

Management's Direction

Message from the Chairman



Further strengthening our top global businesses

Chihiro Kanagawa
Chairman

We wish to express our sincere appreciation to all the stockholders for your continued support and long-term view of our company's direction. We are pleased to present the annual report for fiscal 2013, in which you will see our steady progress since fiscal 2010. I would like to take this opportunity to highlight a couple of things.

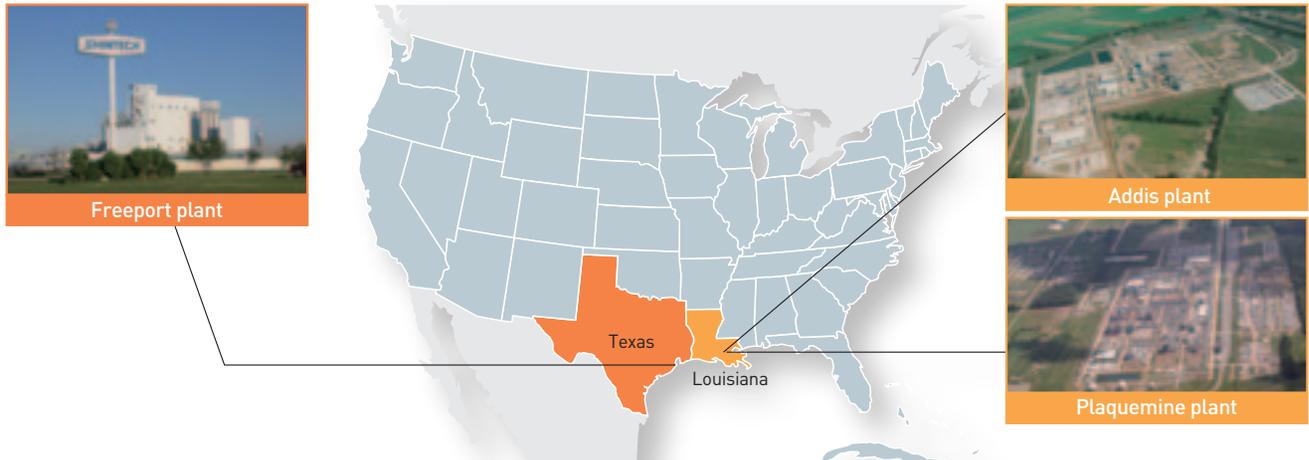
For fiscal 2013, the dynamics of our business portfolio worked again. It was our polyvinyl chloride (PVC) operation in the U.S., namely Shintech. It attained a record income (\$551 million of income before tax, \$371 million of net income), which was more than double that of the last fiscal year. That result contributed significantly to the continued growth in the Shin-Etsu Group's total earnings.

In late 2004, I decided to carry out an investment for the PVC integrated production facilities in the State of Louisiana, U.S. It was the biggest investment in Shin-Etsu Chemical's 80 year history. The total amount invested was \$2.5 billion.

When I made the decision in 2004, the price of natural gas in the U.S. was soaring. Many people believed that the high priced natural gas would continue perpetually and the chemical industries in the U.S. had lost their cost competitiveness. However, I had a different view due to the following perspectives: First, I was confident that the U.S. has the ability to find solutions to the energy issue. In the past, the U.S. was successful in overcoming challenges through its indomitable and pioneering spirit. Second, it is an unwavering policy of mine not to make any major investments in any area where political risks exist.

Frankly, I did not know shale gas back then. I think I can safely say that the U.S. has found a tremendous solution to the energy issue. The U.S. has developed a game-changing technology to extract shale gas. As a result, the price of natural gas in the U.S. dropped significantly, and we started the operation of the new plant at the right time, when U.S. natural gas regained its global competitiveness.

Shintech's U.S. Operations



For fiscal 2013, Shintech's ratio of EBITDA (earnings before interest, tax, depreciation and amortization) to revenue reached 26%, which compares to the average EBITDA margin of 15% among the global specialty chemical industries. While PVC is regarded as a typical commodity, what Shintech delivers is a kind of specialty.

We have several top global businesses. The most notable ones are Shintech's PVC and Shin-Etsu's silicon wafer businesses. However, we should not be complacent with the current position. Our mission is to further strengthen those top global businesses through strong research and development, strong production, nimble sales and wise investments. To give you an example, we recently acquired the total shares held by General Electric Company (GE) of Asia Silicones Monomer Limited, which had been jointly managed by GE and Shin-Etsu. With this acquisition, Shin-Etsu will expand its business in the Asia region by optimizing the efficiency of its silicone business operations in Thailand.

On behalf of the management team and all the employees of the Shin-Etsu Group, I would like to express my appreciation to customers and suppliers, and to thank you, our stockholders, for your investment in the values of our company.

Sincerely yours,

Chihiro Kanagawa
Chairman

Management's Direction

Message from the President



Acting swiftly and producing results

Shunzo Mori
President

Results of operations

In fiscal 2013, net sales decreased 2.1% to ¥1,025,409 million, but earnings were higher mainly because of doubling income at U.S.-based Shintech. Operating income increased 5.0% to ¥157,043 million, and ordinary income increased 3.0% to ¥170,207 million. As a result, earnings were higher for the third consecutive year. Furthermore, the stockholder's equity ratio remained high at 82%.

I would like to introduce the results of the following business segments:

PVC/Chlor-Alkali

Shintech recorded significant growth in sales and earnings, with high volumes of shipments to customers worldwide despite a slow recovery in the U.S. housing market. We would like to deeply thank our Shintech people for their great contributions to the Shin-Etsu Group's earnings.

Semiconductor Silicon

Although the demand for some cutting-edge semiconductor devices, such as smartphones and tablet PCs, remained strong, demand for consumer electronics products such as PCs and flat-panel TVs continued to be slow, and a severe business situation continued.

Silicones

Sales in Japan were firm for product applications in the cosmetics field. However, sales of product applications for electronics equipment generally continued to be slow. On the other hand, in our silicones business outside of Japan, the business was strongly affected by a slump in market prices in the Asian region, such as China.

Electronics and Functional Materials

With regard to the rare-earth magnets businesses, shipments of products for applications in automobiles were strong. The photoresist business continued to be good, and the business of materials for LED packaging continued to be firm. Shipments of optical fiber preform continued to be robust, contributed to by the operations of our new plant in China as well as continued strong demand.

Strategies for sustained growth

As a manufacturer, the Shin-Etsu Group must make capital expenditures in order to continue growing. Over the years, our substantial financial resources have been used for investments in existing and new businesses. I would like to report our capital expenditures in existing businesses during fiscal 2013 herein.

From a geographical point of view, the U.S. is one of the most important locations for the Shin-Etsu Group's investments. Our group company Shintech, the world's largest manufacturer of PVC, has gained extensive

The Shin-Etsu Group's Investments in Asia



experience from operating in the U.S. for 40 years. This experience is a valuable asset not only for Shintech but also for the entire Shin-Etsu Group. It will be extremely beneficial toward making future U.S. investments.

In 2012, the decision was made to build a plant to make hydroxyethyl cellulose (HEC) in Louisiana. HEC is expected to be in increasing demand for the production of coatings for building materials. Construction of the plant started and is scheduled for completion in 2014. With the Group's existing plant in Germany, we will diversify manufacturing operations as well as reinforce our ability to capture the expected growth in demand for HEC.

In Asia, we constructed several production facilities. Two of them, in China and Vietnam, will diversify our procurement of raw materials for rare-earth magnets. Another is for LED packaging materials that will enable us to meet the increasing demand in Asia.

The Shin-Etsu Group is working to develop our innovations into new technologies and products. Two of our new fields for development are energy and health care. In the energy field, we are developing materials for advanced high-capacity lithium ion batteries. In health care, we have made an investment in pharmaceutical venture company NanoCarrier Co., Ltd., in 2012. Shin-Etsu Chemical is applying its cutting-edge technology to joint research for materials to effectively deliver drugs to targeted parts of the body. The Shin-Etsu Group aims to continue growing by developing these and other new businesses while strengthening our existing businesses.

Our ongoing mission

The mission of the Shin-Etsu Group is to strictly comply with all laws and regulations, conduct fair business practices, and contribute to people's daily lives as well as to the advancement of industry and society by providing key materials and technologies. To do this, group companies will further reinforce internal controls and maintain strict compliance. Also, we will continue to carry out our social responsibilities as a chemicals manufacturer while promoting a "safety first" policy among our executives and employees.

The Shin-Etsu Group will continue to pursue higher earnings while fulfilling our social responsibility, and will also keep working to meet our stockholders' expectations by maximizing our corporate value.

Sincerely yours,

Shunzo Mori
President