreciation	**(172,895)**	(172,287)	**(1,464,346)**
Property, plant and equipment, net (Note 6)	**71,294**	72,301	**603,829**
Investments and other assets:			
Investment securities (Notes 4 and 8)	**28,283**	18,746	**239,545**
Long-term loans receivable	**280**	381	**2,377**
Intangible assets, net	**1,004**	1,209	**8,508**
Deferred tax assets (Note 10)	**314**	1,651	**2,663**
Other assets	**3,929**	4,363	**33,281**
Allowance for doubtful receivables	**(109)**	(131)	**(925)**
Total investments and other assets	**33,703**	26,220	**285,452**
Total	**¥186,521**	¥174,766	**$1,579,755**

See accompanying notes to consolidated financial statements.

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2005	2004	2005
Liabilities and shareholders' equity			
Current liabilities:			
Notes and accounts payable	¥ 19,854	¥ 18,897	$ 168,157
Short-term bank loans (Note 8)	3,930	3,930	33,285
Current portion of long-term debt (Note 8)	6,892	1,916	58,373
Commercial paper	9,000	15,000	76,225
Deferred tax liabilities (Note 10)	0	0	6
Accrued income taxes	3,264	1,489	27,651
Reserve for losses from guarantees granted to the obligations of others	1,085	1,021	9,195
Other current liabilities	8,071	7,618	68,359
Total current liabilities	52,098	49,874	441,254
Long-term liabilities:			
Long-term debt (Note 8)	16,340	23,567	138,393
Deferred tax liabilities (Note 10)	2,658	1,104	22,518
Accrued retirement benefits for employees (Note 9)	1,842	2,373	15,606
Accrued retirement benefits for directors	309	328	2,624
Other long-term liabilities	3,460	4,287	29,307
Total long-term liabilities	24,611	31,660	208,450
Minority interests in consolidated subsidiaries	10,309	9,718	87,315
Shareholders' equity (Notes 11, 17 and 18):			
Common stock, without par value:			
Authorized – 480,000,000 shares			
Issued:			
2005 – 263,992,598 shares	20,886	—	176,898
2004 – 263,992,598 shares	—	20,886	—
Capital surplus	15,063	15,031	127,577
Retained earnings	54,644	44,363	462,816
Unrealized holding gain on securities	9,697	4,326	82,134
Translation adjustments	(239)	(608)	(2,032)
Less treasury stock, at cost: 2,628,376 shares in 2005 and 2,787,166 shares in 2004	(550)	(486)	(4,660)
	99,501	83,513	842,734
Commitments and contingencies (Note 15)			
Total	¥186,521	¥174,766	$1,579,755

Consolidated Statements of Income

Toagosei Co., Ltd. and Consolidated Subsidiaries

Years ended December 31

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2005	2004	2005
Net sales	¥151,443	¥144,283	$1,282,657
Cost of sales	105,645	102,022	894,766
Gross profit	45,798	42,260	387,890
Selling, general and administrative expenses (Notes 10 and 12)	30,561	29,649	258,844
Operating income	15,236	12,611	129,046
Other income (expenses):			
Interest and dividend income	491	304	4,164
Interest expense	(384)	(521)	(3,252)
Gain on sales and disposal of property, plant and equipment	415	—	3,520
Equity in earnings of affiliates	439	59	3,719
Amortization of net retirement benefit obligation at transition	—	(88)	—
Provision of reserve for losses from guarantees granted to the obligations of others	(63)	(1,021)	(541)
Other, net	711	(1,021)	6,025
Income before income taxes and minority interests	16,846	10,321	142,682
Income taxes (Note 10):			
Current	4,952	3,324	41,941
Reversal of the prior year's income taxes	—	(260)	—
Deferred	(914)	(2,737)	(7,742)
	4,037	326	34,199
Minority interests in earnings of consolidated subsidiaries	(677)	(998)	(5,733)
Net income (Note 17)	¥ 12,131	¥ 8,996	$ 102,750

See accompanying notes to consolidated financial statements.

Consolidated Statements of Shareholders' Equity

Toagosei Co., Ltd. and Consolidated Subsidiaries

Years ended December 31

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2005	2004	2005
Common stock			
Balance at beginning of the year	¥20,886	¥20,886	$176,898
Balance at end of the year	¥20,886	¥20,886	$176,898
Capital surplus			
Balance at beginning of the year	¥15,031	¥15,014	$127,312
Gain on disposal of treasury stock	31	17	265
Balance at end of the year	¥15,063	¥15,031	$127,577
Retained earnings			
Balance at beginning of the year	¥44,363	¥36,804	$375,738
Cash dividends paid	(1,829)	(1,436)	(15,491)
Bonuses to directors	(21)	—	(181)
Net income	12,131	8,996	102,750
Balance at end of the year	¥54,644	¥44,363	$462,816
Net unrealized holding gain on securities			
Balance at beginning of the year	¥ 4,326	¥ 3,078	$ 36,647
Net change during the year	5,370	1,248	45,487
Balance at end of the year	¥ 9,697	¥ 4,326	$ 82,134
Translation adjustments			
Balance at beginning of the year	¥ (608)	¥ (865)	$ (5,155)
Net change during the year	368	256	3,122
Balance at end of the year	¥ (239)	¥ (608)	$ (2,032)
Treasury stock			
Balance at beginning of the year	¥ (486)	¥ (442)	$ (4,119)
Acquisition during the year, net of sales	(63)	(43)	(540)
Balance at end of the year	¥ (550)	¥ (486)	$ (4,660)

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

Toagosei Co., Ltd. and Consolidated Subsidiaries

Years ended December 31

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2005	2004	2005
Operating activities			
Income before income taxes and minority interests	¥16,846	¥10,321	$142,682
Depreciation and amortization	7,516	7,942	63,664
Impairment loss of property, plant and equipment	8	—	75
Decrease in provision for doubtful receivables	(749)	(66)	(6,348)
Increase in provision of reserve for losses from guarantees granted to the obligations of others	63	1,021	541
Reversal of provision for retirement benefits	(530)	(613)	(4,493)
Increase (decrease) in other provisions	(8)	10	(71)
Interest and dividend income	(491)	(304)	(4,164)
Interest expense	384	521	3,252
Foreign currency exchange loss (gain)	(186)	224	(1,582)
Equity in earnings of affiliates	(439)	(59)	(3,719)
Gain on sales of property, plant and equipment	(415)	—	(3,520)
Gain on sales of investments in securities	(14)	(146)	(119)
Loss on disposal of property, plant and equipment	998	758	8,458
Unrealized loss on securities	—	194	—
Losses related to an accident	—	366	—
Out-of-court settlement of accident claim	(200)	—	(1,693)
Receivables	(1,714)	(2,390)	(14,518)
Inventories	(1,525)	(405)	(12,920)
Payables	755	292	6,396
Director's bonuses	(24)	—	(206)
Other	1,259	1,499	10,667
	21,533	19,169	182,379
Interest and dividend received	491	307	4,166
Interest paid	(389)	(572)	(3,301)
Income taxes paid	(3,428)	(3,653)	(29,033)
Settlement package received for accident	200	—	1,693
Cost related to accident restoration paid	(27)	(338)	(228)
Net cash provided by operating activities	18,380	14,912	155,675
Investing activities			
Deposits of time deposits	(28)	—	(241)
Proceeds from sales of marketable securities	140	59	1,185
Purchases of investments in securities	(63)	(1,744)	(537)
Proceeds from sales of investments in securities	33	290	285
Purchases of property, plant and equipment	(7,333)	(7,460)	(62,109)
Proceeds from sales of property, plant and equipment	438	52	3,712
Increase (decrease) in short-term loans	406	(424)	3,443
Long-term loans made	(118)	(15)	(1,007)
Collection of long-term loans	5	8	42
Other, net	(368)	(234)	(3,124)
Net cash used in investing activities	(6,889)	(9,469)	(58,349)
Financing activities			
Decrease in short-term bank loans	—	(1,750)	—
Increase (decrease) in commercial paper	(6,000)	7,000	(50,817)
Proceeds from long-term loans	—	6,254	—
Repayment of long-term loans	(2,545)	(2,060)	(21,555)
Redemption of bonds	—	(10,000)	—
Repayment of lease obligation	(154)	(152)	(1,304)
Purchases of treasury stock	(150)	(81)	(1,278)
Proceeds from sales of treasury stock	118	55	1,003
Cash dividends to shareholders	(1,979)	(1,581)	(16,769)
Net cash used in financing activities	(10,711)	(2,316)	(90,722)
Effect of exchange rate changes on cash and cash equivalents	160	(33)	1,361
Net increase in cash and cash equivalents	940	3,092	7,965
Cash and cash equivalents at beginning of the year	10,500	7,407	88,932
Cash and cash equivalents at end of the year	¥11,440	¥10,500	$ 96,898

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Toagosei Co., Ltd. and Consolidated Subsidiaries
December 31, 2005

1. Basis of Preparation

Toagosei Co., Ltd. ("the Company") and its domestic subsidiaries maintain their books of account in conformity with the financial accounting standards of Japan, and its foreign subsidiaries maintain their books of account in conformity with those of the countries of their domicile.

The accompanying consolidated financial statements have been prepared on the basis of accounting principles generally accepted in Japan, which are different in certain respects as to the application and disclosure requirements of International Financial Reporting Standards, and have been compiled from the consolidated financial statements prepared by the Company as required by the Securities and Exchange Law of Japan.

As permitted by the Securities and Exchange Law of Japan, amounts of less than one million yen have been omitted. Consequently, the totals shown in the accompanying consolidated financial statements (both in yen and U.S. dollars) do not necessarily agree with the sum of the individual amounts.

Certain amounts in the prior year's financial statements have been reclassified to conform to the current year's presentation.

2. Summary of Significant Accounting Policies

(a) Principles of consolidation and accounting for investments in unconsolidated subsidiaries and affiliates

The accompanying consolidated financial statements include the accounts of the Company and any significant companies controlled directly or indirectly by the Company. Significant companies over which the Company exercises significant influence in terms of their operating and financial policies have been included in the consolidated financial statements on an equity basis. All significant intercompany balances and transactions have been eliminated in consolidation.

Investments in subsidiaries and affiliates which are not consolidated or accounted for by the equity method are carried at cost or less. Where there has been a permanent decline in the value of such investments, the Company has written down the investments.

The difference at the dates of acquisition between the cost and the underlying net equity of investments in consolidated subsidiaries and companies accounted for by the equity method is being amortized by the straight-line method over a period of five years.

(b) Foreign currency translation

Revenue and expense accounts of foreign consolidated subsidiaries are translated at the rate of exchange in effect at the balance sheet date, and, except for the components of shareholders' equity, the balance sheet accounts are also translated into yen at the same exchange rate. The components of shareholders' equity are translated at the historical exchange rates.

(c) Cash equivalents

All highly liquid investments with a maturity of three months or less when purchased are considered cash equivalents.

(d) Securities and investment securities

Securities other than those of subsidiaries and affiliates are classified into three categories: trading, held-to-maturity or other securities. Trading securities are carried at fair value and held-to-maturity securities are carried at amortized cost. Marketable securities classified as other securities are carried at fair value determined based on the average of the quoted prices (or the equivalent) in the one-month period prior to the balance sheet date with changes in unrealized holding gain or loss, net of the applicable income taxes, included directly in shareholders' equity. Non-marketable securities classified as other securities are carried at cost. Cost of securities sold is determined by the moving average method.

Contributions to the investment business limited liability partnerships and the similar partnerships are regarded as securities under the amended Securities and Exchange Law of Japan and practical guidance related to the accounting for financial instruments revised as of February 15, 2005, and accordingly, the contributions to the investment business limited liability partnerships and the similar partnerships are disclosed as investment securities rather than other assets as of December 31, 2005. The contributions to the investment business limited liability partnerships and the similar partnerships as reported as other assets as of December 31, 2004 was ¥343 million (US$2,095 thousand).

(e) Inventories

Inventories are stated at cost determined by the moving average method.

(f) Property, plant and equipment and depreciation

Depreciation of property, plant and equipment of the Company and its consolidated subsidiaries is calculated principally by the straight-line method based on the estimated useful lives of the respective assets and residual value except for certain consolidated subsidiaries for which depreciation is calculated by the declining-balance method based on the estimated useful lives of the respective assets and residual value.

Effective the year ended December 31, 2004, certain consolidated subsidiary has changed its depreciation method of property, plant and equipment from the declining-balance method to the straight-line method to be able to recover the capital investment within shorter period of time to improve the financial position but the effect of this change was immaterial.

(g) Accounting for impairment of property, plant and equipment

The Company and its consolidated subsidiaries have adopted and accounted for impairment of property, plant and equipment under the Statement of Opinion related to "Accounting for Impairment of Fixed Assets" issued by the Business Accounting Council on August 9, 2002 and related ASB Guidance No. 6 "Guidance for Accounting Standard for Impairment of Fixed Assets" issued by the Accounting Standard Board of Japan (ASB) on October 31, 2003 from the year ended March 31, 2005. Under the statement, tangible and intangible fixed assets be carried at cost less depreciation, and be reviewed for impairment whether events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The Company and consolidated subsidiaries would be required to recognize an impairment loss in the statement of income if certain indicators of assets impairment exist and the book value of an asset exceeds the undiscounted sum of future cash flows of the assets.

(h) Income taxes

Deferred tax assets and liabilities have been recognized in the consolidated financial statements determined with respect to the differences between financial reporting and the tax bases of assets and liabilities and were measured using the enacted tax rates and laws which will be in effect when the differences are expected to reverse.

(i) Research and development costs

Research and development costs are charged to income when incurred.

(j) Leases

Noncancelable lease transactions are primarily accounted for as operating leases (whether such leases are classified as operating or finance leases) except that lease agreements which stipulate the transfer of ownership of the leased assets to the lessee are accounted for as finance leases.

(k) Retirement benefits

Accrued retirement benefits for employees have been provided mainly at an amount calculated based on the retirement benefit obligation and the fair value of the pension plan assets as of the balance sheet date, as adjusted for the unrecognized net retirement benefit obligation at transition and unrecognized actuarial gain or loss. The retirement benefit obligation is attributed to each period by the straight-line method over the estimated years of service of the eligible employees. The net retirement benefit obligation at transition was fully charged to income since the year ended December 31, 2001, except for that of one consolidated subsidiary which is being amortized over a period of 4 years by the straight-line method. Actuarial gain and loss of the Company are amortized in the year following the year in which the gain or loss is recognized by the straight-line method over the average remaining years of service of the employees (14 to 15 years). Actuarial gain and loss of two consolidated subsidiaries are amortized by the straight-line method over a period (5 years and 10 years, respectively) which is shorter than the average remaining years of service of the employees.

In addition, directors and corporate auditors of the Company and certain consolidated subsidiaries are customarily entitled to lump-sum payments under the unfunded retirement benefits plans. The provision for retirement benefits for these officers has been made at estimated amounts.

On April 1, 2004, the Company changed its rules for tax-qualified pension plans and lump-sum payment plans. As a result, unrecognized prior year service cost to reduce the retirement benefit obligation incurred. The unrecognized prior year service cost is amortized by the straight-line method over a period (14 years) which is shorter than the average remaining years of service of the employees.

On April 1, 2005, a consolidated subsidiary changed its rules for tax-qualified pension plans and lump-sum payment plans. As a result unrecognized prior year service cost to reduce the retirement benefit obligation incurred. The unrecognized prior year service cost is amortized by the straight-line method over a period (5 years) which is shorter than the average remaining years of service of the employees.

(l) Reserve for losses from guarantees granted to the obligations of others

Reserve for losses from guarantees granted to the obligations of others is established based on the estimate for the possible losses arising from the performance of obligations as a guarantor taking into account the credit conditions of guarantees involved.

(m) Derivative financial instruments

The Company has entered into various derivative financial instruments in order to manage certain risks arising from adverse fluctuations in foreign currency exchange rates and interest rates. Derivative financial instruments are carried at fair value with any changes in unrealized gain or loss charged or credited to operations, except for those which meet the criteria for the special accounting treatment under which any differences paid or received on the interest rate swaps are recognized as adjustments to interest expense over the life of each swap, thereby adjusting the effective interest rate on the hedged items, which are the underlying borrowings. Receivables and payables hedged by qualified forward foreign exchange contracts are translated at the rates of the corresponding foreign exchange contacts.

(n) Appropriation of retained earnings

Under the Commercial Code of Japan, the appropriation of retained earnings with respect to a given financial year is made by the resolution of the shareholders at a general meeting held subsequent to the close of such financial year. The accounts for that year do not, therefore, reflect such appropriations. See Note 18.

3. U.S. Dollar Amounts

The translation of yen amounts into U.S. dollar amounts is made, at the rate of ¥118.07 = $1.00, the approximate exchange rate at December 31, 2005 and included solely for convenience. The translation should not be construed as a representation that yen have been, could have been, or could in the future be, converted into U.S. dollars at the above or any other rate.

4. Securities and Investment Securities

(a) At December 31, 2005 and 2004, information with respect to held-to-maturity securities for which market prices were available was summarized as follows:

	Millions of yen		
	December 31, 2005		
	Balance sheet amount	Market value	Unrecognized gain
Unrecognized gain items:			
Bonds:			
Corporate bonds	¥100	¥102	¥2
Total	¥100	¥102	¥2

	Thousands of U.S. dollars		
	December 31, 2005		
	Balance sheet amount	Market value	Unrecognized gain
Unrecognized gain items:			
Bonds:			
Corporate bonds	$846	$871	$24
Total	$846	$871	$24

	Millions of yen		
	December 31, 2004		
	Balance sheet amount	Market value	Unrecognized gain
Unrecognized gain items:			
Bonds:			
Corporate bonds	¥100	¥103	¥3
Total	¥100	¥103	¥3

(b) Information regarding marketable securities classified as other securities as of December 31, 2005 and 2004 is as follows:

	Millions of yen		
	December 31, 2005		
	Acquisition cost	Carrying value	Unrealized gain (loss)
Securities whose carrying value exceeds their acquisition cost:			
Stock	¥7,566	¥24,011	¥16,445
Bonds:			
Government bonds	—	—	—
Corporate bonds	—	—	—
Others	51	78	27
Subtotal	7,617	24,090	16,472
Securities whose acquisition cost exceeds their carrying value:			
Stock	12	11	(0)
Bonds:			
Government bonds	—	—	—
Subtotal	12	11	(0)
Total	¥7,629	¥24,102	¥16,472

	Thousands of U.S. dollars		
	December 31, 2005		
	Acquisition cost	Carrying value	Unrealized gain (loss)
Securities whose carrying value exceeds their acquisition cost:			
Stock	$64,083	$203,369	$139,285
Bonds:			
Government bonds	—	—	—
Corporate bonds	—	—	—
Others	432	664	231
Subtotal	64,516	204,033	139,516
Securities whose acquisition cost exceeds their carrying value:			
Stock	105	100	(5)
Bonds:			
Government bonds	—	—	—
Subtotal	105	100	(5)
Total	$64,622	$204,133	$139,511

	Millions of yen		
	December 31, 2004		
	Acquisition cost	Carrying value	Unrealized gain (loss)
Securities whose carrying value exceeds their acquisition cost:			
Stock	¥7,149	¥14,486	¥7,337
Bonds:			
Government bonds	19	19	0
Corporate bonds	100	101	1
Others	51	71	20
Subtotal	7,320	14,679	7,358
Securities whose acquisition cost exceeds their carrying value:			
Stock	278	261	(17)
Bonds:			
Government bonds	20	20	(0)
Corporate bonds	—	—	—
Subtotal	298	281	(17)
Total	¥7,619	¥14,960	¥7,341

(c) Sales of securities classified as other securities amounted to ¥33 million (US$285 thousand) with gain of ¥14 million (US$119 thousand) for the year ended December 31, 2005.

(d) Other securities without market value as of December 31, 2005 and 2004 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Investments in subsidiaries and affiliates:			
Unconsolidated subsidiaries	¥2,291	¥2,204	$19,410
Other securities:			
Unlisted securities	1,193	1,322	10,108
Other	598	302	5,065

(e) The redemption schedule for securities with maturity dates classified as other securities is summarized as follows:

	Millions of yen		
	December 31, 2004		
	Due in one year or less	Due after one year through five years	Due after five years through ten years
Government bonds	¥ 40	¥—	¥—
Corporate bonds	100	—	—
Total	¥140	¥—	¥—

5. Inventories

Inventories at December 31, 2005 and 2004 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Merchandise and finished products	¥ 9,343	¥ 8,492	$ 79,133
Semi-finished goods	720	574	6,101
Work in process	461	449	3,911
Raw materials and supplies	3,851	3,201	32,622
	¥14,377	¥12,718	$121,768

6. Property, Plant and Equipment

Property, plant and equipment at December 31, 2005 and 2004 are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Land	¥18,381	¥18,197	$155,682
Buildings and structures	23,683	25,005	200,590
Machinery, equipment and other	26,336	26,382	223,055
Construction in progress	2,892	2,714	24,500
	¥71,294	¥72,301	$603,829

7. Impairment Loss of Property, Plant and Equipment

The Company and its consolidated subsidiaries have recognized impairment loss on the following class of assets for the year ended December 31, 2005

Major use	Category	Location
Idle	Building and structures	Fukuchiyama city, Hiroshima

The Company and its consolidated subsidiaries have identified an idle asset as one group, for the purpose of accounting for impairment of property, plant and equipment on an individual basis.

When there is no specific plan for future use and the book value of such idle asset is less than the recoverable amount, the book value of each idle asset is written down to the recoverable amount. The idle assets listed in the above table were written down to the recoverable amount and ¥8 million (US$75 thousand) of impairment loss was recognized in the statement of income for the year ended March 31, 2006 and was reported as other expenses. The impairment loss was measured based on the net sales price of the idle assets as a basis of the recoverable amount. The net sales price was determined based on the valuation of the assets in question using the valuation techniques of a real estate.

8. Short-Term Bank Loans and Long-Term Debt

Short-term bank loans, principally unsecured, were notes payable to banks bearing annual interest at 0.6% at December 31, 2005 and 2004.

Long-term debt at December 31, 2005 and 2004 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
1.35% yen bonds due 2006	¥ 5,000	¥ 5,000	$ 42,347
Loans with collateral from banks, insurance companies and others, bearing annual interest rates of 2.75% and 1.01% for the current portion of long-term debt and the long-term debt other than current portion at December 31, 2005, respectively	18,232	20,483	154,418
	23,232	25,483	196,766
Less: current portion	(6,892)	(1,916)	(58,373)
	¥16,340	¥23,567	$138,393

Assets pledged as collateral for short-term bank loans and long-term debt at December 31, 2005 and 2004 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Property, plant and equipment, at net book value	¥26,009	¥28,162	$220,291
Marketable securities and investments securities	6,845	4,993	57,977
	¥32,855	¥33,156	$278,269

The aggregate annual maturities of long-term debt subsequent to December 31, 2005 are summarized as follows:

For the year ending December 31,	Millions of yen	Thousands of U.S. dollars
2006	¥ 6,892	$ 58,373
2007	9,582	81,155
2008	3,643	30,855
2009	1,772	15,011
2010	272	2,307
2011 and thereafter	1,070	9,064
	¥23,232	$196,766

9. Retirement Benefit Plans

The Company and its domestic consolidated subsidiaries have defined benefit plans, tax-qualified pension plans and lump-sum payment plans, covering substantially all employees who are entitled to lump-sum or annuity payments, the amounts of which are determined by reference to their basic rates of pay, length of service, and the conditions under which termination occurs.

The following table sets forth the funded and accrued status of the plans, and the amounts recognized in the consolidated balance sheets as of December 31, 2005 and 2004 related to the Company's and the consolidated subsidiaries' defined benefit plans:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Retirement benefit obligation	¥(18,018)	¥(17,842)	$(152,604)
Plan assets at fair value	17,079	13,448	144,659
Unfunded retirement benefit obligation	(938)	(4,393)	(7,945)
Unrecognized actuarial gain or loss	(623)	2,303	(5,281)
Unrecognized prior service cost	(280)	(283)	(2,379)
Accrued retirement benefits	¥ (1,842)	¥ (2,373)	$ (15,606)

The components of retirement benefit expenses for the years ended December 31, 2005 and 2004 are outlined as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Service cost	¥ 799	¥ 790	$ 6,768
Interest cost	336	391	2,851
Expected return on plan assets	(120)	(120)	(1,024)
Amortization of net retirement benefit obligation at transition	—	88	—
Amortization of actuarial gain or loss	236	241	2,002
Amortization of unrecognized prior service cost	(24)	(16)	(209)
Total	¥1,226	¥1,375	$10,388

The assumptions used in accounting for the above plans were as follows:

	December 31,	
	2005	2004
Discount rates	Mainly 2.0%	Mainly 2.0%
Expected return on plan assets	Mainly 0.75%	Mainly 1.5%

10. Income Taxes

The Company and its domestic consolidated subsidiaries are subject to a number of taxes based on earnings, i.e. corporation tax, inhabitants' taxes and enterprise tax, which, in the aggregate, resulted in statutory tax rate of approximately 40.5 per cent and 41.9 per cent for 2005 and 2004, respectively.

The effective tax rate reflected in the consolidated statement of income for the year ended December 31, 2005 differs from the statutory tax rate for the following reasons:

	2005	2004
Statutory tax rate	40.5%	41.9%
Effect of:		
Permanent difference – entertainment expense	1.1	1.7
Permanent difference – dividend income	(0.4)	(0.3)
Inhabitants' taxes per capita	0.4	0.8
Amortization of excess of cost over net assets acquired	(1.5)	(2.5)
Equity in losses of affiliates	(1.1)	(0.2)
Valuation allowance	4.3	7.8
Different tax rates applied to income of foreign consolidated subsidiaries	(2.2)	(7.5)
Loss on investment in consolidated subsidiaries	(14.7)	—
Cessation of equity method on certain investment	—	(33.1)
Other, net	(2.4)	(5.4)
Effective tax rate	24.0%	3.2%

Significant components of the deferred tax assets and liabilities held by the Company and its consolidated subsidiaries as of December 31, 2005 and 2004 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Deferred tax assets:			
Valuation loss on securities	¥ 4,439	¥ 2,608	$ 37,596
Elimination of unrealized profit	1,413	1,304	11,971
Accrued retirement benefit	2,645	2,858	22,408
Accrued enterprise tax	297	177	2,517
Allowance for doubtful receivables	1,991	1,674	16,870
Reserve for losses on guaranteed liabilities	440	414	3,727
Accrued bonuses	79	73	671
Net operating loss carryforwards	1,272	2,800	10,780
Others	499	456	4,233
	13,079	12,367	110,778
Valuation allowance	(4,270)	(4,458)	(36,169)
Total deferred tax assets	8,809	7,909	74,608
Deferred tax liabilities:			
Reserve under Special Taxation Measures Law	(2,426)	(2,406)	(20,549)
Undistributed earnings of overseas partnerships	(591)	(554)	(5,010)
Gain on contribution of securities to retirement benefit trust	(847)	(854)	(7,180)
Valuation difference on other securities	(6,681)	(2,981)	(56,593)
Other	(4)	(0)	(41)
Total deferred tax liabilities	(10,552)	(6,798)	(89,375)
Net deferred tax assets	¥ 1,743	¥ 1,111	$ 14,766

Local tax law of Japan has revised in March 2003 and new taxation system under which a component of enterprise tax is charged based on other than income (such as amount of value-added and paid-up capital) from the year ending on and after April 1, 2004 and the Company and its domestic consolidated subsidiaries have adopted the practical guideline No. 12 related to the presentation of enterprise tax charged on the basis of other than income in the statement of income issued by the Accounting Standard Board of Japan (ASB) and accordingly, enterprise tax related to the value-added and paid up capital was reported under the selling, general and administrative expenses. As a result, the selling, general and administrative expenses for the year ended December 31, 2005 has increased by ¥239 million (US$2,028 thousand) as compared with the that of the previous year and operating income and income before income taxes and minority interest for the year ended December 31, 2005 have decreased by the same amount, respectively.

11. Capital Surplus and Retained Earnings

In accordance with the commercial Code of Japan ("The Code"), the Company has provided a legal reserve, which was included in retained earnings. The Code provides that an amount equal to at least 10% of the amount to be disbursed as a distribution of earnings be appropriated to the legal reserve until the total of such reserve and the capital surplus account equals 25% of the common stock account. The legal reserve amounted to ¥3,990 million (US$33,793 thousand) and ¥3,990 million as of December 31, 2005 and 2004, respectively.

12. Research and Development Costs

Research and development costs included in selling, general and administrative expenses and manufacturing costs for the year ended December 31, 2005 and 2004 were ¥5,275 million (US$44,678 thousand) and ¥5,032 million, respectively.

13. Leases

The following pro forma amounts represent the acquisition cost, accumulated depreciation and net book value of leased property as of December 31, 2005 and 2004, which would have been reflected in the consolidated balance sheets if finance lease accounting had been applied to the finance lease transactions currently accounted for as operating leases:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	**2005**
Acquisition cost:			
Machinery and equipment ...	**¥1,177**	¥1,543	**$9,969**
	¥1,177	¥1,543	**$9,969**
Accumulated depreciation:			
Machinery and equipment ...	**¥ 832**	¥1,109	**$7,054**
	¥ 832	¥1,109	**$7,054**
Net book value:			
Machinery and equipment ...	**¥ 344**	¥ 433	**$2,915**
	¥ 344	¥ 433	**$2,915**

Lease payments relating to finance lease transactions accounted for as operating leases amounted to ¥244 million (US$2,067 thousand) and ¥317 million, which were equal to the depreciation expense of the leased assets computed by the straight-line method over the respective lease terms for the years ended December 31, 2005 and 2004, respectively.

Future minimum lease payments (including the interest portion thereon) subsequent to December 31, 2005 for noncancelable operating leases and finance lease transactions accounted for as operating leases are summarized as follows:

	Millions of yen		Thousands of U.S. dollars	
Year ending December 31,	Operating leases	Finance leases	Operating leases	Finance leases
2006	¥ 88	¥147	$ 750	$1,246
2007 and thereafter	413	196	3,503	1,668
Total	¥502	¥344	$4,253	$2,915

14. Derivative Transactions

The Company utilizes derivative financial instruments for the purpose of hedging its exposure to adverse fluctuations in foreign currency exchange rates and interest rates, but does not enter into such transactions for speculation or trading purposes.

The Company is exposed to credit loss in the event of nonperformance by the counterparties to the derivative financial instruments, but any such loss would not be material because the Company enters into transactions only with financial institutions with high credit ratings. The notional amounts of the derivative financial instruments do not necessarily represent the amounts exchanged by the parties and, therefore, are not a direct measure of the Company's risk exposure in connection with derivative financial instruments. The disclosure of fair value information for derivatives as of December 31, 2005 and 2004 has been omitted since all derivatives have been accounted for as hedges.

15. Commitments and Contingencies

At December 31, 2005, the Company and consolidated subsidiaries had the following contingent liabilities:

	Millions of yen	Thousands of U.S. dollars
Guarantees of indebtedness	¥1,885	$15,973
	¥1,885	$15,973

16. Segment Information

The Company and its consolidated subsidiaries are primarily engaged in the manufacture and sale of products in the chemical industry segment in Japan. As net sales, operating income and total assets from the chemical business of the Company and its consolidated subsidiaries constituted more than 90% of the consolidated totals for both years ended December 31, 2005 and 2004, the disclosure of business segment information has been omitted.

Geographical Segments

Geographical segment information of the Company and its consolidated subsidiaries for the years ended December 31, 2005 and 2004 is summarized as follows:

	Millions of yen				
Year ended December 31, 2005	Japan	Other countries	Total	Eliminations or corporate	Consolidated
Sales:					
Sales to third parties...	¥137,499	¥13,944	¥151,443	¥ —	¥151,443
Intersegment sales	2,371	3,303	5,674	(5,674)	—
Total sales.................	139,870	17,248	157,118	(5,674)	151,443
Operating costs and expenses..................	127,167	14,504	141,671	(5,465)	136,206
Operating income......	¥ 12,702	¥ 2,743	¥ 15,446	¥ (209)	¥ 15,236
Assets........................	¥178,892	¥10,709	¥189,601	¥(3,080)	¥186,521

	Thousands of U.S. dollars				
Year ended December 31, 2005	Japan	Other countries	Total	Eliminations or corporate	Consolidated
Sales:					
Sales to third parties...	$1,164,555	$118,102	$1,282,657	$ —	$1,282,657
Intersegment sales...	20,082	27,982	48,064	(48,064)	—
Total sales.................	1,184,637	146,084	1,330,722	(48,064)	1,282,657
Operating costs and expenses..................	1,077,051	122,846	1,199,898	(46,287)	1,153,611
Operating income......	$ 107,585	$ 23,238	$ 130,823	$ (1,777)	$ 129,046
Assets........................	$1,515,139	$ 90,701	$1,605,841	$(26,086)	$1,579,755

	Millions of yen				
Year ended December 31, 2004	Japan	Other countries	Total	Eliminations or corporate	Consolidated
Sales:					
Sales to third parties...	¥132,163	¥12,120	¥144,283	¥ —	¥144,283
Intersegment sales...	1,227	2,031	3,259	(3,259)	—
Total sales.................	133,391	14,152	147,543	(3,259)	144,283
Operating costs and expenses..................	122,807	12,165	134,972	(3,300)	131,672
Operating income......	¥ 10,583	¥ 1,986	¥ 12,570	¥ 40	¥ 12,611
Assets........................	¥175,493	¥ 8,610	¥184,104	¥(9,337)	¥174,766

Overseas Sales

Overseas sales, which include export sales of the Company and its domestic consolidated subsidiaries and sales (other than exports to Japan) of its foreign consolidated subsidiaries, for the years ended December 31, 2005 and 2004 are summarized as follows:

	Millions of yen				
Year ended December 31, 2005	Asia	North America	Europe	Other	Total
Overseas sales	¥16,206	¥3,427	¥1,703	¥637	¥ 21,975
Consolidated net sales					151,443
Ratio of overseas sales to consolidated net sales	10.7%	2.3%	1.1%	0.4%	14.5%

	Thousands of U.S. dollars				
Year ended December 31, 2005	Asia	North America	Europe	Other	Total
Overseas sales	$137,258	$29,029	$14,432	$5,400	$ 186,120
Consolidated net sales					1,282,657
Ratio of overseas sales to consolidated net sales	10.7%	2.3%	1.1%	0.4%	14.5%

	Millions of yen				
Year ended December 31, 2004	Asia	North America	Europe	Other	Total
Overseas sales	¥14,126	¥2,856	¥1,378	¥633	¥ 18,994
Consolidated net sales					144,283
Ratio of overseas sales to consolidated net sales	9.8%	2.0%	1.0%	0.4%	13.2%

17. Amounts Per Share

The following table sets forth the net income, cash dividends and net assets per share of common stock for the years ended December 31, 2005 and 2004.

	Yen		U.S. dollars
Year ended December 31,	**2005**	2004	**2005**
Net income:			
Basic	**¥ 46.31**	¥ 34.38	**$0.39**
Diluted	**46.29**	34.38	**0.39**
Cash dividends	**7.50**	6.00	**0.06**
Net assets	**380.59**	319.66	**3.22**

Cash dividends per share represent the cash dividends proposed by the Board of Directors as applicable to the respective years together with the interim cash dividends paid.

18. Subsequent Event

Cash dividends

The following appropriations of retained earnings of the Company, which have not been reflected in the accompanying consolidated financial statements for the year ended December 31, 2005, were approved at a shareholders' meeting held on March 30, 2006:

	Millions of yen	Thousands of U.S. dollars
Cash dividends – ¥4.00 ($0.033) per share	¥1,045	$8,854

Basic Agreements to Integrate Polymer Flocculant Operations

On February 8, 2006, the Company and Mitsui Chemicals AquaPolymer, Inc. (MAP) signed a letter of undertaking to integrate the polymer flocculant businesses of the Company with the business of MAP by October 1, 2006. The polymer flocculant business of the Company will be spun off, based on the contract to be signed as of June 30, 2006, and the shares to be issued by MAP will be allocated to the Company.

Report of Independent Auditors

The Board of Directors
Toagosei Co., Ltd.

We have audited the accompanying consolidated balance sheets of Toagosei Co., Ltd. and consolidated subsidiaries as of December 31, 2005 and 2004, and the related consolidated statements of income, shareholders' equity, and cash flows for the years then ended, all expressed in yen. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Japan. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Toagosei Co., Ltd. and consolidated subsidiaries at December 31, 2005 and 2004, and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in Japan.

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended December 31, 2005 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 3.

Ernst & Young ShinNihon

March 30, 2006

Corporate Data

Organization (As of April 1, 2006)

- General Meeting of Shareholders
  - Board of Directors
    - Chairman
    - President
      - Internal Control Section
      - Corporate Management
        - Corporate Strategy Department
          - Planning Group
          - Secretariat Group
          - China Representative Office
          - Coagulant Business Integration Team
        - Corporate Research and Development Department
          - Life Science Group
          - Electronics Group
          - Corporate Research Laboratory
          - Intellectual Property Group
          - Nagoya Research Institute
          - New Product Development Laboratory
          - Innovative Research Group
          - HOG Project
        - Administrative Department
          - Personnel & General Affairs Group
          - Investor Relations & Public Relations Section
          - Finance Group
          - Information System Group
        - Supply Chain Management Department
          - Purchasing Group
          - Logistics Group
          - Sales Administrative Group
          - SCM Center
          - Satellite Marketing Group
        - Technology Administrative Department
          - Technology Administrative Group
          - Environment & Safety Group
          - Quality Assurance Group
          - Productive Technology Laboratory
      - Operations Management
        - Commodity Chemicals Department
          - Chlorine & Alkali Products Group
          - Sulfuric Acid & Agricultural Chemicals Group
          - Specialty Inorganic Products Group
          - Commodity Chemicals Group
        - Acrylic Products Department
          - Acrylic Products Group
          - Construction Products Group
          - Macromolecular Material Research Laboratory
          - Kawasaki Plant
        - Adhesives Department
          - Adhesives Group
          - Adhesives Laboratory
        - Functional Materials Department
          - UV-curable Resins Group
          - Functional Materials Group
          - Functional Materials Research Laboratory
        - Tokyo Sales Department
          - Commodity Chemicals Group
          - Acrylic Products Group
          - Functional Materials Group
          - Adhesives Group
          - Sapporo Sales Office
        - Osaka Branch
          - General Affairs Group
          - Commodity Chemicals Group
          - Acrylics & Functional Materials Group
          - Adhesives Group
          - Shikoku Sales Office
          - Fukuoka Sales Office
        - Nagoya Branch
          - General Affairs Group
          - Commodity Chemicals Group
          - Acrylics, Functional Materials & Adhesives Group
          - Hokuriku Sales Office
        - Nagoya Plant
          - Administrative Department
          - Manufacturing Department I
          - Manufacturing Department II
        - Tokushima Plant
          - Administrative Department
          - Manufacturing Department
          - Sakaide Plant
        - Takaoka Plant
          - Administrative Department
          - Manufacturing Department
          - Productive Technology Group

Directory

Domestic Network

Head Office
1-14-1 Nishi-Shimbashi, Minato-ku, Tokyo
105- 8419
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Tsukuba Research Laboratory
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Tel: 029-865-2600 Fax: 029-865-2610

Principal Overseas Subsidiaries

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Kong City 33 Canton road, Tsimshatsui,
Kowloon, Hong Kong
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Toagosei America Inc.
1450 West Main St., West Jefferson, Ohio
43162, U.S.A.
Tel: 614-718-3855 Fax: 614-718-3866

Toagosei Singapore Pte Ltd
1 Robinson Road, #21-02 AIA Tower
Singapore 048542
Tel: 65-64385411 Fax: 65-64385422

Principal Subsidiaries and Affiliates (As of December 31, 2005)

Name of Company	Lines of Business	Our Share (%)	Capital (¥ in millions)
Tsurumi Soda Co., Ltd.	Manufacture & sale of chemical products	100.0	¥2,080
Aron Kasei Co., Ltd.	Manufacture & sale of synthetic resin molded products	61.1	¥4,220
Toagosei Asia Pte Ltd	Sale of chemical products	100.0	S$62,713,000
Aron Ever-Grip Ltd.	Manufacture & sale of adhesives	100.0	£223,000
Oita Chemical Co., Ltd.	Manufacture of chemical products	90.0	¥450
Toagosei America Inc.	Manufacture & sale of chemical products; technological research	100.0	US$6,100,000
Nihon Junyaku Co., Ltd.	Manufacture & sale of chemical products	99.0	¥351
TG Corporation	Sale of chemical products	100.0	¥174
Toa Logistics Co., Ltd.	Product distribution	100.0	¥16
TOA Engineering Co., Ltd.	Construction & repair of chemical facilities	100.0	¥50
Toa Techno-Gas Co., Ltd.	Manufacture & sale of industrial gases	100.0	¥400
Toa Estate Co., Ltd.	Real estate sales agency and real estate management	100.0	¥30
Toa-Jet Chemical Co., Ltd.	Manufacture & sale of chemical products	51.0	NT$15,000,000
Toa Kogyo Co., Ltd.	Product distribution	100.0	¥25
Taiwan Toagosei Co., Ltd.	Sale of chemical products	70.0	NT$5,000,000
Aron Packaging Co., Ltd.	Filling and packaging of adhesives	100.0	¥10
Toagosei Singapore Pte Ltd	Manufacture & sale of chemical products	100.0	S$60,571,000
Hokuriku Toa Logistics Co., Ltd.	Product distribution	90.0	¥10
Shikoku Toa Logistics Co., Ltd.	Product distribution	70.0	¥10
TG Support Co.	Outsourced provision of clerical work for other Group members	100.0	¥10
Chubu Ekisan Co., Ltd.(Note)	Manufacture & sale of industrial gases	30.0	¥480
Elmer’s & Toagosei Co.	Sale of adhesives	50.0	US$32,786,000

Note Equity-method affiliates

Investor Information

Established

March 1942

Common Stock

Authorized: 480,000,000 shares

Issued: 263,992,598 shares

Capital: ¥20,886 million

Number of shareholders: 28,306

Listings: Common stock listed on the exchanges in Tokyo, Osaka, Nagoya and Fukuoka

Transfer Agent for Common Stock

The Chuo Mitsui Trust and Banking Co., Ltd.
3-33-1, Shiba, Minato-ku, Tokyo 105-8574

Certified Accountants

Shin Nihon & Co.
Hibiya Kokusai Bldg., 2-2-3, Uchisaiwai-cho
Chiyoda-ku, Tokyo 100-0011

Major Shareholders

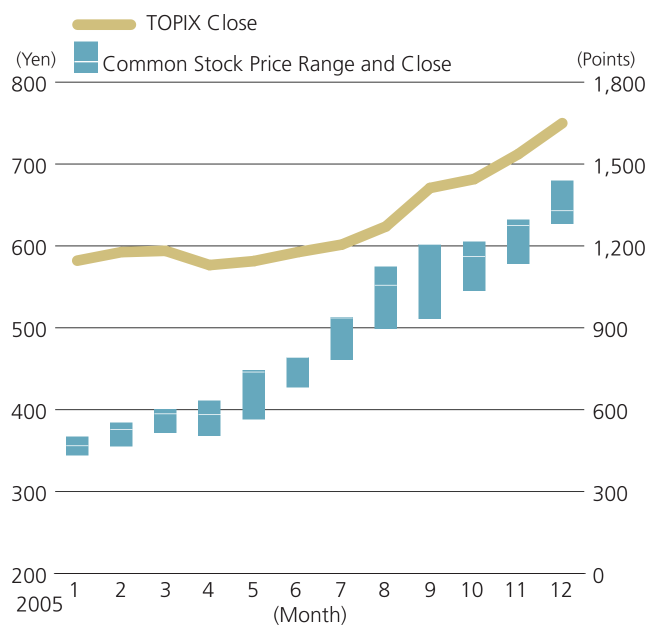
	(%)
The Master Trust Bank of Japan, Ltd. (Trust account)	5.71
Japan Trustee Services Bank, Ltd. (Trust account)	5.05
Sumitomo Mitsui Banking Corp.	4.40
The Bank of Tokyo-Mitsubishi UFJ, Ltd.	4.27
Employee Shareholders' Committee	2.25
Business Partner Shareholders' Committee	2.14
Aioi Insurance Co., Ltd.	2.09
Tokio Marine & Nichido Fire Insurance Co., Ltd.	2.00
Mitsui Life Insurance Co. Ltd.	1.76
The Norinchukin Bank	1.49

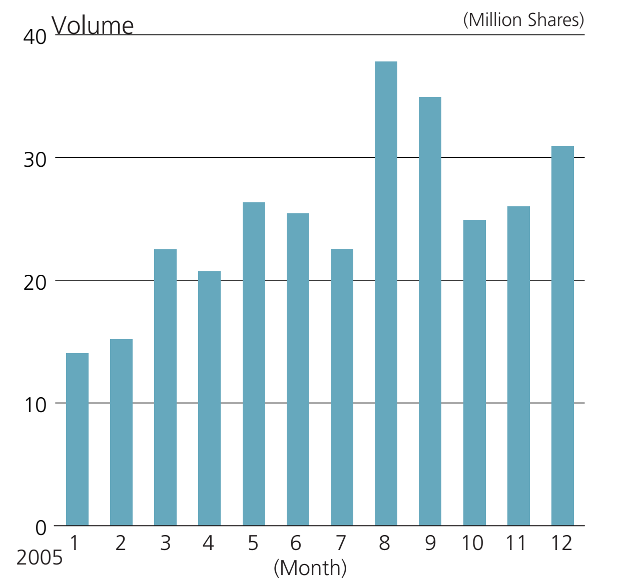
(As of December 31, 2005)

Stock Price Range & Trading Volume

(Tokyo Stock Exchange)

	2001	2002	2003	2004	2005
High	¥253	¥210	¥231	¥365	¥680
Low	¥160	¥121	¥133	¥197	¥344
TOPIX Close (Year-end)	1,032	843	1,043	1,149	1,649





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