PROGRESS MADE IN THE FIRST YEAR OF THE “SPROUT PROJECT”

Showa Denko and its Group companies have been carrying out a six-year consolidated business plan that extends from 2000 through 2005. Following the successful completion of the “Cheetah Project,” which focused on restructuring, we launched the “Sprout Project” at the beginning of 2003. Under this newest project, which covers the remaining three-year period, we aim to establish ourselves as a “focused and individualized chemical company” by nurturing and expanding strategic growth businesses.

Basic Strategy
IDENTIFICATION OF 12 SMUs IN THREE MAJOR MARKETS

Through the interconnection of inorganic/aluminum and organic chemical technologies, we will provide even more individualized products that meet customer requirements in the three major target markets of electronics, automotive parts, and personal care/environmental goods.

Specifically, after detailed market analyses, we have identified 12 strategic market units (SMUs)—market segments in which we can expect to achieve high growth by fully utilizing our core technologies—and have begun implementing 12 projects based on these SMUs. Independent of conventional organization, these projects are directly reported to the CEO.

In addition, we have established 27 technology platforms (TPFs) to support these SMUs, accelerate development, and further cultivate core technologies. Engineers assigned to the TPFs are prepared to solve various technical problems pertaining to the SMU projects.

Portfolio Management

We have classified all our businesses into three categories, namely, strategic growth businesses, base businesses, and businesses that need restructuring.

In strategic growth businesses, we will accelerate growth through the SMU approach and preferential allocation of resources.

In base businesses, which support the strategic growth businesses, we will improve profitability by maintaining and strengthening competitiveness.

Regarding the businesses that need restructuring, we will try to rehabilitate these businesses through changes in business models. In some cases, we will make decisions on whether we should curtail or withdraw from operations. Through these measures, we will establish ourselves as an “individualized chemical company” and achieve high profitability.

Major Accomplishments

In 2003, Showa Denko achieved an operating income of ¥38.5 billion, surpassing the target for the first year of the Sprout Project. We have made the following progress in implementing the project:

1. Improvement in our earning power
(1) Higher sales profit ratio
As a result of the drastic restructuring of unprofitable operations under the Cheetah Project and concentration of resources on high-value businesses, the ratio of operating income to net sales increased 1.0 percentage point from the previous year, to 5.6%. In 2005, the last year of the Sprout Project, we intend to further improve this figure, to 7.5%.

(2) Cost reductions
In addition to the cost reductions of around ¥40 billion achieved during the three years of the Cheetah Project, we will be reducing costs by a total of ¥20 billion during the three years of the Sprout Project. In 2003, we achieved cost reductions of ¥10.5 billion.

(3) Expansion and strengthening of strategic growth businesses
In 2003, we made the following announcements concerning major achievements, mainly in the field of electronics:

- Developed a four-element LED with the highest level of brightness in the world
- Established MEFS Co., Ltd., a joint venture with Professor Morinobu Endo of Shinshu University, to conduct research on advanced carbon materials, including carbon nanofibers
- Became the first Japanese company to start the commercial production of C4F6, an advanced dry etching gas that enables semiconductor processing at extremely narrow line widths
- Decided to install a second production line for solid conductive polymer aluminum capacitors
- Expanded the production capacity for ceria-based chemical mechanical polishing (CMP) slurries
- Started sample shipments of titanium oxide paste (SP-X) for use in electrodes of dye-sensitized solar cells

2. Improvement in our consolidated balance sheet

Reduction of debt
We are in the process of achieving our goal of reducing interest-bearing debt to ¥20 billion or less by the end of 2005. The interest-bearing debt at the end of 2003 was ¥527.4 billion, representing a decrease of ¥53.7 billion, or 9.2%, from the previous year-end. We are also aiming to improve the debt/equity ratio to 2.8 times by 2005.

<table>
<thead>
<tr>
<th></th>
<th>2002</th>
<th>2003</th>
<th>2005 (Sprout Project target)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating income/net sales ratio</td>
<td>4.6%</td>
<td>5.6%</td>
<td>7.0%</td>
</tr>
<tr>
<td>ROA (operating income basis)</td>
<td>3.1%</td>
<td>4.1%</td>
<td>5.1%</td>
</tr>
<tr>
<td>Interest-bearing debt</td>
<td>¥521.1 billion</td>
<td>¥527.4 billion</td>
<td>¥200.0 billion</td>
</tr>
<tr>
<td>Debt/equity ratio</td>
<td>3.8 times</td>
<td>3.2 times</td>
<td>2.8 times</td>
</tr>
</tbody>
</table>
3. Segment strategies under the Sprout Project

(1) Petrochemicals
With the enhancement of olefin production efficiency and successful completion of alliances in the areas of plastics and organic chemicals, we will further reduce costs in this segment by Y5 billion by 2005 to improve profitability.

(2) Chemicals
In specialty chemicals, we will develop high-value product lines and launch new products to expand the strategic growth businesses. In base chemicals, one of the base businesses, we will maintain and increase cost-competitiveness to secure a stable source of profit. As part of this move, we are adopting new feedstock for ammonia production.

(3) Electronics
Since this segment represents the most important growth engine for Showa Denko, we will concentrate our resources in this segment to accelerate R&D efforts and expand business.

(4) Inorganic materials
Regarding commodity ceramic products, we will gradually shift production overseas, including to China, to strengthen our cost-competitiveness. In the area of graphite electrodes, we will continue to make cost reductions at our production sites in Japan and the United States to strengthen our earning power.

(5) Aluminum
We will accelerate the growth of high-value product lines through the enhanced allocation of resources. For commodity rolled products and extrusions (both classified as businesses that need restructuring), we will review the present production setup to reduce costs and improve profitability.

4. Accelerated advancement into the Chinese market
In addition to the two subsidiaries in China supporting the Group’s activities in that country, to either increase our own cost-competitiveness or to support customers’ local production, we have established production bases for the following items:
- Semiconductor-processing specialty gas and scrubbers for resulting waste gases: Shanghai
- Unsaturated polyester resin compounds: Shanghai
- Rare earth magnetic alloys: Baotou
- Aluminum cylinders for laser beam printers: Dalian
- Ceramic abrasive grains: Lianyungang

5. Introduction of a new personnel system
We introduced a new personnel system in January 2004 whereby the set annual pay raise system has been abolished and each employee is rewarded according to his/her job accountability and performance.

Showa Denko is committed to fully implementing the strategies under the Sprout Project, thereby realizing its vision and enhancing corporate value.