Financial Section

Consolidated Six-Year Summary

Kuraray Co., Ltd. and Consolidated Subsidiaries

Years ended March 31	Millions of yen						Thousands of U.S. dollars
	1997	1996	1995	1994	1993	1992	**1997**
For period:							
Net sales	**¥340,112**	¥330,869	¥327,270	¥326,781	¥353,187	¥355,717	**$2,742,839**
Cost of sales	**255,240**	246,768	249,399	251,863	272,594	271,601	**2,058,387**
Selling, general and administrative expenses	**58,324**	58,008	56,370	55,141	59,419	57,162	**470,355**
Operating income	**26,548**	26,093	21,501	19,777	21,174	26,954	**214,097**
Net income	**11,741**	11,049	9,617	8,157	9,444	11,526	**94,685**
Net income per share (Exact yen or U.S. dollar)							
Primary	**34.99**	35.43	30.94	26.30	30.55	39.89	**0.28**
Fully diluted	**32.48**	32.71	—	—	—	—	**0.26**
Cash dividends per share (Exact yen or U.S. dollar)	**9.00**	9.00	8.50	8.00	8.00	8.00	**0.07**
Capital expenditures	**19,049**	17,479	10,645	15,626	16,287	23,949	**153,621**
Depreciation and amortization	**14,111**	14,263	15,087	15,443	16,225	15,838	**113,798**
Total research and development expenses	**13,592**	12,646	12,549	13,200	14,869	14,524	**109,613**
At period end:							
Total assets	**¥514,167**	¥535,173	¥477,874	¥477,690	¥437,754	¥428,545	**$4,146,508**
Total shareholders' equity	**208,635**	178,776	164,931	157,251	150,003	143,127	**1,682,540**

Note: The United States dollar amounts represent translation of Japanese yen at the rate of ¥124=$1.
Fully diluted net income per share is required to be disclosed effective from fiscal year ended March 31, 1996.

Contents

Results of Operations

In the fiscal year ended March 31, 1997, consolidated net sales of Kuraray Co., Ltd. and its subsidiaries totaled ¥340,112 million (US$2,742.8 million), a 2.8% increase over the previous year.

The ratio of gross profit to net sales decreased 0.4 percentage point from the previous year to 25.0%. Selling, general and administrative expenses totaled ¥58,324 million (US$470.4 million), a 0.5% increase over the previous year. The ratio of selling, general and administrative expenses to net sales was 17.1%.

The net financial revenue and expenditure was ¥3,274 million (US$26.4 million), a ¥77 million (US$0.6 million) increase over the previous year. This increase was attributable to our efforts to improve our overall financial condition.

As a result, income before income taxes totaled ¥26,205 million (US$211.3 million), a 5.7% increase over the previous year. Net income for the term amounted to ¥11,741 million (US$94.7 million), a 6.3% increase over the previous year.

As a result of an increase in the total number of shares outstanding, primary net income per share decreased ¥0.44 from the previous year to ¥34.99 (US$0.28).

Financial Position

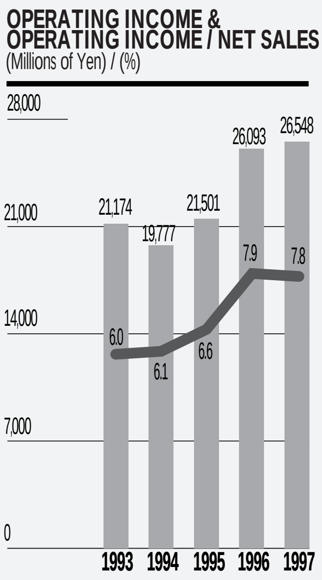
Total assets at the end of March 1997 stood at ¥514,167 million (US$4,146.5 million), a 3.9% decrease from the previous year.

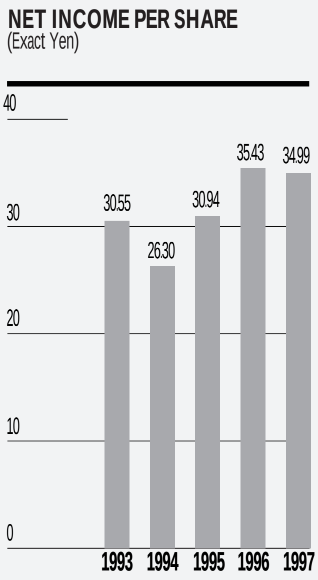
Current assets decreased by 19.2% to ¥223,543 million (US$1,802.8 million) mainly because marketable securities declined by ¥46,770 million (US$377.2 million).

Capital expenditures during the year reached to ¥19,049 million (US$153.6 million), a 9.0% increase over the previous year. Depreciation and amortization expenses totaled ¥14,111 million (US$113.8 million), a 1.1% decrease from the previous year.

Investments and other assets increased by 17.2% to ¥193,297 million (US$1,558.8 million).

Current liabilities decreased by 4.5% to ¥186,925





million (US$1,507.5 million). Long-term liabilities decreased by 25.3% to ¥118,262 million (US$953.7 million) mainly due to a drop in long-term debt.

Shareholders' equity increased by ¥29,859 million (US$240.8 million) over the previous year, to ¥208,635 million(US$1,682.5 million), mainly as a result of a substantial increase in retained earnings and issue of stock upon exercise of warrants.

The ratio of net worth to total assets was 40.6%, a 7.2% increase over the previous year.

With regard to financing activities, Kuraray issued ¥12,500 million (US$100.8 million) worth of bonds from January to March 1997, mainly for loans to its subsidiaries.

Cash Flows

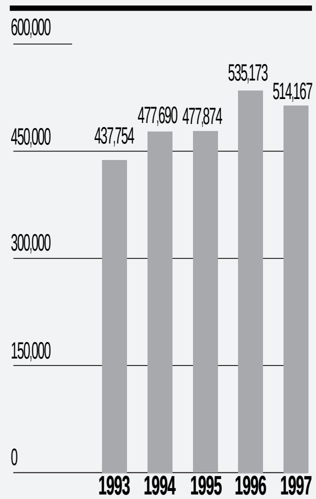
Net cash provided by operating activities was a little more than the amount provided during the previous year.

Net cash used in investing activities totaled ¥1,245 million (US$10.0 million), substantially lower than the amount used during the previous year. This was mainly attributable to a decrease of ¥49,885 million (US$402.3 million) in marketable securities, compared with the previous year's ¥7,502 million decrease, and a decrease of ¥1,131 million (US$9.1 million) in loans receivable, compared with the previous year's ¥6,031 million decrease.

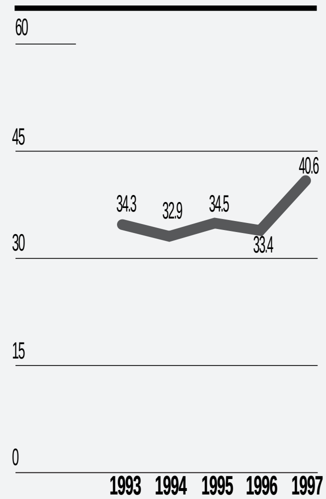
Net cash used in financing activities totaled ¥18,893 million (US$152.4 million), compared with ¥23,164 million provided by financing activities during the previous year. The difference was mainly attributable to higher repayments of long-term debt, which amounted to ¥50,264 million (US$405.4 million), compared with the previous year's ¥14,190 million, and to a decline in proceeds from long-term debt, which amounted to ¥16,640 million (US$134.2 million), compared with the previous year's ¥28,602 million.

As a result, cash and cash equivalents at the end of the year amounted to ¥29,585 million (US$238.6 million), up ¥7,523 million (US$60.7 million), or 34.1%, from the previous fiscal year-end.

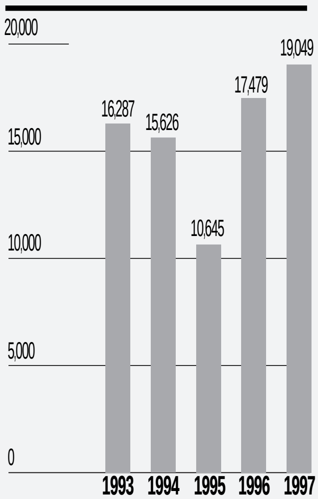
TOTAL ASSETS
(Millions of Yen)



EQUITY RATIO
(%)



CAPITAL EXPENDITURES
(Millions of Yen)



Consolidated Balance Sheets

Kuraray Co., Ltd. and Consolidated Subsidiaries

March 31, 1997 and 1996	Millions of yen 1997	Millions of yen 1996	Thousands of U.S. dollars (Note 1) 1997
ASSETS			
Current assets:			
Cash and cash equivalents	**¥ 29,585**	¥ 22,062	**$ 238,589**
Marketable securities (Note 3)	**28,778**	75,548	**232,081**
Notes and accounts receivable (Note 9):			
Trade	**95,059**	103,327	**766,605**
Unconsolidated subsidiaries and affiliates	**5,986**	7,318	**48,274**
Other	**3,369**	3,809	**27,169**
Allowance for doubtful accounts	**(1,865)**	(1,655)	**(15,040)**
	102,549	112,799	**827,008**
Inventories (Note 4)	**61,265**	64,538	**494,073**
Other current assets	**1,366**	1,839	**11,015**
Total current assets	**223,543**	276,786	**1,802,766**
Property, plant and equipment (Note 5):			
Land	**17,291**	17,808	**139,444**
Buildings	**79,245**	76,852	**639,073**
Machinery and equipment	**299,567**	284,014	**2,415,862**
Construction in progress	**4,138**	7,609	**33,371**
	400,241	386,283	**3,227,750**
Less accumulated depreciation	**(302,914)**	(292,825)	**(2,442,855)**
	97,327	93,458	**784,895**
Investments and other assets:			
Investment securities (Notes 3 and 5)	**116,876**	89,950	**942,548**
Investments in and advances to unconsolidated subsidiaries and affiliates	**12,473**	13,303	**100,589**
Other	**63,948**	61,676	**515,710**
	193,297	164,929	**1,558,847**
	¥514,167	¥535,173	**$4,146,508**

See Notes to consolidated financial statements.

	Millions of yen		Thousands of U.S. dollars (Note 1)
	1997	1996	**1997**
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities:			
Short-term bank loans (Note 5)	**¥ 28,100**	¥ 31,825	**$ 226,613**
Current portion of long-term debt (Note 5)	**55,632**	50,615	**448,645**
Notes and accounts payable:			
Trade	**56,415**	62,288	**454,960**
Unconsolidated subsidiaries and affiliates	**1,614**	1,469	**13,016**
Other	**5,581**	6,414	**45,008**
Accrued income taxes (Note 7)	**7,979**	8,279	**64,347**
Accrued expenses and other	**31,604**	34,904	**254,871**
Total current liabilities	**186,925**	195,794	**1,507,460**
Long-term liabilities:			
Long-term debt (Note 5)	**93,996**	133,874	**758,032**
Accrued retirement benefits (Note 8)	**11,841**	12,107	**95,492**
Other	**12,425**	12,295	**100,202**
Total long-term liabilities	**118,262**	158,276	**953,726**
Minority interests	**345**	2,327	**2,782**
Commitments and contingencies (Note 9)			
Shareholders' equity (Note 6)**:**			
Common stock with par value of ¥50 ($0.40) per share:			
Authorized — 700,000,000 shares			
Issued and outstanding —			
340,207,727 shares at March 31, 1997	**66,131**		**533,315**
317,120,272 shares at March 31, 1996		55,158	
Additional paid-in capital	**60,369**	49,396	**486,847**
Legal reserve	**5,064**	4,762	**40,838**
Retained earnings	**77,074**	69,471	**621,565**
	208,638	178,787	**1,682,565**
Treasury stock at cost	**(3)**	(11)	**(25)**
Total shareholders' equity	**208,635**	178,776	**1,682,540**
	¥514,167	¥535,173	**$4,146,508**

Consolidated Statements of Income

Kuraray Co., Ltd. and Consolidated Subsidiaries

Years ended March 31, 1997 and 1996	Millions of yen 1997	Millions of yen 1996	Thousands of U.S. dollars (Note 1) 1997
Net sales	**¥340,112**	¥330,869	**$2,742,839**
Cost of sales	**255,240**	246,768	**2,058,387**
(Gross profit)	**84,872**	84,101	**684,452**
Selling, general and administrative expenses	**58,324**	58,008	**470,355**
(Operating income)	**26,548**	26,093	**214,097**
Other income (expenses):			
Interest and dividend income	**7,313**	8,310	**58,976**
Interest expenses	**(4,039)**	(5,113)	**(32,573)**
Other, net	**(3,617)**	(4,500)	**(29,170)**
(Income before income taxes)	**26,205**	24,790	**211,330**
Income taxes (Note 7)	**14,442**	13,405	**116,468**
Minority interests in net income of consolidated subsidiaries	**(22)**	(336)	**(177)**
Net income	**¥ 11,741**	¥ 11,049	**$ 94,685**
	Yen		U.S. dollars (Note 1)
Net income per share:			
Primary	**¥34.99**	¥35.43	**$0.28**
Fully diluted	**32.48**	32.71	**0.26**

See Notes to consolidated financial statements.

Consolidated Statements of Shareholders' Equity

Kuraray Co., Ltd. and Consolidated Subsidiaries

Years ended March 31, 1997 and 1996	Common stock	Additional paid-in capital	Legal reserve	Retained earnings
	(Millions of yen)			
Balance at March 31, 1995	¥ 52,354	¥ 46,592	¥ 4,476	¥ 61,511
Net income				11,049
Stock issued on exercise of warrants	2,804	2,804		
Cash dividends ¥9.00 per share				(2,801)
Transfer to legal reserve			286	(286)
Bonuses to directors and statutory auditors				(89)
Foreign currency translation adjustment				87
Balance at March 31, 1996	55,158	49,396	4,762	69,471
Net income				**11,741**
Conversion of convertible debentures	**226**	**226**		
Stock issued on exercise of warrants	**10,747**	**10,747**		
Cash dividends ¥9.00 per share				**(2,958)**
Transfer to legal reserve			**302**	**(302)**
Bonuses to directors and statutory auditors				**(80)**
Effect of changes in reporting entity				**(798)**
Balance at March 31, 1997	**¥ 66,131**	**¥ 60,369**	**¥ 5,064**	**¥ 77,074**
	(Thousands of U.S. dollars) (Note 1)			
Balance at March 31, 1996	$444,823	$398,355	$38,403	$560,250
Net income				**94,685**
Conversion of convertible debentures	**1,823**	**1,823**		
Stock issued on exercise of warrants	**86,669**	**86,669**		
Cash dividends $0.07 per share				**(23,855)**
Transfer to legal reserve			**2,435**	**(2,435)**
Bonuses to directors and statutory auditors				**(645)**
Effect of changes in reporting entity				**(6,435)**
Balance at March 31, 1997	**$533,315**	**$486,847**	**$40,838**	**$621,565**

See Notes to consolidated financial statements.

Consolidated Statements of Cash Flows

Kuraray Co., Ltd. and Consolidated Subsidiaries

Years ended March 31, 1997 and 1996	Millions of yen 1997	Millions of yen 1996	Thousands of U.S. dollars (Note 1) 1997
Cash flows from operating activities			
Net income	**¥11,741**	¥11,049	**$ 94,685**
Adjustments to reconcile net income to net cash provided by operating activities –			
Depreciation and amortization	**14,111**	14,263	**113,798**
Provision for doubtful accounts, net	**210**	121	**1,694**
(Decrease) increase in accrued retirement benefits	**(266)**	873	**(2,145)**
Decrease (increase) in notes and accounts receivable	**9,793**	(12,790)	**78,975**
Decrease (increase) in inventories	**1,833**	(978)	**14,782**
(Decrease) increase in notes and accounts payable	**(6,250)**	9,316	**(50,403)**
(Decrease) increase in accrued income taxes	**(300)**	2,549	**(2,419)**
Other, net	**(3,211)**	3,150	**(25,895)**
Net cash provided by operating activities	**27,661**	27,553	**223,072**
Cash flows from investing activities			
Acquisitions of property, plant, and equipment	**(19,360)**	(16,719)	**(156,129)**
Decrease in marketable securities	**49,885**	7,502	**402,298**
Decrease in loans receivable	**1,131**	6,031	**9,121**
Increase in investments, mainly investment securities and long-term fixed deposits	**(32,999)**	(34,340)	**(266,120)**
Other, net	**98**	1,211	**790**
Net cash used in investing activities	**(1,245)**	(36,315)	**(10,040)**
Cash flows from financing activities			
(Decrease) increase in short-term bank loans	**(3,725)**	6,034	**(30,040)**
Proceeds from long-term debt	**16,640**	28,602	**134,194**
Repayments of long-term debt	**(50,264)**	(14,190)	**(405,355)**
Proceeds from exercise of warrants	**21,494**	5,608	**173,338**
Dividends paid	**(2,958)**	(2,801)	**(23,855)**
Other, net	**(80)**	(89)	**(645)**
Net cash (used in) provided by financing activities	**(18,893)**	23,164	**(152,363)**
Net increase in cash and cash equivalents	**7,523**	14,402	**60,669**
Cash and cash equivalents, beginning of period	**22,062**	7,660	**177,920**
Cash and cash equivalents, end of period	**¥29,585**	¥22,062	**$238,589**

See Notes to consolidated financial statements.

Years ended March 31, 1997 and 1996

1. Basis of presenting consolidated financial statements:

These consolidated financial statements are prepared in accordance with the provisions set forth in the Japanese Securities and Exchange Law and the related accounting regulations and in conformity with generally accepted accounting principles and practices in Japan.

In preparing these consolidated financial statements, certain reclassifications have been made to the consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan. In addition, certain notes included herein are not required under generally accepted accounting principles and practices in Japan but are presented as additional information.

The United States dollar amounts included herein are given solely for convenience and are stated, as a matter of arithmetical computation only, at the rate of ¥124=$1, the approximate exchange rate prevailing on March 31, 1997. The translations should not be construed as representations that the Japanese yen amounts have been, could have been or could in the future be, converted into United States dollars at that or any other rate.

2. Significant accounting policies:

(a) Principles of consolidation

These consolidated financial statements include the accounts of Kuraray Co., Ltd. (the 'Company') and its significant subsidiaries (the 'Companies'). During the year ended March 31, 1996, EVAL Company of America, a consolidated subsidiary, has changed its fiscal year end from December 31 to March 31. Accordingly its financial statements for the fifteen month period ended March 31, 1996 were included in the consolidated financial statements as of and for the year ended March 31,1996. Significant intercompany items are eliminated in consolidation.

During the year ended March 31, 1997, the accounts of Kuraray America, Inc. and one other company have been included in consolidation, because these companies were newly incorporated in the year ended March 31, 1997, and the accounts of Kuraray Europe GmbH and two other companies have been included in consolidation, because the effect of their operations on the results of consolidated operations has become material. On the other hand, the accounts of Japan Medico Co., Ltd. have been excluded from consolidation, because the Company has sold the stocks of Japan Medico Co., Ltd. Kuraray Finance Co., Ltd. has been merged into Kuraray Fudosan Co., Ltd., one of the consolidated subsidiaries.

In the case of a change in reporting entity, the consolidated financial statements are not restated, but the effect of the change to retained earnings at beginning of the period is directly credited to retained earnings during the period.

The difference between the cost of investments and equity in their net assets at dates of acquisition is being amortized over five years.

(b) Cash and cash equivalents

Cash and cash equivalents include all time deposits with original maturities of one year or less, which can be withdrawn at least at face amount at any time without penalty.

(c) Inventories

Inventories other than supplies are stated at cost principally determined by the weighted average method. Supplies are stated at cost principally determined by the moving average method.

(d) Property, plant and equipment

Property, plant and equipment are stated at cost.

Depreciation is principally computed by the declining-balance method over the estimated useful lives of the assets. Estimated useful lives of the assets are principally as follows:—

Buildings	35 to 65 years
Machinery and equipment	2 to 10 years

The Companies use machinery and facilities under financing leases without transferring ownership and such leased assets are not capitalized in the balance sheet in conformity with accounting principles generally accepted in Japan.

(e) Marketable securities and investment securities

Marketable securities and investment securities are principally stated at cost, determined by the moving average method, as determined by each particular security.

(f) Bond discounts

Bond discounts, which are included in investments and other assets on the consolidated balance sheets, are amortized by the straight-line method over the life of the bonds.

(g) Income taxes

Accrued income taxes are provided at the amount currently payable. Deferred income taxes on timing differences in recognizing certain income and expenses between reporting for tax and financial purposes are not provided, except pertaining to the timing differences of four foreign consolidated subsidiaries.

(h) Retirement benefits

The Companies principally have unfunded lump-sum benefit plans and funded contributory pension plans, generally covering all employees.

Under the terms of the Companies' retirement plans, substantially all employees are entitled to a lump-sum payment at the time of retirement. The amount of the retirement benefits is, in general, based on the length of service, basic salary at the time of retirement, and cause of retirement. The liability for lump-sum payments is principally stated at 68% based on the latest actuarial computation of the amount which would be required if all eligible employees voluntarily retired as of the balance sheet date.

The Companies' contributory pension plans, which cover those employees who retire at age 55 or more, or have served the Companies for more than 20 years and retire at age 50 or more, generally provide for pension payments for a period of ten years subsequent to retirement. The annual provision for these plans includes current period costs, amortization of prior service costs over 14 years and interest on the unfunded portion. The provision is determined actuarially and funded currently through outside trustees.

Directors and statutory auditors are entitled, subject to shareholders' approval, to lump-sum payments under the unfunded retirement plan. The accrued liabilities for their retirement benefits are, in general, based upon the amounts which would be required by the Companies' internal regulation.

(i) Foreign currency items
Foreign currency items are translated into Japanese yen at the rates in effect at the balance sheet date for current receivables and payables and at the rates when acquired or incurred for non-current receivables and payables. Income and expenses in foreign currency are translated into Japanese yen at exchange rates prevailing at the transaction dates.

Foreign currency items, which are covered by forward exchange contracts including currency swap contracts, are translated into Japanese yen at the contracted rates.

Resulting exchange differences are charged or credited to income as incurred, except for exchange differences resulting from the translation of non-current payables and receivables in foreign currency hedged by long-term forward exchange contracts including currency swap contracts which are deferred and amortized over the period until the year of maturity of the payables and receivables.

In preparing the consolidated financial statements, assets, liabilities, income and expenses of foreign subsidiaries are translated into Japanese yen at the rates in effect at the balance sheet date. Effective April 1, 1996, the Company adopted the amended "Accounting Standards for Foreign Currency Transactions, etc." which requires the current rate method in preparing the consolidated financial statements. As a result of this change, however, there was no effect on income before income taxes.

(j) Stock and bond issue expenses
Stock and bond issue expenses are charged to income when incurred.

(k) Research and development expenses
Expenses relating to research and development activities are charged to income when incurred.

(l) Net income per share
The computation of primary net income per share is based on the weighted average number of shares outstanding during each financial period. The computation of fully diluted net income per share is based on the weighted average number of shares outstanding after consideration of the effect of dilution of common stock equivalents.

(m) Allowance for doubtful accounts
An allowance for doubtful accounts, principally at management's estimate of probable bad debts, has in some years exceeded the maximum amount permitted to be charged to income under Japanese tax regulations. When these amounts are reversed into income, then, to that extent, they may be deducted from taxable income for that year.

3. Market value information for securities:
At March 31, 1997, book value and market value of marketable securities and investment securities, as to which market value information is available to obtain, were as follows:—

	Millions of yen		Thousands of U.S. dollars	
	Book Value	Market Value	Book Value	Market Value
Marketable securities				
Stocks	¥ 702	¥ 3,961	$ 5,661	$ 31,943
Bonds	7,040	7,123	56,774	57,444
Investment securities				
Stocks	24,347	49,753	196,347	401,234
Bonds	49,786	51,394	401,500	414,468
	¥81,875	¥112,231	$660,282	$905,089

During the year ended March 31, 1997, the Company has transferred stocks of ¥23,654 million ($190,758 thousand) from marketable securities to investment securities.

4. Inventories:
Inventories at March 31, 1997 and 1996 consisted of the following: —

	Millions of yen		Thousands of U.S. dollars
	1997	1996	**1997**
Finished products	**¥40,273**	¥43,080	**$324,783**
Semi-finished products and work in process	**13,176**	13,312	**106,258**
Raw materials and supplies	**7,816**	8,146	**63,032**
	¥61,265	¥64,538	**$494,073**

5. Short-term bank loans and long-term debt:

Short-term bank loans are generally represented by 365-day notes with interest rates principally of 0.90% p.a. and 1.03% p.a. at March 31, 1997 and 1996, respectively.

Long-term debt consisted of the following: —

	Millions of yen		Thousands of U.S. dollars
	1997	1996	**1997**
Loans principally from banks and insurance companies with interest rates ranging from 1.025% p.a. to 8.00% p.a. maturing serially until 2014:			
Secured	**¥ 564**	¥ 4,255	**$ 4,548**
Unsecured	**19,753**	21,543	**159,298**
3.3% yen convertible sinking fund debentures due 1997	**8,899**	8,899	**71,766**
1.8% yen convertible sinking fund debentures due 2003	**13,970**	13,970	**112,661**
1.0% yen convertible debentures due 2003	**9,551**	9,995	**77,024**
2.2% yen convertible debentures due 2002	**14,993**	15,000	**120,911**
2 1/4% United States dollar bonds due 1996 with detachable warrants	**—**	18,521	**—**
1 1/2% United States dollar bonds due 1998 with detachable warrants	**20,305**	20,305	**163,750**
4 1/2% United States dollar bonds due 1999 with detachable warrants	**8,546**	8,546	**68,919**
2 5/8% United States dollar bonds due 1999 with detachable warrants	**17,110**	17,110	**137,984**
2 3/4% Swiss franc notes due 1996 with detachable warrants	**—**	14,055	**—**
3 3/4% Swiss franc notes due 1996 with detachable warrants	**—**	8,853	**—**
3/4% Swiss franc notes due 1997 with detachable warrants	**23,437**	23,437	**189,008**
Floating to fixed rate yen Euro medium term notes due March 5, 2004	**3,000**	—	**24,194**
Floating to fixed rate yen Euro medium term notes due March 4, 2003	**3,000**	—	**24,194**
2.27% yen Euro medium term notes due January 30, 2004	**500**	—	**4,032**
2.02% yen Euro medium term notes due March 26, 2003	**1,000**	—	**8,065**
2.00% yen Euro medium term notes due February 7, 2003	**2,000**	—	**16,129**
Fixed and floating rate yen Euro medium term notes due March 27, 2002	**1,000**	—	**8,065**
Step-up rate yen Euro medium term notes due April 10, 2007	**500**	—	**4,032**
Floating rate yen Euro medium term notes due April 22, 2002	**500**	—	**4,032**
Floating rate yen Euro medium term notes due April 25, 2002	**1,000**	—	**8,065**
	149,628	184,489	**1,206,677**
Current portion	**(55,632)**	(50,615)	**(448,645)**
	¥ 93,996	¥133,874	**$ 758,032**

The 3.3% yen convertible sinking fund debentures due December 12, 1997, which were issued in Japan in December 1985, can be purchased at any time in their entirety at the option of the Company or may be redeemed, at prices declining from 106% to 100% of their principal amount from October 1, 1990 until 1997. The debentures are convertible into common stock of the Company until December 11, 1997 at the conversion price of ¥1,318.5 ($10.63) per share.

The 1.8% yen convertible sinking fund debentures due March 31, 2003, which were issued in Japan in November 1987, can be purchased at any time in their entirety at the option of the Company or may be redeemed, at prices declining from 106% to 100% of their principal amount from April 1, 1996 until 2003. The debentures are convertible into common stock of the Company until March 28, 2003 at the conversion price of ¥1,703.4 ($13.74) per share.

The 1.0% yen convertible debentures due March 31, 2003, which were issued in Japan in January 1994, can be purchased at any time in their entirety at the option of the Company or may be redeemed, at prices declining from 103% to 100% of their principal amount from April 1, 1999 until 2003. The debentures are convertible into common stock of the Company until March 28, 2003 at the conversion price of ¥1,067.3 ($8.61) per share.

The 2.2% yen convertible debentures due March 29, 2002, which were issued in Japan in February 1995, can be purchased at any time in their entirety at the option of the Company or may be redeemed, at prices declining from 102% to 100% of their principal amount from April 1, 1999 until 2002. The debentures are convertible into common stock of the Company until March 28, 2002 at the conversion price of ¥1,036.0 ($8.35) per share.

For the 3.3% and 1.8% yen convertible sinking fund debentures, the Company is required to contribute to a sinking fund, which amount is reduced by the amount of debentures converted or redeemed, ¥1,000 million ($8,065 thousand) on every September 30 for the 7 years ended September 30, 1997 and ¥1,500 million ($12,097 thousand) on every March 31 for the 6 years ending March 31, 2002, respectively. At March 31, 1997, investment securities with a net book value of ¥6,042 million ($48,726 thousand), of which market value approximates the amount of sinking fund requirements were deposited with a designated bank instead of the sinking fund payment.

The indentures under which the 1.8% yen convertible sinking fund debentures due 2003 were issued place a limitation on the payment of cash dividends, which relates, in part, to earnings of the Company. At March 31, 1997, the amount of retained earnings available for the payment of dividends was ¥82,651 million ($666,540 thousand) under such provision of the indentures.

The indentures under which the 1.0% yen convertible debentures due 2003 were issued place a limitation on the payment of cash dividends, which relates, in part, to earnings of the Company. At March 31, 1997, the amount of retained earnings available for the payment of dividends was ¥48,008 million ($387,161 thousand) under such provision of the indentures.

The indentures under which the 2.2% yen convertible debentures due 2002 were issued place a limitation on the payment of cash dividends, which relates, in part, to earnings of the Company. At March 31, 1997, the amount of retained earnings available for the payment of dividends was ¥48,608 million ($392,000 thousand) under such provision of the indentures.

The holders of warrants issued in conjunction with the 1 1/2% United States dollar bonds due January 27, 1998 have the right by way of exercise of warrants to subscribe for shares of common stock of the Company at ¥1,067.1 ($8.61) per share, which right is exercisable from February 14, 1994 to January 13, 1998. The amount of warrants remaining unexercised was ¥22,358 million ($180,306 thousand) at March 31, 1997.

The holders of warrants issued in conjunction with the 4 1/2% United States dollar bonds due February 9, 1999 have the right by way of exercise of warrants to subscribe for shares of common stock of the Company at ¥1,036.0 ($8.35) per share, which right is exercisable from February 27, 1995 to January 26, 1999. The amount of warrants remaining unexercised was ¥10,045 million ($81,008 thousand) at March 31, 1997.

The holders of warrants issued in conjunction with the 2 5/8% United States dollar bonds due December 21, 1999 have the right by way of exercise of warrants to subscribe for shares of common stock of the Company at ¥1,087.0 ($8.77) per share, which right is exercisable from January 8, 1996 to December 7, 1999. The amount of warrants remaining unexercised was ¥20,420 million ($164,677 thousand) at March 31, 1997.

The holders of warrants issued in conjunction with the 3/4% Swiss franc notes due May 13, 1997 have the right by way of exercise of warrants to subscribe for shares of common stock of the Company at ¥1,148.2 ($9.26) per share, which right is exercisable from May 24, 1993 to May 9, 1997. The amount of warrants remaining unexercised was ¥23,595 million ($190,282 thousand) at March 31, 1997.

The conversion prices of the above sinking fund debentures and debentures and the exercise prices of the above warrants are subject to adjustment under certain circumstances, including stock splits pursuant to the relevant agreements.

The number of shares of common stock required for conversion of the above sinking fund debentures and debentures outstanding at March 31, 1997 at the current conversion prices and for exercising of the above warrants remaining unexercised at March 31, 1997 at the current exercise prices would have been 108,355 thousand.

Bonds with warrants issued on and after April 1, 1994 are divided into value of warrants and value of bonds. The value of warrants are included in accrued expenses and other on the consolidated balance sheets.

The rates of floating to fixed rate yen Euro medium term notes due March 5, 2004, are as follows:—

January 20, 1997 ~ March 4, 1997
  Interpolated JPY LIBOR + 0.125%
March 5, 1997~ March 4, 2001
  6 month JPY LIBOR + 0.2%
March 5, 2001~ Due date
  3.70% per annum

The rates of floating to fixed rate yen Euro medium term notes due March 4, 2003, are as follows:—

January 23, 1997 ~ March 3, 1997
  Interpolated JPY LIBOR – 0.15%
March 4, 1997 ~ Due date
  2.00% per annum

The rates of fixed and floating rate yen Euro medium term notes due March 27, 2002, are as follows:—

February 10, 1997 ~ March 26, 1997
  1.00%
March 27, 1997 ~ March 26, 1998
  4.85% –10 YEAR JPY SWAP RATE (Not less than 0%)
March 27, 1998 ~ March 26, 1999
  4.85% –10 YEAR JPY SWAP RATE (Not less than 0%)
March 27, 1999 ~ March 26, 2000
  4.85% –7 YEAR JPY SWAP RATE (Not less than 0%)
March 27, 2000 ~ March 26, 2001
  4.85% –5 YEAR JPY SWAP RATE (Not less than 0%)
March 27, 2001 ~ Due date
  4.85% –3 YEAR JPY SWAP RATE (Not less than 0%)

The rates of step up rate yen Euro medium term notes due April 10, 2007, are as follows:—
February 25, 1997 ~ April 9, 2002
2.50% per annum
April 10, 2002 ~ Due date
3.00% per annum
The rates of floating rate yen Euro medium term notes due April 22, 2002, are as follows:—
March 10, 1997 ~ April 21, 1997
1 month JPY LIBOR + 0.40%
April 22, 1997 ~ Due date
6 month JPY LIBOR + 0.40%
The rates of floating rate yen Euro medium term notes due April 25, 2002, are as follows:—
March 13, 1997 ~ April 24, 1997
1 month JPY LIBOR + 0.41%
April 25, 1997 ~ Due date
6 month JPY LIBOR + 0.41%

The annual maturities of long-term debt outstanding at March 31, 1997 for the respective years ending March 31 were as follows:—

	Millions of yen	Thousands of U.S. dollars
1998	¥ 55,632	$ 448,645
1999	16,278	131,274
2000	19,907	160,540
2001	2,373	19,137
2002	17,327	139,734
Thereafter	38,111	307,347
	¥149,628	$1,206,677

At March 31, 1997, assets pledged as collateral for short-term bank loans and long-term debt were as follows:—

	Millions of yen	Thousands of U.S. dollars
Property, plant and equipment, net of accumulated depreciation	¥16,502	$133,081

6. Shareholders' equity:
The Japanese Commercial Code provides that a portion of retained earnings equal to at least 10% of cash distributions being paid out by means of appropriation for retained earnings with respect to each financial period be appropriated as a legal reserve until such reserve equals 25% of the common stock account.

This reserve is not available for dividends but may be capitalized by resolution of the Board of Directors or used to reduce a deficit by resolution of the shareholders.

Under the Code, at least 50% of the issue price of new shares, with a minimum of the par value thereof, is required to be accounted for as common stock. The remainder is accounted for as additional paid-in capital.

7. Income taxes:
The Companies are subject to several taxes based on income which, in the aggregate, resulted in a normal effective tax rate of approximately 51% for each of the two years in the period ended March 31, 1997.

The effective tax rates in the consolidated statements of income differ from the normal statutory tax rates due to such items as permanently non-deductible expenses and timing differences in recognizing certain income and expense items for financial and tax reporting purposes.

8. Retirement benefits:
The total charges to consolidated income for all retirement and pension plans for the years ended March 31, 1997 and 1996 amounted to ¥4,562 million ($36,790 thousand) and ¥5,724 million, respectively.

As a result of change in estimate of long-term interest rate to be used in actuarial computation of the liability for lump-sum payments, the Company made additional provision of ¥1,124 million in the year ended March 31, 1996.

The actuarial value of net assets under the Companies' contributory funded pension plans amounted to ¥11,442 million ($92,274 thousand) at the most recent valuation dates.

9. Commitments and contingencies:
As is customary in Japan, the Companies receive promissory notes from customers for future settlement of sales proceeds and obtain significant financing by discounting them with banks. The amounts of the discounted notes are not included in the balance sheet but are presented to be contingent liabilities. Notes discounted at banks with recourse at March 31, 1997 and 1996 amounted to ¥33 million ($266 thousand) and ¥1,791 million, respectively.

The Companies were contingently liable for guarantees, mainly for bank loans of unconsolidated subsidiaries, affiliates, and others, of ¥1,417 million ($11,427 thousand) and ¥1,557 million at March 31, 1997 and 1996, respectively.

10. Leases:
Payments and revenue of financing leases without transferring ownership of the leased assets to the lessee were ¥468 million ($3,774 thousand) and ¥37 million ($298 thousand) for the year ended March 31, 1997.

11. Segment Information:

The Companies operate principally within four business segments: chemical and synthetic fibers; chemical products; man-made leather, nonwoven fabrics and fastening materials; diversified businesses.

A summary of net sales and operating income and identifiable assets, capital expenditures and depreciation and amortization by segments of business activities for the year ended March 31, 1997 and 1996 are as follows: —

Net sales and Operating income

	Millions of yen				Thousands of U.S. dollars			
	Net sales to outside customers	Net sales to intersegment	Net sales	Operating income	Net sales to outside customers	Net sales to intersegment	Net sales	Operating income
Year ended March 31, 1997								
Chemical and synthetic fibers	¥112,937	¥ 873	¥113,810	¥ 3,790	$ 910,782	$ 7,040	$ 917,822	$ 30,565
Chemical products	146,812	1,739	148,551	14,884	1,183,968	14,024	1,197,992	120,032
Man-made leather, nonwoven fabrics and fastening materials	38,114	464	38,578	5,060	307,371	3,742	311,113	40,806
Diversified businesses	42,249	11,035	53,284	2,461	340,718	88,992	429,710	19,847
Total	340,112	14,111	354,223	26,195	2,742,839	113,798	2,856,637	211,250
Elimination	—	(14,111)	(14,111)	353	—	(113,798)	(113,798)	2,847
Consolidated total	¥340,112	¥ —	¥340,112	¥26,548	$2,742,839	$ —	$2,742,839	$214,097
Year ended March 31, 1996								
Chemical and synthetic fibers	¥112,861	¥ 725	¥113,586	¥ 2,785				
Chemical products	139,133	1,148	140,281	14,555				
Man-made leather, nonwoven fabrics and fastening materials	36,726	466	37,192	4,709				
Diversified businesses	42,149	11,465	53,614	3,757				
Total	330,869	13,804	344,673	25,806				
Elimination	—	(13,804)	(13,804)	287				
Consolidated total	¥330,869	¥ —	¥330,869	¥26,093				

Identifiable assets, Capital expenditures and Depreciation and amortization

	Millions of yen			Thousands of U.S. dollars		
	Identifiable assets	Capital expenditures	Depreciation and amortization	Identifiable assets	Capital expenditures	Depreciation and amortization
Year ended March 31, 1997						
Chemical and synthetic fibers	¥ 80,349	¥ 2,630	¥ 3,005	$ 647,976	$ 21,210	$ 24,234
Chemical products	120,873	13,263	7,264	974,782	106,960	58,580
Man-made leather, nonwoven fabrics and fastening materials	31,897	1,587	2,258	257,234	12,798	18,210
Diversified businesses	49,017	1,569	1,584	395,298	12,653	12,774
Total	282,136	19,049	14,111	2,275,290	153,621	113,798
Corporate assets and elimination	232,031	—	—	1,871,218	—	—
Consolidated total	¥514,167	¥19,049	¥14,111	$4,146,508	$153,621	$113,798
Year ended March 31, 1996						
Chemical and synthetic fibers	¥ 82,978	¥ 2,831	¥ 3,152			
Chemical products	113,241	9,007	7,243			
Man-made leather, nonwoven fabrics and fastening materials	33,019	3,855	1,966			
Diversified businesses	61,207	1,786	1,902			
Total	290,445	17,479	14,263			
Corporate assets and elimination	244,728	—	—			
Consolidated total	¥535,173	¥17,479	¥14,263			

Foreign sales consisting of export sales of the Company and its domestic consolidated subsidiaries and the sales of foreign consolidated subsidiaries for the years ended March 31, 1997 and 1996 totaled ¥69,227 million ($558,282 thousand) and ¥61,633 million, respectively, and accounted for 20% and 19% of consolidated net sales, respectively.

12. Subsequent event:
The Japanese Commercial Code provides that all appropriations of retained earnings, except interim cash dividends, must be approved at an ordinary general meeting of shareholders. In accordance with customary practice in Japan, the appropriation of retained earnings is not accrued in the financial statements for the year to which it relates but is recorded in the subsequent accounting year after shareholder approval has been obtained. The following appropriations of retained earnings of the Company as of March 31, 1997 were approved by the shareholders on June 27, 1997.

	Millions of yen	Thousands of U.S. dollars
Cash dividends, ¥4.50 ($0.04) per share	¥1,531	$12,347
Transfer to legal reserve	160	1,290
Bonuses to directors and statutory auditors	62	500

The above year-end cash dividends are comprised in annual dividends of ¥9.00 ($0.07) per share, since interim cash dividends of ¥4.50 ($0.04) per share were paid to shareholders, aggregating ¥1,531 million ($12,347 thousand) in December 1996.

Report of Independent Accountants

Kuraray Co., Ltd. and Consolidated Subsidiaries

To the Board of Directors and Shareholders of
Kuraray Co., Ltd.

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income, of shareholders' equity and of cash flows present fairly, in all material respects, the financial position of Kuraray Co., Ltd. and its consolidated subsidiaries at March 31, 1997 and 1996, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in Japan. 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 of these statements in accordance with generally accepted auditing standards which 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

Kohyoh & Co.

Kohyoh & Co.
(Certified Public Accountants)
Osaka, Japan/June 27, 1997

Price Waterhouse

Price Waterhouse
(Certified Public Accountants)