

Consolidated Balance Sheets

Shin-Etsu Chemical Co., Ltd. and Subsidiaries
As of 31st March, 1996 and 1997

	31st March,		31st March,
	1996	1997	1997
ASSETS	(millions of yen)		(thousands of U.S. dollars) (Note 3)
Current Assets:			
Cash and time deposits	¥137,649	¥ 234,152	\$ 1,888,322
Marketable securities (Note 6)	7,881	36,839	297,089
Notes and accounts receivable (Note 4):			
Trade	148,435	156,080	1,258,710
Unconsolidated subsidiaries and affiliates	15,748	10,721	86,460
Other	4,230	5,426	43,758
Less: allowance for doubtful accounts	(2,323)	(3,148)	(25,387)
	166,090	169,079	1,363,541
Inventories (Note 5)	62,825	73,934	596,242
Other current assets	3,240	4,686	37,790
Total current assets	377,685	518,690	4,182,984
Investments and Advances:			
Investments in and advances to unconsolidated subsidiaries and affiliates (Note 7)	21,486	25,186	203,113
Investments in securities (Note 6)	41,771	48,767	393,282
Long-term loans	894	1,510	12,177
Other	9,452	9,707	78,283
Less: allowance for doubtful accounts	(15)	(31)	(250)
Total investments and advances	73,588	85,139	686,605
Property, Plant and Equipment (Note 8):			
Buildings and structures	154,469	196,072	1,581,226
Machinery and equipment	452,836	525,335	4,236,573
Less: accumulated depreciation	(399,065)	(454,626)	(3,666,339)
	208,240	266,781	2,151,460
Land	26,460	27,206	219,403
Construction in progress	14,131	25,968	209,419
Total property, plant and equipment	248,831	319,955	2,580,282
Deferred Charges and Other Assets	1,767	7,375	59,476
Excess of Investment Cost Over Equity in Net Assets of Consolidated Subsidiaries	182	—	—
Adjustments on Foreign Currency Statement Translation (Note 2(4))	6,584	—	—
	¥708,637	¥ 931,159	\$ 7,509,347

The accompanying notes are an integral part of the statements.

	31st March,		31st March,
	1996	1997	1997
LIABILITIES AND STOCKHOLDERS' EQUITY	(millions of yen)		(thousands of U.S. dollars) (Note 3)
Current Liabilities:			
Short-term loans (Note 8)	¥ 62,732	¥ 73,353	\$ 591,556
Current portion of long-term debt (Note 8)	12,425	30,315	244,476
Notes and accounts payable (Note 4):			
Trade	74,191	84,138	678,532
Unconsolidated subsidiaries and affiliates	14,144	11,485	92,621
Other	37,484	46,020	371,129
	125,819	141,643	1,142,282
Accrued income taxes	17,674	22,205	179,073
Accrued expenses	30,988	38,832	313,161
Advance received	956	2,103	16,960
Other current liabilities	8,155	14,510	117,016
Total current liabilities	258,749	322,961	2,604,524
Long-Term Liabilities:			
Long-term debt (Note 8)	96,708	168,192	1,356,387
Accrued employees' severance indemnities (Note 9)	5,891	6,287	50,702
Deferred taxes—non-current	7,623	11,095	89,476
Other	1,439	15,974	128,822
Total long-term liabilities	111,661	201,548	1,625,387
Excess of Investment Cost Over Equity in Net Assets of Consolidated Subsidiaries	—	955	7,702
Adjustments on Foreign Currency Statement Translation (Note 2 (4))	—	12,741	102,750
Minority Interests in Consolidated Subsidiaries	17,240	18,228	147,000
Contingent Liabilities (Note 10)	—	—	—
Stockholders' Equity (Note 11):			
Common stock:			
Authorized: 800,000,000 shares			
Issued, par value ¥50 per share:			
324,691,433 shares and 349,569,337 shares as of			
31st March, 1996 and 1997, respectively	36,440	44,256	356,903
Additional paid-in capital	38,330	46,180	372,419
Legal reserve	4,705	4,967	40,057
Retained earnings (Note 17)	241,513	279,326	2,252,629
	320,988	374,729	3,022,008
Less: treasury stock	(1)	(3)	(24)
Total stockholders' equity	320,987	374,726	3,021,984
	¥708,637	¥931,159	\$7,509,347

The accompanying notes are an integral part of the statements.

Consolidated Statements of Income

Shin-Etsu Chemical Co., Ltd. and Subsidiaries
For the years ended 31st March, 1995, 1996 and 1997

	For the years ended 31st March,			For the year ended 31st March,
	1995	1996	1997	1997
	(millions of yen)			(thousands of U.S. dollars) (Note 3)
Net Sales (Note 14)	¥522,917	¥575,176	¥624,405	\$5,035,524
Cost of Sales (Notes 9, 12 and 14)	396,723	420,818	452,974	3,653,016
Gross profit	126,194	154,358	171,431	1,382,508
Selling, General and Administrative Expenses (Notes 9 and 12)	74,280	80,931	89,407	721,024
Operating income	51,914	73,427	82,024	661,484
Other Income/(Expenses):				
Interest and dividend income	5,108	4,656	7,296	58,839
Interest expenses	(6,197)	(5,369)	(7,669)	(61,847)
Amortisation of bond discounts	—	—	(1,163)	(9,379)
Loss on sale/disposal of property, plant and equipment	(1,035)	(2,701)	(1,136)	(9,161)
Foreign exchange gain/(loss)	(319)	1,120	3,463	27,927
Other, net	333	771	(1,117)	(9,008)
Income before income taxes	49,804	71,904	81,698	658,855
Income Taxes (Note 15):				
Current	26,009	33,547	39,398	317,726
Deferred	526	1,014	2,363	19,056
Income after income taxes	26,535	34,561	41,761	336,782
Income after income taxes	23,269	37,343	39,937	322,073
Minority Interests in Earnings of Consolidated Subsidiaries	(420)	(813)	(1,032)	(8,323)
Equity in Earnings of Affiliates	686	1,291	1,502	12,113
Adjustments on Foreign Currency Statement Translation (Note 2 (4))	3,330	—	—	—
Amortisation of Difference Between Cost of Investment and Equity in Net Assets of Consolidated Subsidiaries	(3)	4	207	1,669
Net income	¥ 26,862	¥ 37,825	¥ 40,614	\$ 327,532
		(Yen)		(U.S. dollars) (Note 3)
Per Share (Note 2 (14)):				
Net income—primary	¥ 82.80	¥ 116.51	¥ 118.24	\$ 0.954
Net income—fully diluted	—	¥ 106.66	¥ 103.95	\$ 0.838
Cash dividends	¥ 7.50	¥ 7.50	¥ 7.50	\$ 0.060
Weighted Average Number of Shares (Thousands)	324,415	324,649	343,490	343,490

The accompanying notes are an integral part of the statements.

Consolidated Statements of Stockholders' Equity

Shin-Etsu Chemical Co., Ltd. and Subsidiaries
For the years ended 31st March, 1995, 1996 and 1997

	Number of shares of common stock issued	Common stock	Additional paid-in capital	Legal reserve	Retained earnings
	(thousands)	(millions of yen)			
Balance as of 31st March, 1994	323,949	¥35,829	¥37,672	¥4,194	¥187,335
Net income for the year	—	—	—	—	26,862
Increase in retained earnings due to additional consolidation of subsidiaries	—	—	—	—	2,463
Increase in retained earnings due to increase in ownership percentage in consolidated subsidiaries	—	—	—	—	3
Cash dividends	—	—	—	—	(2,431)
Transfer to legal reserve	—	—	—	254	(254)
Directors' and statutory auditors' bonuses	—	—	—	—	(163)
Conversion of convertible debentures	672	555	555	—	—
Increase in equity interests in a consolidated subsidiary due to conversion of convertible debentures issued by the consolidated subsidiary	—	—	1	—	—
Increase in additional paid-in capital due to additional consolidation of subsidiaries	—	—	45	—	—
Adjustment on foreign currency statement translation (Note 2 (4))	—	—	—	—	(7,557)
Balance as of 31st March, 1995	324,621	36,384	38,273	4,448	206,258
Net income for the year	—	—	—	—	37,825
Increase in retained earnings due to additional consolidation of subsidiaries	—	—	—	—	320
Increase in retained earnings due to increase in ownership percentage in consolidated subsidiaries	—	—	—	—	4
Cash dividends	—	—	—	—	(2,434)
Transfer to legal reserve	—	—	—	257	(257)
Directors' and statutory auditors' bonuses	—	—	—	—	(203)
Conversion of convertible debentures	70	56	56	—	—
Increase in equity interests in a consolidated subsidiary due to conversion of convertible debentures issued by the consolidated subsidiary	—	—	1	—	—
Balance as of 31st March, 1996	324,691	36,440	38,330	4,705	241,513
Net income for the year	—	—	—	—	40,614
Increase in retained earnings due to additional consolidation of subsidiaries	—	—	—	—	151
Increase in retained earnings due to increase in ownership percentage in consolidated subsidiaries	—	—	—	—	1
Cash dividends	—	—	—	—	(2,501)
Transfer to legal reserve	—	—	—	262	(262)
Directors' and statutory auditors' bonuses	—	—	—	—	(190)
Conversion of convertible debentures	8,463	7,643	7,633	—	—
Exercise of warrant attached to debentures	180	173	216	—	—
Stock split on 20th May, 1996 (1 into 1.05)	16,235	—	—	—	—
Increase in equity interests in a consolidated subsidiary due to conversion of convertible debentures issued by the consolidated subsidiary	—	—	1	—	—
Balance as of 31st March, 1997	349,569	¥44,256	¥46,180	¥4,967	¥279,326

The accompanying notes are an integral part of the statements.

	Number of shares of common stock issued	Common stock	Additional paid-in capital	Legal reserve	Retained earnings
	(thousands)	(thousands of U.S. dollars) (Note 3)			
Balance as of 31st March, 1996	324,691	\$293,871	\$309,113	\$37,944	\$1,947,685
Net income for the year	—	—	—	—	327,532
Increase in retained earnings due to additional consolidation of subsidiaries	—	—	—	—	1,218
Increase in retained earnings due to increase in ownership percentage in consolidated subsidiaries	—	—	—	—	8
Cash dividends	—	—	—	—	(20,169)
Transfer to legal reserve	—	—	—	2,113	(2,113)
Directors' and statutory auditors' bonuses	—	—	—	—	(1,532)
Conversion of convertible debentures	8,463	61,637	61,556	—	—
Exercise of warrant attached to debentures	180	1,395	1,742	—	—
Stock split on 20th May, 1996 (1 into 1.05)	16,235	—	—	—	—
Increase in equity interests in a consolidated subsidiary due to conversion of convertible debentures issued by the consolidated subsidiary	—	—	8	—	—
Balance as of 31st March, 1997	349,569	\$356,903	\$372,419	\$40,057	\$2,252,629

The accompanying notes are an integral part of the statements.

Consolidated Statements of Cash Flows

Shin-Etsu Chemical Co., Ltd. and Subsidiaries
For the years ended 31st March, 1995, 1996 and 1997

	For the years ended 31st March,			For the year ended 31st March,
	1995	1996	1997	1997
	(millions of yen)			(thousands of U.S. dollars) (Note 3)
Cash Flows From Operating Activities:				
Net income	¥ 26,862	¥ 37,825	¥ 40,614	\$ 327,532
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortisation	42,986	46,034	54,554	439,952
Equity in earnings of affiliates	(686)	(1,291)	(1,502)	(12,113)
Loss on sale/disposal of property, plant and equipment	1,035	2,701	1,136	9,161
Other, net	(13,652)	(7,171)	13,779	111,121
Changes in assets and liabilities:				
Increase in notes and accounts receivable	(8,056)	(20,331)	(3,814)	(30,758)
Increase in inventories	(4,734)	(8,681)	(11,109)	(89,589)
Increase in notes and accounts payable	15,858	22,881	15,824	127,613
Increase in accrued income taxes	5,566	1,933	4,531	36,540
Other, net	1,057	6,813	10,663	85,992
Net cash provided by operating activities	66,236	80,713	124,676	1,005,451
Cash Flows From Investing Activities:				
Purchase of properties	(67,689)	(71,863)	(110,570)	(891,694)
Proceeds from sales of properties	839	15,000	1,383	11,153
Increase in investments in securities	(71)	(1,335)	(6,996)	(56,419)
Decrease (increase) in investments in unconsolidated subsidiaries and affiliates	16,495	(2,952)	(2,220)	(17,903)
Other, net	3,580	1,155	410	3,307
Net cash used for investing activities	(46,846)	(59,995)	(117,993)	(951,556)
Cash Flows From Financing Activities:				
Proceeds from issue of debentures	—	—	105,065	847,298
Borrowing of long-term debt	13,394	10,822	15,025	121,169
Payment of long-term debt	(6,814)	(11,597)	(16,243)	(130,992)
Increase (decrease) in short-term loans	(6,391)	375	10,621	85,653
Cash dividends paid	(2,431)	(2,434)	(2,501)	(20,169)
Other, net	381	(1,154)	13,667	110,218
Net cash provided by (used for) financing activities	(1,861)	(3,988)	125,634	1,013,177
Effect of Exchange Rate Changes on Cash	4,487	(1,320)	(6,856)	(55,290)
Net Increase in Cash and Cash Equivalents	22,016	15,410	125,461	1,011,782
Cash and Cash Equivalents at Beginning of Year	108,104	130,120	145,530	1,173,629
Cash and Cash Equivalents at End of Year	¥130,120	¥145,530	¥ 270,991	\$ 2,185,411

The accompanying notes are an integral part of the statements.

Notes to Consolidated Financial Statements

Shin-Etsu Chemical Co., Ltd. and Subsidiaries
As of 31st March, 1995, 1996 and 1997

1. Basis of presenting financial statements

The accompanying consolidated financial statements have been prepared from accounts and records maintained by Shin-Etsu Chemical Co., Ltd. (the "Company") and its subsidiaries. The Company and its domestic consolidated subsidiaries have maintained their accounts and records in accordance with the provisions set forth in the Japanese Commercial Code and the Securities and Exchange Law and in conformity with generally accepted accounting principles prevailing in Japan. The accounts of overseas consolidated subsidiaries are based on their accounting records maintained in conformity with generally accepted accounting principles and practices prevailing in the respective countries. In general, no adjustments to the accounts of overseas consolidated subsidiaries have been reflected in the accompanying consolidated financial statements to present them in compliance with Japanese accounting principles and practices followed by the Company.

The presentation of the accompanying consolidated financial statements is made in conformity with the "Consolidated Financial Statements Regulation" (ordinance promulgated by the Ministry of Finance) and meets the requirements for disclosure of financial information of the Company on a consolidated basis. However, certain account balances, as disclosed in the basic consolidated financial statements in Japan, have been reclassified to the extent deemed necessary to enable presentation in a form which is more familiar to readers outside Japan.

Although the consolidated statements of cash flows are not disclosed in Japan for domestic reporting purposes, such statements for the years ended 31st March, 1995, 1996 and 1997 have been prepared in compliance with the methods recommended by the Japanese Institute of Certified Public Accountants.

2. Summary of significant accounting policies

(1) Principles of consolidation

The Company had 96 majority-owned subsidiaries as of 31st March, 1997 (97 as of 31st March, 1996 and 90 as of 31st March, 1995). The consolidated financial statements include the accounts of the Company and its 54 (51 for 1996 and 1995) majority-owned subsidiaries listed on page 41 with closing dates for their respective fiscal years (the "Companies").

The remaining 42 (46 for 1996 and 39 for 1995) unconsolidated subsidiaries whose combined assets, net sales, net income and retained earnings in the aggregate are not significant compared to those of the consolidated financial statements of the Companies, therefore, have not been consolidated with the Company. For consolidation of the accounts of subsidiaries whose closing dates are not in agreement with the Company, necessary adjustments are made on significant intercompany transactions which took place during the periods between the closing dates for the fiscal years of respective consolidated subsidiaries and that of the Company.

Unrealised intercompany profits and losses among the Companies are entirely eliminated, and the portion thereof attributable to the minority interests is charged to the minority interests.

Elimination of cost of investments in consolidated subsidiaries with the underlying equity in net assets of such subsidiaries has been made by the Company to include equity in the net income (loss) of subsidiaries earned subsequent to the acquisition of each block of shares. Any difference between the cost of an investment in a subsidiary and the amount of underlying equity in net assets of the subsidiary is treated as an asset or a liability, as the case may be, and amortised over a period of five years on a straight-line basis.

Legal reserve of consolidated subsidiaries provided subsequent to the acquisition of such subsidiaries by the Company is included in retained earnings and is not shown separately in the consolidated financial statements.

(2) Accounting for investments in unconsolidated subsidiaries and affiliates

The Company had 42 (39 for 1995 and 46 for 1996) unconsolidated subsidiaries (majority-owned) and 21 (19 for 1995 and 22 for 1996) affiliates (meaning 20 percent to 50 percent ownership of company's equity interest). The equity method is applied to the investments in two unconsolidated subsidiaries and four major affiliates since investments in the remaining unconsolidated subsidiaries and affiliates are not material for the consolidated financial statements.

The major unconsolidated subsidiaries and affiliates accounted for by the equity method are listed below:

Shin-Etsu Handotai Taiwan Co., Ltd.

Shin-Etsu Quartz Products Co., Ltd.

Kashima Vinyl Chloride Monomer Co., Ltd.

Nagano Electronics Industrial Co., Ltd.

(3) Translation of foreign currency transactions

Revenue and expense items arising from transactions denominated in foreign currencies are generally translated into Japanese yen at the rates effective at the respective transaction dates.

Foreign currency deposits and short-term receivables and payables denominated in foreign currencies are translated into Japanese yen at the current exchange rate prevailing at the respective balance sheet dates and the resulting translation gain or loss is included in determination of net income for the year.

Long-term receivables and payables denominated in foreign currencies including investments in overseas unconsolidated subsidiaries and affiliates are translated at the historical rates prevailing at the transaction dates.

Exceptionally, receivables and payables denominated in foreign currencies which are hedged by forward exchange contracts are translated at the contracted rate of exchange.

However, all of the overseas consolidated subsidiaries apply the current rate method to translate transactions and account balances in foreign currencies into their respective home currencies.

The accounting standards for translation of transactions and account balances denominated in foreign currencies have been amended and became effective from the year ended 31st March, 1996. The new standards were adopted by the Company and its domestic subsidiaries during the year ended 31st March, 1996 and 1997. If the new standards had been applied in the year ended 31st March, 1995, there would have been no effect at all.

(4) Translation of foreign currency financial statements (accounts of overseas subsidiaries)

The translation of foreign currency financial statements of overseas subsidiaries into Japanese yen for consolidation purposes is made by the method of translation prescribed by the statements issued by the Business Accounting Council (“BAC”) of Japan.

Until the year ended 31st March, 1995, short-term monetary items were translated at current rates. In contrast, short-term non-monetary items and long-term assets and liabilities were translated at historical rates, except for some overseas subsidiaries whose foreign currency financial statements were translated at current exchange rates prevailing at the balance sheet dates because short-term non-monetary items and long-term assets and liabilities of these subsidiaries were not significant.

Net income for the year and the balance of retained earnings at year-end were required to be translated at current exchange rates while revenue and expense items were translated at the average exchange rate or at the historical rate, as appropriate.

In this connection, certain adjusting accounts were set up in the balance sheet, statements of income, and stockholders’ equity to enable balancing of debit and credit totals as well as the reconciliation of the beginning balance with the ending balance of retained earnings. Such adjusting account balances are shown as “Adjustments on Foreign Currency Statement Translation” in the accompanying consolidated financial statements as of 31st March, 1995 and for the fiscal years then ended.

In compliance with the new accounting standards for foreign currency transactions, which became effective from the year ended 31st March, 1996, the Company changed its translation method. Under the new standards, all assets and liabilities are translated into Japanese yen at current exchange rates while capital accounts and retained earnings are translated at historical rates, and revenue and expense items are translated at the average exchange rates during the year. The resulting translation adjustments are, as before, shown as “Adjustments on Foreign Currency Statement Translation” in the accompanying balance sheets as of 31st March, 1996 and 1997.

The “income before income taxes” for the year ended 31st March, 1995 would have increased by ¥3,640 million as compared with the amount which would have been reported if the current method had been applied for the translation of the financial statements of subsidiaries for the year 1995 stated in foreign currencies.

(5) Inventory valuation

Inventories are valued principally at cost determined by the annual average method.

(6) Valuation of securities

Investments in securities, both quoted and non-quoted, are valued principally at cost determined by the moving average method.

(7) Property, plant and equipment

Depreciation of property, plant and equipment is principally computed on the declining-balance method, based on the estimated useful lives of assets prescribed by the Japanese tax laws. The cost of property, plant and equipment retired or otherwise disposed of and accumulated depreciation are eliminated from the related accounts, and the resulting profit or loss is reflected in income.

(8) Amortisation

New share issue expenses are charged to income as incurred. Discounts on bond issues are deferred and amortised on a straight-line basis over a period up to the maturity of the relevant bonds. Research and development costs are charged to income as incurred.

(9) Repairs and maintenance

Normal repairs and maintenance, including minor renewals and improvements, are charged to income as incurred.

(10) Accounting for leases

Finance leases other than those which are deemed to transfer the ownership of the leased assets to lessees are accounted for by the method similar to that applicable to ordinary operating leases.

(11) Recognition of certain accrued expenses

In general, the Companies follow the accrual basis of accounting for all income and expense items. However, the Japanese income tax laws provide for limits deductible for tax purposes with respect to certain accrued expenses which are essentially the estimates of amounts to be determined in future years. The accrued expenses of the Companies to which such limits apply under the laws are: accrued bonuses to employees, accrued employees' severance indemnities and allowance for doubtful accounts. The Companies generally record such accrued expense items on the Companies' own estimate, which is deemed to be adequate for financial reporting purposes.

(12) Income taxes

Income taxes are provided based on amounts required by the tax returns for the period. No tax effect is recorded for timing differences in recognition of certain expenses between tax and financial reporting, except for those of 14 subsidiaries including Shintech, Inc., Shin-Etsu Handotai America, Inc., which follow the interperiod income tax allocation.

(13) Research and development costs

Research and development costs are charged to income as incurred.

(14) Net income and dividend per share

Net income per share is based upon the weighted average number of shares of common stock outstanding during each fiscal year. In accordance with the amendments to the Japanese securities and exchange regulations, net income per share adjusted for dilution (assuming full conversion of all convertible debentures of the Company outstanding with related reduction in interest expenses) has been disclosed from the fiscal year ended 31st March, 1996.

Cash dividends per share represent actual dividends per share declared as applicable to the respective years.

(15) Dividends

Dividends are proposed by the Board of Directors and approved by the stockholders at meetings held subsequent to the fiscal year to which the dividends are applicable, and registered stockholders as of the end of such fiscal year are entitled to the subsequently declared dividends. Also the interim cash dividends are paid. (See Note 11)

Dividends charged to retained earnings in the accompanying consolidated statements of stockholders' equity represent dividends approved and paid during the year.

(16) Appropriation of retained earnings

Under the Japanese Commercial Code and the Articles of Incorporation of the Company, the plan for appropriation of retained earnings (primarily for cash dividend payments) proposed by the Board of Directors should be approved by the stockholders' meeting which must be held within three months after the end of each fiscal year. The appropriation of retained earnings reflected in the accompanying consolidated financial statements represents the results of such appropriations which relate to the immediately preceding fiscal year but were approved by the stockholders' meeting and disposed of during that year. As is customary practice in Japan, the payment of bonuses to directors and statutory auditors is made out of retained earnings instead of being charged to income for the year and constitutes a part of appropriations cited above.

(17) Consumption tax

The consumption tax withheld by the Company on sales of products is not included in the amount of "Net Sales" in the accompanying Consolidated Statements of Income. And the consumption tax borne by the Company on purchases of goods and services, and expenses is not included in the related amounts in the accompanying Consolidated Statements of Income, either.

3. United States dollar amounts

The Company prepares its consolidated financial statements in yen. The dollar amounts included in the consolidated financial statements and notes thereto represent the arithmetical results of translating yen to dollars on a basis of ¥124 to U.S.\$1, the approximate effective rate of exchange on 31st March, 1997.

The inclusion of such dollar amounts is solely for convenience and is not intended to imply that yen amounts have been or could be readily converted, realised or settled in dollars at ¥124 to U.S.\$1 or at any other rate.

4. Notes and accounts receivable and payable

The companies recognise the settlements of notes receivable and notes payable at such time as the bank clearance of the notes are actually made. The balance sheet date of 31st March, 1996 was incidentally a holiday for financial institutions and,

therefore, the following accounts include the balances of notes receivable and notes payable due on that date as unsettled in the relevant amount in the accompanying consolidated balance sheet as of 31st March, 1996:

	(millions of yen)
Notes and accounts receivable	¥8,263
Notes and accounts payable	7,049
Contingent liabilities—Notes discounted by banks	104
Contingent liabilities—Notes endorsed to outsiders	41

5. Inventories

Inventories as of 31st March, 1996 and 1997 consisted of the following:

	31st March,		
	1996	1997	1997
	(millions of yen)		(thousands of U.S. dollars)
Merchandise	¥ 3,991	¥ 4,197	\$ 33,847
Finished products	24,571	30,544	246,322
Semifinished products	10,981	11,419	92,089
Raw materials	14,736	16,960	136,774
Supplies	5,090	7,808	62,968
Others	3,456	3,006	24,242
	¥62,825	¥73,934	\$596,242

6. Marketable securities and investments in securities

Marketable securities (current portfolio) and investments in securities (non-current portfolio) held by the Companies as of 31st March, 1996 and 1997 consisted of the following:

	31st March,		
	1996	1997	1997
	(millions of yen)		(thousands of U.S. dollars)
Marketable securities (current portfolio):			
Listed corporate shares	¥ 1,606	¥ 1,395	\$ 11,250
Bonds, debentures and others	6,275	35,444	285,839
	¥ 7,881	¥36,839	\$297,089
Investments in securities (non-current portfolio):			
Listed corporate shares	¥35,950	¥37,003	\$298,411
Other shares (unquoted)	1,609	2,113	17,040
Bonds, debentures and others	4,212	9,651	77,831
	¥41,771	¥48,767	\$393,282

The aggregate market value of listed corporate shares (marketable equity securities) and net unrealised gains as of 31st March, 1996 and 1997 amounted to as follows:

	31st March,		
	1996	1997	1997
	(millions of yen)		(thousands of U.S. dollars)
Current:			
Market value	¥ 3,642	¥ 2,726	\$ 21,984
Net unrealised gains	2,036	1,331	10,734
Non-current:			
Market value	¥101,616	¥80,303	\$647,605
Net unrealised gains	65,666	43,300	349,194

7. Investments in and advances to unconsolidated subsidiaries and affiliates

Investments in and advances to unconsolidated subsidiaries and affiliates as of 31st March, 1996 and 1997 consisted of the following:

	31st March,		
	1996	1997	1997
	(millions of yen)		(thousands of U.S. dollars)
Held directly by the Company:			
Affiliates:			
Three affiliates accounted for by the equity method (See Note 2(2))	*¥ 5,977	*¥ 7,525	*\$ 60,685
Kashima Denkai Co., Ltd.	805	805	6,492
Unitika Chemical Co., Ltd.	600	600	4,839
Others	233	203	1,637
	7,615	9,133	73,653
Unconsolidated subsidiaries:			
Silicon Metal Company of Australia Ltd. (1)	2,567	—	—
Shin-Etsu Silicones Europe B.V.	734	734	5,919
MicroSi, Inc.	499	499	4,024
Shin-Etsu Electronics Malaysia Sdn. Bhd.	494	1,400	11,290
Shin-Etsu Electronics Materials Singapore Pte. Ltd. (1)	203	—	—
Shin-Etsu Film Co., Ltd.	199	199	1,605
Others	354	332	2,678
	5,050	3,164	25,516
Held indirectly through subsidiaries			
Unconsolidated subsidiaries:			
Two unconsolidated subsidiaries and an affiliate accounted for by the equity method (See Note 2(2))	—	5,318	42,887
Others	8,138	5,710	46,049
	8,138	11,028	88,936
Advances	683	1,861	15,008
	¥21,486	¥25,186	\$203,113

*Accounted for by the equity method. Others are carried at cost or less.

(1) Newly consolidated with effect from the year ended 31st March, 1997.

8. Short-term loans and long-term debt

Short-term loans outstanding as of 31st March, 1996 and 1997 are represented generally by one-year notes issued by the Companies to banks. Substantially all of the notes are issued to banks which have written basic agreements with the Companies to the effect that, with respect to all present or future loans with such banks, the Companies shall provide collateral

(including sums on deposit with such banks), or guarantors for such loans, immediately upon the banks' request, and that any collateral furnished pursuant to such agreement or otherwise will be applicable to all indebtedness to such banks.

Long-term debt as of 31st March, 1996 and 1997 consisted of the following:

	31st March,		
	1996	1997	1997
	(millions of yen)		(thousands of U.S. dollars)
Loans with banks and other financial institutions:			
Secured	¥ 18,970	¥ 16,474	\$ 132,855
Unsecured	26,792	28,105	226,653
Secured debentures:			
6.5% mortgage debentures issued by a consolidated subsidiary, due November 1997	2,000	2,000	16,129
Unsecured debentures:			
3 ³ / ₈ % notes in U.S. dollars, due August 2000 with warrants	—	52,562	423,887
2.7% debentures issued by a consolidated subsidiary, due April 2001	—	3,274	26,403
Unsecured convertible debentures:			
3.0% convertible debentures in U.S. dollars, due May 2000	40	29	234
2.1% convertible debentures, due May 1997	439	357	2,879
2.0% convertible debentures, due March 1998	20,992	17,966	144,887
1.3% convertible debentures, due March 1999	39,794	37,538	302,726
0.4% convertible debentures, due September 2005	—	40,098	323,371
Secured convertible debentures:			
2.4% convertible mortgage debentures issued by a consolidated subsidiary, due March 1999	106	104	839
	109,133	198,507	1,600,863
Less portion due within one year	(12,425)	(30,315)	(244,476)
	¥ 96,708	¥168,192	\$1,356,387

Additional information with respect to the Companies' convertible debentures is summarised as follows:

	Issue date and principal amount at issue	Balance as of 31st March, 1997 in denominated currencies	Terms of conversion of 31st March, 1997		
			Current conversion price per share**	Fixed exchange rates for conversion	Additional shares issuable upon full conversion (in thousands)
Unsecured:					
3.0% convertible debentures in U.S. dollars, due 2000	4th March, 1985 (U.S.\$30 million)	U.S.\$0.115 million	¥1,112.2	U.S.\$1=¥262.60	27
2.1% convertible debentures in yen, due 1997	16th December, 1986 (¥15,000 million)	¥357 million	¥1,084.1	—	329
2.0% convertible debentures in yen, due 1998	5th December, 1988 (¥25,000 million)	¥17,966 million	¥1,560.5	—	11,513
1.3% convertible debentures in yen, due 1999	13th February, 1990 (¥40,000 million)	¥37,538 million	¥1,748.6	—	21,467
0.4% convertible debentures in yen, due 2005	8th August, 1996 (¥50,000 million)	¥40,098 million	¥1,917.0	—	20,917
Secured:					
2.4% convertible mortgage debentures in yen, due 1999*	31st March, 1987 (¥5,000 million)	¥104 million	¥ 540.7	—	N/A
					54,253

Additional information with respect to the Companies' warrants is summarised as follows:

	Issue date and principal amount at issue	Balance as of 31st March, 1997 in denominated currencies	Terms of exercise of 31st March, 1997		
			Current exercise price per share**	Fixed exchange rates for exercise	Additional shares issuable upon full exercise (in thousands)
Warrants attached to:					
3 ³ / ₈ % notes in U.S. dollars, due 2000	8th August, 1996 (U.S.\$500 million)	U.S.\$497 million	¥1,917.0	U.S.\$1=¥109.45	28,367
					28,367

*Issued by a subsidiary Shin-Etsu Polymer Co., Ltd.

**Subject to adjustment for subsequent stock dividends, stock splits and others.

3³/₈% notes with warrants denominated in foreign currency are covered by a long-term forward exchange contract and accordingly are translated into yen at the contracted exchange rate. The difference between the amount translated at the contract rates and the amount translated at the historical exchange rates is deferred and amortised over a period from the date of concluding the forward exchange contract to the date of settlement based on the number of months. As a result, during the year ended 31st March, 1997, ¥273 million (\$2,202 thousand) was amortised to income as a credit to "Interest expenses" and

"Other, net", respectively, in "Other Income/(Expenses)" in the accompanying Consolidated Statements of Income for the year ended 31st March, 1997. The unamortised balance was included in "Other current liabilities" in an amount of ¥410 million (\$3,306 thousand) and in "Other" in the Long-term Liabilities section in an amount of ¥956 million (\$7,710 thousand), respectively in the accompanying Consolidated Balance Sheet at 31st March, 1997. Under the Japanese tax laws, such translation gains are not taxable until such time as the forward exchange contract is performed.

As of 31st March, 1997, assets pledged as collateral for short-term loans, mortgage debentures and long-term loans were as follows:

	(millions of yen)	(thousands of U.S. dollars)
Net book value of property, plant and equipment	¥57,946	\$467,306

The aggregate annual maturities of long-term debt are as follows:

	(millions of yen)	(thousands of U.S. dollars)
Year ending 31st March, 1998	¥ 30,315	\$ 244,476
1999	50,735	409,153
2000	65,756	530,290
2001 and thereafter	51,701	416,944
	¥198,507	\$1,600,863

9. Retirement and pension plans

Employees of the Company and certain subsidiaries are covered by non-contributory funded pension plans. Benefits under these plans are based on the current rate of pay, length of service and conditions under which terminations occur. The plans provide for either a lump sum payment to terminating employees after 20 years of service or pension payments for a period of 10 years at their option. Employees with more than three years but less than 20 years of service are also entitled to receive a lump sum payment upon retirement under the plans.

Unamortised past service liability, arising from the adoption of the plan during 1970, is being funded and amortised over a 29-year period.

In addition to the programmes described above, the Company and certain subsidiaries have also established employee early retirement plans. In such plans, the employees are entitled to receive lump sum payments which are determined according to their age at the time of voluntary termination of

their employment. Reserves for liabilities for payments under such plans are provided for 100 percent of the amounts payable if all eligible employees voluntarily terminated employment at the respective balance sheet date.

In certain subsidiaries which have not adopted the above-mentioned plans, employees are entitled to receive lump sum payments based on the current rate of pay, length of service and conditions under which terminations occur. These subsidiaries provide reserves for liabilities for payments under the plans for 40 percent of the amount payable, which is the maximum amount permitted by the Japanese tax laws, if all employees voluntarily terminated their employment at the respective balance sheet date.

Charges to income for such retirement and pension plan costs for the years ended 31st March, 1995, 1996 and 1997 were ¥2,999 million, ¥2,803 million and ¥3,498 million (\$28,210 thousand), respectively.

10. Contingent liabilities

As of 31st March, 1997, the Companies were contingently liable as a guarantor of housing loans for employees and loans to unconsolidated subsidiaries, affiliates and others in the aggregate amount of ¥1,438 million (\$11,597 thousand).

In addition, as of 31st March, 1997, the Companies had contingent liabilities arising from notes discounted by banks in the amounts of ¥541 million (\$4,363 thousand).

11. Legal reserve and retained earnings

The Japanese Commercial Code provides that an amount equal to at least 10 percent of cash distribution paid out of retained earnings should be appropriated to legal reserve until such reserve equals 25 percent of stated common stock. The legal reserve may be used to reduce a deficit or may be transferred to a common stock account through appropriate stockholder and director actions, but is not available for dividend payment.

The legal reserve of consolidated subsidiaries is included in the retained earnings and is not shown separately in the accompanying consolidated financial statements.

The Company's Board of Directors, with subsequent approval by stockholders, has made annual appropriations of retained earnings for various purposes. Any dispositions of such appropriations shall be at the discretion of the Board of Directors and stockholders. Such administrative appropriations have not been segregated from retained earnings in the accompanying consolidated financial statements.

The Japanese Commercial Code provides that interim cash dividends (payable to stockholders of record as of 30th September of each year in the case of the Company on a semi-annual basis) may be distributed upon approval by the Board of Directors. The Company paid interim dividends during the years ended 31st March, 1995, 1996 and 1997 in the amounts of ¥1,217 million, ¥1,217 million and ¥1,283 million (\$10,347

thousand) (¥3.75 per share) respectively, which were actually paid to stockholders on 9th December, 1994, 8th December, 1995 and 8th December, 1996, respectively. In the accompanying consolidated statements of stockholders' equity, these dividend payments are reflected in the years ended 31st March, 1995, 1996 and 1997, respectively.

12. Research and development costs

Research and development costs incurred and charged to income for the years ended 31st March, 1995, 1996 and 1997

were ¥16,674 million, ¥17,634 million and ¥18,256 million (\$147,226 thousand), respectively.

13. Lease transactions

Lease rental expenses on finance lease contracts without ownership-transfer for the year ended 31st March, 1997 amounted to ¥377 million (\$3,040 thousand).

14. Related party transactions

The Company's sales to and purchases from its unconsolidated subsidiaries and affiliates for the years ended 31st March, 1995, 1996 and 1997 are summarised as follows:

	Year ended 31st March,			1997 (thousands of U.S. dollars)
	1995	1996	1997	
	(millions of yen)			
Sales	¥22,715	¥26,016	¥14,891	\$120,089
Purchases	22,666	25,290	28,316	228,355

15. Income taxes

Income taxes in Japan applicable to the Company and its domestic subsidiaries for the years ended 31st March, 1995, 1996 and 1997 consisted of corporate income tax (national),

enterprise tax (local) and resident income taxes (local) at the approximate rates indicated below:

	Rates on taxable income		
	1995	1996	1997
Corporate income tax	37.5%	37.5%	37.5%
Enterprise tax	12.1	12.1	12.1
Resident income taxes	7.5	7.7	7.5
	57.1%	57.3%	57.1%
Statutory tax rate in effect to reflect the deductibility of enterprise tax when paid (unlike other income taxes, enterprise tax is deductible for tax purposes when it is paid)	50.9%	51.1%	50.9%

Income tax expenses as shown in the accompanying consolidated statements of income are different from the amounts computed by applying the above-mentioned statutory rates to income before income taxes. The principal reasons such differences arise are that no tax effects have been recognised by

the Company and its domestic subsidiaries on certain timing differences between financial accounting and tax reporting purposes consisting primarily of accrued enterprise tax not deductible until paid.

16. Segment information

(1) Business segment information

The Companies operate principally in the following three lines of business, "Chemicals", "Electronics Materials" and "Other." These lines of business deal with the following main products and merchandise:

Chemicals

Synthetic resins	Polyvinyl chloride, silicones, vinyl acetate monomer, polyvinyl alcohol
Organic chemicals	Methanol, chloromethanes, cellulose derivatives
Other chemicals	Caustic soda, lime nitrogen, fused phosphates, ferroalloys, silicon metal
Electronics Materials	Semiconductor silicon, oxide single-crystals, synthetic quartz, organic materials for electronics industry, rare earths, rare earth magnets
Other	Export of technology and plants, export and import of merchandise, construction and plant engineering, information processing

Sales, related operating costs and expenses, operating income, assets, depreciation and capital expenditure of the Companies at 31st March, 1995, 1996 and 1997 and for the years then ended, classified by business segments are presented below. The disclosure of assets, depreciation and

capital expenditure for each segment classified by business has been made since it became mandatory with effect from the year ended 31st March, 1996, as a result of the amendments to the Consolidated Financial Statement Regulations.

	For the year ended 31st March, 1995				
	Chemicals	Electronics materials	Other	Elimination of inter-segment sales/income	Consolidated total
	(millions of yen)				
Sales					
Sales to outside customers	¥298,467	¥170,706	¥53,744	¥ —	¥522,917
Inter-segment sales	10,841	1,053	33,340	(45,234)	—
Total	309,308	171,759	87,084	(45,234)	522,917
Operating costs and expenses	280,304	149,404	86,526	(45,231)	471,003
Operating income (Note 2)	¥ 29,004	¥ 22,355	¥ 558	¥ (3)	¥ 51,914
	For the year ended 31st March, 1996				
	Chemicals	Electronics materials	Other	Elimination or common assets (Note 1)	Consolidated total
	(millions of yen)				
Sales					
Sales to outside customers	¥303,285	¥214,635	¥57,256	¥ —	¥575,176
Inter-segment sales	12,628	1,208	34,990	(48,826)	—
Total	315,913	215,843	92,246	(48,826)	575,176
Operating costs and expenses	282,134	176,788	91,393	(48,566)	501,749
Operating income	¥ 33,779	¥ 39,055	¥ 853	¥ (260)	¥ 73,427
Assets	¥303,905	¥270,529	¥42,941	¥ 91,262	¥708,637
Depreciation	17,918	27,200	529	—	45,647
Capital expenditure	23,513	42,964	546	(232)	66,791

	For the year ended 31st March, 1997				
	Chemicals	Electronics materials	Other	Elimination or common assets (Note 1)	Consolidated total
	(millions of yen)				
Sales					
Sales to outside customers	¥310,030	¥255,840	¥ 58,535	¥ —	¥624,405
Inter-segment sales	12,844	1,595	47,861	(62,300)	—
Total	322,874	257,435	106,396	(62,300)	624,405
Operating costs and expenses	294,429	205,942	104,334	(62,324)	542,381
Operating income	¥ 28,445	¥ 51,493	¥ 2,062	¥ 24	¥ 82,024
Assets	¥336,365	¥366,980	¥ 55,852	¥171,962	¥931,159
Depreciation	18,434	33,079	678	—	52,191
Capital expenditure	15,478	76,846	835	(315)	92,844

	For the year ended 31st March, 1997				
	Chemicals	Electronics materials	Other	Elimination or common assets (Note 1)	Consolidated total
	(thousands of U.S. dollars)				
Sales					
Sales to outside customers	\$2,500,242	\$2,063,226	\$472,056	\$ —	\$5,035,524
Inter-segment sales	103,580	12,863	385,976	(502,419)	—
Total	2,603,822	2,076,089	858,032	(502,419)	5,035,524
Operating costs and expenses	2,374,427	1,660,823	841,403	(502,613)	4,374,040
Operating income	\$ 229,395	\$ 415,266	\$ 16,629	\$ 194	\$ 661,484
Assets	\$2,712,621	\$2,959,516	\$450,420	\$1,386,790	\$7,509,347
Depreciation	148,661	266,766	5,468	—	420,895
Capital expenditure	124,822	619,726	6,734	(2,540)	748,742

Notes:

- (1) The amounts of the common assets included in the column "Elimination or common assets" for the years ended 31st March, 1996 and 1997 were ¥113,904 million and ¥199,078 million (\$1,605,468 thousand), respectively, which mainly consist of surplus working funds (cash, deposits and marketable securities) and long-term investment funds (investments in securities) of the Company.
- (2) If the new method of translating foreign currency financial statements, which became effective from the year ended 31st March, 1996, had been applied in the year ended 31st March, 1995, operating income of "Chemicals" and "Electronics Materials" would have increased by ¥1,190 million and ¥2,451 million, respectively, operating income of "Other" would have decreased by ¥1 million and consolidated total operating income would have increased by ¥3,640 million as compared with the amounts which have been reported.

(2) Geographical segment information

The analysis of the sales, operating costs and expenses, operating income and assets of the Companies by geographical segments (within Japan and outside Japan) of 31st March, 1995, 1996 and 1997 and for the years then ended are presented

below. The disclosure of assets for each segment classified by geographic area has become mandatory with effect from the year ended 31st March, 1996, as a result of the amendments to the Consolidated Financial Statement Regulations:

	Year ended 31st March, 1995			
	Within Japan	Outside Japan	Elimination of inter-segment sales/income	Consolidated total
	(millions of yen)			
Sales				
Sales to outside customers	¥380,773	¥142,144	¥ —	¥522,917
Inter-segment sales	34,293	14,128	(48,421)	—
Total	415,066	156,272	(48,421)	522,917
Operating costs and expenses	381,572	138,834	(49,403)	471,003
Operating income (Note 2)	¥ 33,494	¥ 17,438	¥ 982	¥ 51,914

	Year ended 31st March, 1996			
	Within Japan	Outside Japan	Elimination or common assets (Note 1)	Consolidated total
	(millions of yen)			
Sales				
Sales to outside customers	¥397,026	¥178,150	¥ —	¥575,176
Inter-segment sales	45,323	15,531	(60,854)	—
Total	442,349	193,681	(60,854)	575,176
Operating costs and expenses	398,343	164,981	(61,575)	501,749
Operating income	¥ 44,006	¥ 28,700	¥ 721	¥ 73,427
Assets	¥447,690	¥198,313	¥ 62,634	¥708,637

	Year ended 31st March, 1997			
	Within Japan	Outside Japan	Elimination or common assets (Note 1)	Consolidated total
	(millions of yen)			
Sales				
Sales to outside customers	¥404,109	¥220,296	¥ —	¥624,405
Inter-segment sales	65,073	17,261	(82,334)	—
Total	469,182	237,557	(82,334)	624,405
Operating costs and expenses	418,712	206,511	(82,842)	542,381
Operating income	¥ 50,470	¥ 31,046	¥ 508	¥ 82,024
Assets	¥498,088	¥304,004	¥129,067	¥931,159

	For the year ended 31st March, 1997			
	Within Japan	Outside Japan	Elimination or common assets (Note 1)	Consolidated total
	(thousands of U.S. dollars)			
Sales				
Sales to outside customers	\$3,258,944	\$1,776,580	\$ —	\$5,035,524
Inter-segment sales	524,782	139,202	(663,984)	—
Total	3,783,726	1,915,782	(663,984)	5,035,524
Operating costs and expenses	3,376,710	1,665,411	(668,081)	4,374,040
Operating income	\$ 407,016	\$ 250,371	\$ 4,097	\$ 661,484
Assets	\$4,016,839	\$2,451,645	\$1,040,863	\$7,509,347

Notes:—

- (1) The amounts of the common assets included in the column “Elimination or common assets” for the years ended 31st March, 1996 and 1997 were ¥113,904 million and ¥199,078 million (\$1,605,468 thousand), respectively, which mainly consist of surplus working funds (cash, deposits and marketable securities) and long-term investment funds (investments in securities) of the Company.
- (2) If the new method of translating foreign currency financial statements, which became effective from the year ended 31st March, 1996, had been applied in the year ended 31st March, 1995, operating income of “Outside Japan” and consolidated total operating income would have increased by ¥3,640 million as compared with the amounts which have been reported.

(3) Overseas sales information

Overseas sales of the Companies (export sales of the Company and domestic subsidiaries plus sales of overseas consolidated subsidiaries) for the years ended 31st March, 1995, 1996 and 1997 are summarised as follows:

	Year ended 31st March,			
	1995	1996	1997	1997
	(millions of yen)			(thousands of U.S. dollars)
Overseas sales	¥205,930	¥246,829	¥289,451	\$2,334,282
Consolidated sales	¥522,917	¥575,176	¥624,405	\$5,035,524
Percentage of overseas sales over consolidated sales	39.4%	42.9%	46.4%	46.4%

17. Subsequent events

(1) Appropriation of retained earnings

Subsequent to 31st March, 1997, the Company’s Board of Directors, with the subsequent approval of stockholders on 27th June, 1997, declared a cash dividend of ¥1,311 million (\$10,573 thousand) equal to ¥3.75 (\$0.030) per share, applicable to earnings of the year ended 31st March, 1996 and payable to stockholders on the stockholders’ register on 31st March, 1997.

(2) Stock options

At the stockholders meeting held in June 1997, approval was given for the acquisition of treasury stock for the purpose of granting stock options. The amendment to the Articles of Incorporation provides for the acquisition of no more than 722 thousand shares of the Company’s par-value common stock at a cost that shall not exceed ¥2,500 million (US\$20 million).

Consolidated Subsidiaries

Name of Consolidated Subsidiary	Equity Ownership Percentage	Closing Date	Name of Consolidated Subsidiary	Equity Ownership Percentage	Closing Date
Shintech, Inc. ⁽¹⁾	100.0	31st December	Shinkoh Mold Co., Ltd.	100.0	31st March
Shin-Etsu Handotai Co., Ltd.	100.0	31st March	Skyward Information System Co., Ltd.	100.0	31st March
Shin-Etsu Handotai America, Inc. ⁽¹⁾	100.0	31st December	Human Create Co., Ltd.	100.0	31st March
Shin-Etsu Polymer Co., Ltd.	52.5	31st March	Shinano Electric Refining Co., Ltd.	68.7	31st March
Shin-Etsu Astech Co., Ltd.	89.4	31st March	Shin-Etsu Technology Service Co., Ltd.	76.9	28th February
S.E.H. Malaysia Sdn. Bhd. ⁽¹⁾⁽²⁾	100.0	31st December	S.E.H. (Shah Alam) Sdn. Bhd. ⁽¹⁾	100.0	31st December
Naoetsu Electronics Co., Ltd.	90.0	28th February	Shin-Etsu Polymer (Malaysia) Sdn. Bhd. ⁽¹⁾	100.0	31st December
Shin-Etsu Handotai Europe, Ltd. ⁽¹⁾	100.0	31st December	Shincor Silicones, Inc. ⁽¹⁾	100.0	31st December
Shin-Etsu Engineering Co., Ltd.	100.0	31st March	Shin-Etsu Polymer America, Inc. ⁽¹⁾	100.0	31st January
Shin-Etsu Vinyl Acetate Co., Ltd.	51.0	31st March	Shin-Etsu Polymer Europe B.V. ⁽¹⁾	100.0	31st December
Nissin Chemical Industry Co., Ltd.	100.0	28th February	Shin-Etsu Unit Co., Ltd.	100.0	31st December
Silicon Metal Company of Australia Ltd. ⁽¹⁾	100.0	31st December	Polymer East Japan Co., Ltd.	100.0	31st March
Shin-Etsu Silicones of America, Inc. ⁽¹⁾	100.0	31st December	Shinano Polymer Co., Ltd.	100.0	28th February
Shin-Etsu (Malaysia) Sdn. Bhd. ⁽¹⁾	100.0	31st December	Nihon Resin Co., Ltd.	100.0	31st December
Shin-Etsu International Europe B.V. ⁽¹⁾	100.0	31st December	Polymer Chemicals Co., Ltd.	100.0	31st March
Shin-Etsu Electronics Materials Singapore Pte. Ltd. ⁽¹⁾	100.0	31st December	Sanshin Electronics Co., Ltd.	100.0	31st March
Shin-Etsu Kasei Co., Ltd.	100.0	31st March	Saitama Shinkoh Mold Co., Ltd.	100.0	31st March
Shin-Etsu Metallurgical Co., Ltd.	100.0	31st March	Niigata Polymer Company Limited	100.0	31st December
Naoetsu Sangyo Limited	100.0	31st March	San-Ace Co., Ltd.	100.0	28th February
Shin-yo Home Service Company	100.0	31st March	Urawa Polymer Co., Ltd.	100.0	31st January
Shin-Etsu Sealant Co., Ltd.	100.0	31st March	S.E.H. Techno Service Sdn. Bhd. ⁽¹⁾	100.0	31st December
Shin-Etsu Singapore Pte. Ltd. ⁽¹⁾	100.0	31st December	Simcoa Operations Pty. Ltd. ⁽¹⁾	100.0	31st December
Shin-Etsu Delivery Co., Ltd.	100.0	31st March	S.E.H. Urus Khidmat Sdn. Bhd. ⁽¹⁾	100.0	31st December
Shin-Etsu Magnet Co., Ltd.	100.0	31st March	K-Bin, Inc. ⁽¹⁾	100.0	31st December
Shin-Etsu Silicone Korea Co., Ltd. ⁽¹⁾	90.0	31st December	Microsilica Pty. Ltd. ⁽¹⁾	100.0	31st December
Naoetsu Precision Co., Ltd.	100.0	28th February	Simcoa International Pty. Ltd. ⁽¹⁾	100.0	31st December
Shin-Etsu Silicone Taiwan Co., Ltd. ⁽¹⁾	93.3	31st December	Suzhou Shin-Etsu Polymer Co., Ltd. ⁽¹⁾	80.0	31st December

⁽¹⁾ Overseas subsidiary

⁽²⁾ S.E.H. Malaysia Sdn. Bhd. issues non-voting shares.

Report of Independent Certified Public Accountants

To the Board of Directors
Shin-Etsu Chemical Co., Ltd.

We have audited the consolidated balance sheets of Shin-Etsu Chemical Co., Ltd. and its consolidated subsidiaries as of 31st March, 1996 and 1997, and the related consolidated statements of income, stockholders' equity, and cash flows for each of the three years in the period ended 31st March, 1997, all expressed in Japanese yen. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Shin-Etsu Chemical Co., Ltd. and its consolidated subsidiaries as of 31st March, 1996 and 1997, and the consolidated results of their operations and their cash flows for each of the three years in the period ended 31st March, 1997, in conformity with generally accepted accounting principles in Japan applied on a consistent basis.

Tokyo, Japan
27th June, 1997

Chuo Audit Corporation
Chuo Audit Corporation