

To Our Shareholders



Chihiro Kanagawa

President and CEO

In reaching its 80th anniversary in 2006, the Shin-Etsu Group also celebrated the start of a new era. Net sales, operating income, ordinary income and net income all increased substantially to set new records. With operating income and net income each rising by more than 30 percent, the Shin-Etsu Group attained year-on-year growth in profits for the 12th consecutive year in fiscal 2007, which ended on March 31, 2007. As a result, we have been able to double our profits over the past three years.

Our management has achieved these results by taking the offensive with intense aggressive sales and major capital investments in key markets, while assuming a defensive stance through the careful evaluation of every type of business risk and taking steps to control the risks.

To prepare for rapid technological progress and market changes in the semiconductor silicon wafer business, in fiscal 2007 we implemented an unprecedented depreciation system where all the equipment for this business will be depreciated over only three years.

We made another important decision with dividends to be paid to shareholders. The chemical industry is relatively affected by changing market conditions which require constant efforts to minimize their impact. The Shin-Etsu Group's continuous management efforts have included accurately understanding and analyzing current market conditions to forecast the coming market situation when making decisions for business growth, then steadily implementing capital investments and other measures. As a result, the Shin-Etsu Group has generated significant performance gains.

Consequently, for fiscal 2007 we doubled our cash dividends per share from ¥35 in fiscal year 2006 to ¥70 for fiscal year 2007. The per-share amount of cash dividends totaled ¥7.5 for fiscal 1997, meaning dividends are now nearly 10 times greater than they were a decade ago. Furthermore, the Shin-Etsu Group's dividend payments are significantly higher than those of its peer companies in Japan.

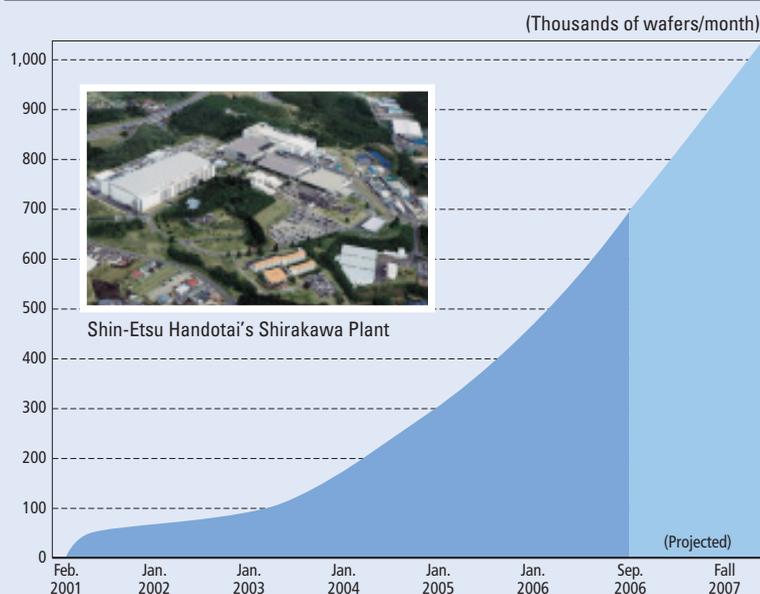
Toward Further Development

Amid concerns about the U.S. economy and raw material price trends, the Shin-Etsu Group must strengthen its existing businesses and develop and commercialize new businesses in order to generate sustained growth. Moreover, we need to solidify both our offensive and defensive stances.

In our existing core businesses, we will further strengthen our world-class technologies, product

Growth in the 300mm Silicon Wafer Business

300mm Wafer Production Capacity



In 2001, Shin-Etsu Handotai Co., Ltd. was the first company in the world to mass produce 300mm wafers. Shin-Etsu Handotai has continued to invest aggressively in this business since then, and expanded production capacity to 700 thousand wafers per month in fall 2006. After considering all the risks, Shin-Etsu Handotai's current plan calls for investing in capacity expansions at its primary Shirakawa Plant, Shin-Etsu Handotai America, Inc., and Group company Mimasu Semiconductor Industry Co., Ltd., in addition to a new investment at Nagano Electronics Industrial Co., Ltd. These investments will promote multiple production bases and help to ensure a stable supply of 300mm wafers to customers. In addition, we will work to disperse risk by increasing existing single-crystal ingot production capacity at the Shirakawa Plant and Shin-Etsu Handotai America, and by initiating production at Shin-Etsu Handotai's Takefu Plant in Fukui Prefecture Japan.

quality and cost competitiveness. While building stable business relationships with numerous customers worldwide, we will keep our organizational structure flexible in order to respond properly and in a timely manner to changing economic conditions.

The Shin-Etsu Group is the world's largest manufacturer of semiconductor silicon. We are rapidly increasing our production capability for 300mm silicon wafers to meet a fast-growing global demand. At the same time, we are increasing our security of supply by placing manufacturing facilities at five different sites in Japan and the United States. The capacity expansions we are implementing will raise our monthly production from 700,000 wafers as of September 2006 to 1 million in the autumn of

2007. In this way, we are fulfilling our duty to our customers as the world's leading supplier of semiconductor silicon.

The Shin-Etsu Group is also the world's largest manufacturer of polyvinyl chloride (PVC). To supply the growing demand in the United States and around the world, our U.S. subsidiary, Shintech Inc., is building a large-scale integrated PVC manufacturing facility that will encompass the entire manufacturing process, from salt electrolysis to PVC resin production. This new plant will further strengthen the Shin-Etsu Group's position as the world's largest PVC producer.

In our manufacturing businesses, it is important to maintain diligent quality control and assure a stable supply in order to deepen the trust of our all-important customers. By ensuring strict quality

Intelligent Investment Drives A New Phase of Growth



Europe

In the cellulose business, Shin-Etsu is investing in additional production facilities at SE Tylose GmbH & Co. KG in Germany as it works to create multiple production and supply bases for specialty cellulose products used in pharmaceuticals and other applications.

Japan

In the semiconductor silicon business, Shin-Etsu is expanding production capacity for 300mm wafers at five production bases in Japan and the U.S. to respond to rising global demand.

United States

In the PVC business, Shintech Inc. in the U.S. is constructing a large-scale plant that is integrated from electrolysis to PVC resin to respond to growing demand in the U.S. and elsewhere in the world.

control that does not let even a single defect slip through and by constantly adhering to delivery schedules, we will further strengthen our relationship of trust with our customers.

In addition, we are taking steps to effectively deal with crude oil prices and other energy costs, which remain at record-high levels. We are coping with this effect by adjusting the prices of our products when appropriate and by securing multiple suppliers of raw materials. At the same time, we are striving to mitigate the economic impact of a possible sharp rise in crude oil prices and energy costs.

For the Shin-Etsu Group to continue growing and prospering in the future, we will pursue business expansion from the medium- and long-term perspectives by making timely investments based on an accurate understanding of current and future customer needs and market trends. Shin-Etsu PVC B.V. in the Netherlands is one good example. We completed the expansion of our PVC production capacity there in 2006. Since then, we have sold out the increased capacity and are now studying the feasibility of a further business expansion.

In the cellulose business, we completed the expansion of our production capacity at SE Tylose GmbH & Co. KG in Germany in 2006 and are now moving forward with the expansion of our business there. Moreover, in view of an accident at the Naoetsu Plant's cellulose production facilities, we have committed ourselves to making an additional facility investment in SE Tylose to ensure multiple production and supply locations for specialty cellulose products used in pharmaceuticals and various other applications.

In the rare earth magnet business, demand is increasing not only for hard-disk drives but also for automobiles and such home appliances as air

conditioners. Since demand for rare earth magnets is growing for diverse applications where low energy consumption and light weight are required, we are carrying out a series of capacity expansions for this business.

When making major investment decisions, it goes without saying that we constantly collect relevant market information. We invest in manufacturing facilities only after fully considering the impact of the investment on profitability and cash flow, but we will not miss out on opportunities to capture growing long-term demand. In addition, we look to the M&A of businesses as another method of expanding our business. Throughout its history, the Shin-Etsu Group has employed mergers and acquisitions to expand its businesses. In 1976, for example, Shintech became a wholly owned subsidiary of Shin-Etsu. In recent years, the Shin-Etsu Group purchased its European PVC and cellulose operations. We will continue to carefully evaluate factors such as the earning potential of M&A candidates as well as their synergy with our existing businesses, and we will energetically execute mergers and acquisitions that can increase corporate value.

Research and Development

R&D is a critical driving force for the Shin-Etsu Group's future business growth. Our R&D centers work tirelessly to develop new products for existing businesses and related peripheral businesses. In developing new products, we aim to create unique products that can set us apart from other companies and that have value customers will recognize. In addition, theme selection is critical to new product R&D. Selecting themes and focusing on them further enhances R&D efficiency, as we work to commercialize new products in the shortest possible time.

Intellectual property, including patents and know-how, is an important business asset. Since many of our research activities culminate in the acquisition of patents, we are working to acquire rights and thereby reinforce the Group's patent administration.

Corporate Governance

In the Shin-Etsu Group, we consistently carry out our management activities with strict legal compliance. We disclose and publicize appropriate information to shareholders, investors and other concerned parties. As part of our efforts to strengthen corporate governance, we have appointed four external directors to Shin-Etsu's 20-member Board of Directors. External directors provide Shin-Etsu not only with independent monitoring and supervision, but also with extensive and valuable advice on overall corporate management. Moreover, three of Shin-Etsu's five statutory auditors are from outside the company. This system enhances and strengthens our auditing function.

One of our external directors chairs the officers' Remuneration Committee, which reviews and evaluates the remuneration for the board members. Shin-Etsu has also established a Risk Management Committee to pinpoint and take preventive measures on the potential risks that could occur during its business operations. Furthermore, the Auditing Department is responsible on a full-time basis for the internal audits of operations as well as the internal controls, and is working to further strengthen corporate governance. From the fiscal year starting April 2008, Japan will introduce its own version of the Sarbanes-Oxley Accounting Reform and Investor Protection Act that was passed in the U.S. To be prepared for this legal change, Shin-Etsu has begun to construct a Group-wide system of internal controls centered on the Auditing Department.

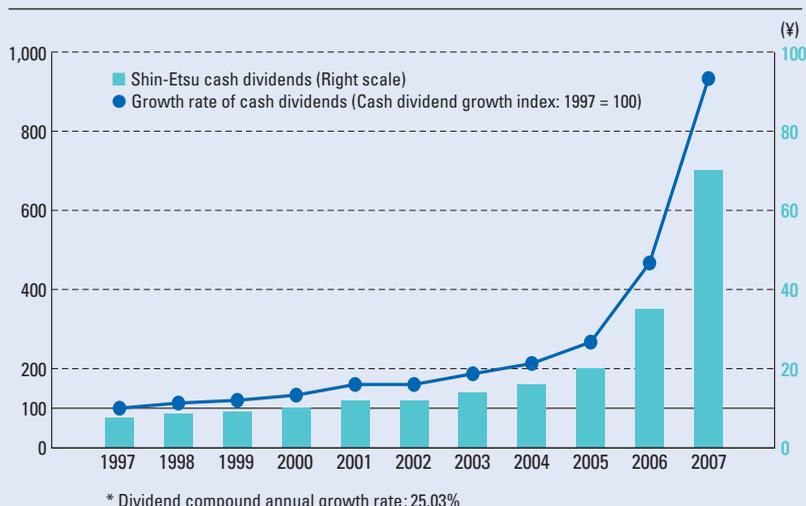
Creating Value for Shareholders

A company belongs to its shareholders. As we continue our management aimed at increasing

Striving to Create Value for Shareholders

Shin-Etsu has strived to create value for shareholders over the past decade. We have increased dividends per share from ¥7.50 for the year ended March 1998 to ¥70.00 for the year ended March 2007. Dividends therefore increased at a compound annual growth rate of over 25 percent. As shown in the chart, Shin-Etsu dividend growth has far outpaced inflation, and as of March 31, 2007, Shin-Etsu's stock price was nearly four times higher than on March 31, 1997.

Real Rate of Dividend Growth



shareholder value, the Shin-Etsu Group communicates with shareholders through such means as investor relations activities, and we also continually seek and listen to the opinions of our investors. We are working to enhance corporate value through the improvement of earnings and performance. The Shin-Etsu Group seeks the understanding and trust of its shareholders, and believes that it must defend corporate value and the profits that belong to shareholders in the event of an attempted acquisition that would not be beneficial to shareholders. The General Meeting of Shareholders held in 2007 approved specific rules in the event of a major acquisition attempt. The Shin-Etsu Group will provide relevant information regarding any such acquisition attempts to shareholders and seek their instructions.

Corporate Social Responsibility (CSR)

We believe that one of the societal responsibilities that a company must fulfill is to make a profit from its operations and pay its taxes while observing each host nation's laws and regulations. In addition, an important task in fostering the sustainable growth of the company is to create a work environment in which employees can perform their jobs effectively and professionally. The Shin-Etsu Group listens carefully to the opinions of the people who work at its plants, research centers and sales divisions. Through dialogues with them we learn many of their ideas and concerns and help deepen their understanding of the Company's management policies. We have implemented a merit-based personnel system under which staff members can fully realize their professional potential. The Shin-Etsu Group has always proactively engaged in corporate social responsibility (CSR) activities. In 2005 we established a CSR Promotion Committee.

We are making strong efforts to promote CSR activities at each location where we have facilities.

On March 20, 2007, an explosion occurred at the Naoetsu Plant's cellulose production facilities. We sincerely apologize to all who were affected by the accident, including local residents, and for the trouble and anxiety it caused. To ensure that such an accident does not happen again, we are redoubling our efforts to prevent a recurrence of any accident and are implementing rigorous safety management measures throughout the Shin-Etsu Group. We will continue to do everything possible to restore trust in the Shin-Etsu Group.

Toward Further Growth

The Shin-Etsu Group puts safety first in all situations and conducts all of its business activities in a fair and ethical manner. We aim to meet the expectations of our shareholders by increasing corporate value with materials and technologies that contribute to economies, industry and society.

In looking forward, we will further strengthen our existing businesses and steadily execute capital investments. Moreover, we will devote extensive resources to new businesses and to the promotion of their rapid development.

As we are challenged by rapidly changing markets, we are committed to managing with the aim of further enhancing corporate value. We would like to express our sincere appreciation for the continued support of and relationship with our stakeholders, our customers and our suppliers.



Chihiro Kanagawa
President and CEO