

LETTER TO SHAREHOLDERS

Matsumoto Yushi-Seiyaku Co., Ltd., has been growing since its establishment in 1939, thanks to the friendly support of our customers. All of our workforce understand the roles of our products, most of which are used behind the scenes of industries, and have always been concentrating on research and study with their best effort. Now we are confident that we have gained the steady reputation, “Matsumoto, the excellent producer of surface active agents.”

Our products are widely employed in various fields including not only textile industries but also non-textile industries, such as automobiles, precision instruments, civil engineering, construction, rubber, plastics, cosmetics, toiletries and agriculture.

We are trying to get in closer business relationship with our customers for grasping their needs more precisely for quicker response.

We gained the certificates of ISO 9001, a quality management standard in 1995 and ISO 14001, an environmental management standard, in 1998. We are concentrating on the optimization of our quality and environmental management systems for satisfying our customers' requirement. We are retaining challenging spirit as a company of venture management for contributing to society.

In this accounting year, Matsumoto Yushi-Seiyaku Co.,Ltd. and its subsidiary (the Group) got results as follows;

The Group managed to achieve ¥23,493 million sales (2.6% increase), and ¥1,900 million of operating income (4.1% decrease). The Group achieved ¥1,753 million of net income (13.9% increase).

It is said that the nation's economy will, at the end of this year, exceed “the Izanagi Boom” which lasted for 57months from 1965 to 1970 with the growth of economy of the BRICs and the wide economic recovery from the capital investment through general consumption. But the volume of products by domestic textile companies was down, because of the production moving overseas and the rising prices of the raw materials due to high prices of the crude oil.

On non-textile industries, the situation continued that companies were inequally affected especially in surfactant industries, and the recovery is delayed because of the high prices of the raw materials and the low prices of the products.

In order to cope with the foregoing domestic economy, our Group developed

high-quality and low-price products. To make sure of earning sales and profit, we worked all the sections closely, and endeavored to analyze the demand from consumer, to develop new products and to save costs of products.

The surfactant division managed to achieve ¥14,967 million sales (2.5% increase), and ¥1,125 million of operating income (12.7% decrease), respectively.

The anionic surfactant segment, because of the sales promotion of the lubricants for the textile overseas, secured ¥3,169 million sales (0.1% decrease).

The nonionic surfactant gained ¥10,907 million sales (3.5% increase) thanks to the sales promotion of new solvents in China.

In the cationic and amphoteric surfactant category, the surfactant for acryl and wool had a hard fight, and so did the amphoteric surfactant use for toiletry. As a result, sales for the year stood at ¥890 million (0.5% decrease).

The other divisions recorded ¥8,525 million of sales (2.9% increase), and ¥775 million of operating income (11.7% increase).

For the high polymer and inorganic chemicals category, the sales of thermo-expansive microcapsules and some other construction materials increased. Sales for the year reached ¥8,525 million (2.9% increase) .

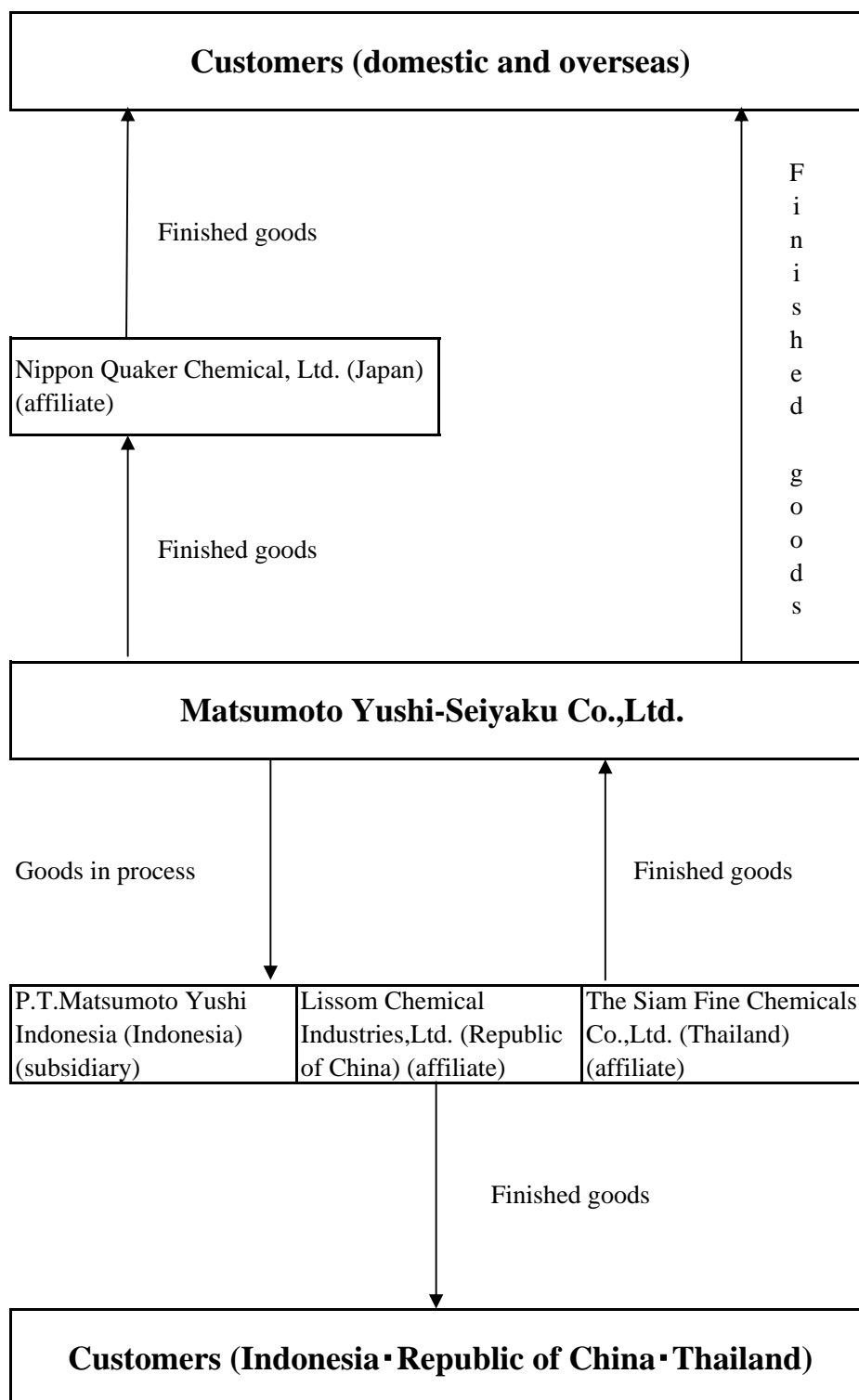
Geographically, the Group achieved in Japan sales of ¥22,740 million (2.4% increase) and the operating income in the amount of ¥1,709 million (12.7% decrease).

In Indonesia, we sold as much as ¥1,029 million (10.3% increase) and managed to get ¥191 million (637.3% increase) on the operating income as a result.

We anticipate a tougher economic and business environment for the next year. Your management is firmly determined to take proactive leadership, as always, through aggressive resources reallocation, further registration of new customers, and enhanced sharing of information with the employees for reinforced awareness of business management.

NAOKI KIMURA
President

Holding Company Configuration and Highlights of Business



MATSUMOTO YUSHI-SEIYAKU CO., LTD**Selected Financial Data**

Years ended March 31

	<u>2006</u>	<u>2005</u>	<u>2004</u>	<u>2003</u>	<u>2002</u>
Results for the year (millions of Yen):					
Net Sales	23,493	22,892	22,352	22,813	22,181
Cost of sales	17,019	16,297	15,416	15,403	14,946
Gross profit	6,475	6,595	6,936	7,409	7,235
Selling, general and administrative expenses	4,574	4,613	4,598	4,574	4,454
Operating income	1,900	1,982	2,338	2,835	2,781
Other income(expenses)	1,053	518	(340)	(1,515)	(324)
Income before income taxes and minority interests	2,953	2,500	1,998	1,320	2,457
Income taxes					
current	1,157	902	978	519	1,028
deferred	(17)	57	(197)	29	84
Minority interests in subsidiary	60	1	84	52	31
Net income	1,753	1,540	1,133	721	1,314
Acquisition of property, plant and equipment	519	528	379	431	480
Depreciation and amortization	480	448	462	493	512
Per share of common stock(Yen):					
Net income	155.06	135.90	99.66	62.30	117.33
Cash dividends	50.00	45.00	40.00	35.00	35.00
Year-end financial position(millions of Yen):					
Total current assets	32,451	22,370	24,801	29,491	30,000
Total investments and other assets	13,453	19,690	16,698	9,757	8,658
Total property, plant and equipment	3,214	3,203	3,136	3,239	3,298
Total current liabilities	7,630	7,797	7,762	6,903	6,865
Total long-term liabilities	1,628	533	842	642	665
Minority interests	147	85	89	113	57
Foreign currency translation adjustments	168	184	186	81	70
Total shareholders' equity	39,713	36,848	35,942	34,828	34,369
Other year-end data:					
Number of shares issued(thousands)	11,282	11,282	11,282	11,282	11,282
Number of shareholders	594	610	680	698	711

MATSUMOTO YUSHI-SEIYAKU CO.,LTD. AND A SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
MARCH 31, 2006 and 2005

ASSETS	Millions of yen		Thousands of U.S.dollars (Note 1)	
	2006	2005	2006	2005
Current assets:				
Cash and cash equivalents	¥ 21,165	¥ 11,302	\$ 180,894	\$ 96,598
Short-term investments (Note 3)	1,262	1,014	10,786	8,665
Notes and accounts receivable:				
Trade	5,132	5,084	43,864	43,450
Associates	1,540	1,386	13,161	11,844
Other	4	29	32	251
	<u>6,676</u>	<u>6,499</u>	<u>57,057</u>	<u>55,545</u>
Inventories (Note 4)	2,900	3,000	24,785	25,645
Deferred income taxes (Note 9)	394	479	3,367	4,096
Other current assets	55	76	467	649
Total current assets	<u>32,451</u>	<u>22,370</u>	<u>277,356</u>	<u>191,198</u>
Property, plant and equipment :				
Land	536	537	4,583	4,587
Building and structures	3,943	3,909	33,704	33,407
Machinery and equipment	8,779	8,787	75,033	75,104
Construction in progress	51	36	435	306
	<u>13,309</u>	<u>13,268</u>	<u>113,756</u>	<u>113,404</u>
Accumulated depreciation	(10,095)	(10,066)	(86,284)	(86,031)
	<u>3,214</u>	<u>3,203</u>	<u>27,472</u>	<u>27,372</u>
Investments and other assets:				
Investments in affiliates (Note 12)	495	502	4,230	4,287
Investments in securities (Note 3)	11,934	18,207	102,002	155,616
Long-term loans, net of allowance for doubtful accounts	448	407	3,826	3,479
Other (Note 8)	576	574	4,923	4,908
	<u>13,453</u>	<u>19,690</u>	<u>114,981</u>	<u>168,290</u>
	<u>¥ 49,118</u>	<u>¥ 45,263</u>	<u>\$ 419,809</u>	<u>\$ 386,859</u>

LIABILITIES AND SHAREHOLDERS' EQUITY	Millions of yen		Thousands of U.S. dollars (Note 1)	
	2006	2005	2006	2005
Current liabilities:				
Short-term bank loans (Note 5)	¥ 900	¥ 1,362	\$ 7,692	\$ 11,645
Accounts payable:				
Trade	4,479	4,603	38,279	39,346
Associates	321	82	2,742	699
Other	889	909	7,597	7,770
Accrued income taxes (Note 9)	678	434	5,791	3,706
Accrued employee bonuses	343	357	2,935	3,049
Other current liabilities	21	50	176	431
Total current liabilities	<u>7,630</u>	<u>7,797</u>	<u>65,213</u>	<u>66,645</u>
Long-term debt (Note 5)	100	—	855	—
Accrued severance indemnities (Note 6)	335	356	2,865	3,042
Deferred income taxes (Note 9)	1,115	98	9,533	840
Other liabilities	77	78	662	670
Total long-term liabilities	<u>1,628</u>	<u>533</u>	<u>13,915</u>	<u>4,553</u>
Total liabilities	<u>9,258</u>	<u>8,330</u>	<u>79,127</u>	<u>71,197</u>
Minority interests	147	85	1,255	724
Contingencies (Note 7)				
Shareholders' equity (Note 2(p)):				
Common stock				
Authorized 21,000,000 shares				
Issued				
2006- 11,281,629 shares	6,090	6,090	52,052	52,052
Capital surplus	6,518	6,518	55,707	55,707
Retained earnings	25,767	24,536	220,230	209,712
Net unrealized holding gains (losses) on securities	1,779	149	15,203	1,271
Foreign currency translation adjustments	(168)	(184)	(1,436)	(1,575)
	<u>39,985</u>	<u>37,108</u>	<u>341,756</u>	<u>317,166</u>
Less, treasury stock, at cost:	(273)	(261)	(2,329)	(2,228)
	<u>39,713</u>	<u>36,848</u>	<u>339,427</u>	<u>314,938</u>
	<u>¥ 49,118</u>	<u>¥ 45,263</u>	<u>\$ 419,809</u>	<u>\$ 386,859</u>

The accompanying notes are an integral part of these statements.

MATSUMOTO YUSHI-SEIYAKU CO.,LTD AND A SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
YEARS ENDED MARCH 31, 2006 and 2005

	Millions of yen		Thousands of U.S. dollars (Note 1)	
	2006	2005	2006	2005
Net sales(Note 10,11)	¥ 23,493	¥ 22,892	\$ 200,798	\$ 195,659
Cost of sales(Note 10)	17,019	16,297	145,458	139,291
Gross profit	6,475	6,595	55,340	56,368
Selling, general and administrative expenses (Note 10)	4,574	4,613	39,097	39,426
Operating income	1,900	1,982	16,243	16,942
Other income (expenses):				
Interest and dividend income	367	256	3,138	2,189
Interest expenses	(30)	(36)	(254)	(309)
Equity in earnings of affiliates	2	45	21	385
Foreign exchange profit (loss)	1,146	178	9,797	1,517
Profit (Loss) on securities sold	(573)	248	(4,896)	2,123
Loss from revaluation of securities	—	(140)		(1,196)
Impairment losses	(14)	—	(118)	
Other, net	153	(33)	1,310	(285)
Income before income taxes and minority interests	2,953	2,500	25,240	21,366
Income taxes (Note 9):				
Current	1,157	902	9,885	7,713
Deferred	(17)	57	(141)	484
Income before minority interests	1,813	1,541	15,497	13,169
Minority interests in subsidiary	(60)	(1)	(510)	(8)
Net income	¥ 1,753	¥ 1,540	\$ 14,987	\$ 13,161

	Yen		U.S. dollars (Note 1)	
	2006	2005	2006	2005
Net income per share:				
Basic	¥ 155.06	¥ 135.90	\$ 1.325	\$ 1.162
Cash dividends per share	50.00	45.00	0.427	0.385

The accompanying notes are an integral part of these statements.

**MATSUMOTO YUSHI-SEIYAKU CO.,LTD AND A SUBSIDIARY
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
YEARS ENDED MARCH 31, 2006 and 2005**

	Number of shares issued (thousands)	Millions of yen					
		Common stock	Capital surplus	Retained earnings	Net unrealized holding gains (losses) on securities	Foreign currency translation adjustments	Treasury stock
Balance at April 1, 2004	11,282	6,090	6,518	23,462	311	(186)	(253)
Net income for the year				1,540			
Net unrealized holding gains on securities					(162)		
Foreign currency translation adjustments						2	
Cash dividends				(448)			
Bonuses to directors and corporate auditors				(18)			
Purchase of treasury stock							(8)
Loss on disposals of treasury stock				(0)			
Balance at March 31, 2005	11,282	6,090	6,518	24,536	149	(184)	(261)
Net income for the year				1,753			
Net unrealized holding gains on securities					1,630		
Foreign currency translation adjustments						16	
Cash dividends				(503)			
Bonuses to directors and corporate auditors				(19)			
Purchase of treasury stock							(12)
Loss on disposals of treasury stock							
Balance at March 31, 2006	<u>11,282</u>	<u>¥ 6,090</u>	<u>¥ 6,518</u>	<u>¥ 25,767</u>	<u>¥ 1,779</u>	<u>¥ (168)</u>	<u>¥ (273)</u>

	Thousands of U.S. dollars (Note 1)					
	Common stock	Capital surplus	Retained earnings	Net unrealized holding gains (losses) on securities	Foreign currency translation adjustments	Treasury stock
Balance at April 1, 2004	\$ 52,052	\$ 55,707	\$ 200,530	\$ 2,660	\$ (1,590)	\$ (2,163)
Net income for the year			13,161			
Net unrealized holding gains on securities				(1,389)		
Foreign currency translation adjustments					14	
Cash dividends			(3,825)			
Bonuses to directors and corporate auditors			(153)			
Purchase of treasury stock						(66)
Loss on disposals of treasury stock			(3)			
Balance at March 31, 2005	\$ 52,052	\$ 55,707	\$ 209,712	\$ 1,271	\$ (1,575)	\$ (2,228)
Net income for the year			14,987			
Net unrealized holding gains on securities				13,932		
Foreign currency translation adjustments					140	
Cash dividends			(4,302)			
Bonuses to directors and corporate auditors			(166)			
Purchase of treasury stock						(101)
Loss on disposals of treasury stock						
Balance at March 31, 2006	<u>\$ 52,052</u>	<u>\$ 55,707</u>	<u>\$ 220,230</u>	<u>\$ 15,203</u>	<u>\$ (1,436)</u>	<u>\$ (2,329)</u>

The accompanying notes are an integral part of these statements.

MATSUMOTO YUSHI-SEIYAKU CO.,LTD AND A SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED MARCH 31, 2006 and 2005

	Thousands of U.S. dollars			
	Millions of yen		(Note 1)	
	2006	2005	2006	2005
Cash flows from operating activities:				
Net income before income taxes and minority interests	¥ 2,953	¥ 2,500	\$ 25,240	\$ 21,366
Adjustments for:				
Depreciation and amortization	480	448	4,100	3,833
Impairment losses	14	—	118	—
Loss(gain) on sales and disposal of property, plant and equipment	8	9	72	74
Loss(gain) on sale and evaluation of securities and other assets	573	(76)	4,896	(648)
Allowance for doubtful accounts	(3)	(2)	(24)	(17)
Equity in earnings of affiliates	(2)	(45)	(21)	(385)
Accrued severance indemnities	(21)	(36)	(177)	(304)
Accrued employee bonuses	(13)	(78)	(114)	(666)
Interest and dividend income	(367)	(256)	(3,138)	(2,189)
Interest expenses	30	36	254	309
Foreign exchange (profit) loss	(1,157)	(240)	(9,889)	(2,053)
Decrease(Increase) in notes and accounts receivable	(102)	(249)	(870)	(2,130)
Decrease(Increase) in inventories	97	(92)	828	(788)
Increase(Decrease) in accounts payable	118	94	1,007	801
Increase (Decrease) in accrued consumption tax	27	(59)	229	(503)
Other,net	8	51	71	436
Sub total	2,642	2,005	22,582	17,135
Interest and dividend income received	362	392	3,090	3,352
Interest expenses paid	(31)	(36)	(265)	(310)
Income taxes paid	(936)	(1,195)	(8,004)	(10,212)
Net cash provided by operating activities	2,036	1,166	17,404	9,966
Cash flows from investing activities:				
Proceeds from maturity of time deposits	110	—	940	—
Receipt from sale of short-term investments	226	30	1,929	255
Payments for purchase of property, plant and equipment	(519)	(528)	(4,439)	(4,516)
Receipt from sale of investments in securities	9,517	4,438	81,342	37,932
Payments for purchase of investments in securities	(1,742)	(6,555)	(14,889)	(56,022)
Decrease(Increase)of long-term loans receivable	4	5	31	39
Other,net	2	1,073	19	9,169
Net cash provided by (used in) investing activities	7,597	(1,538)	64,933	(13,143)
Cash flows from financing activities:				
Increase(Decrease) in short-term bank loans, net	(361)	116	(3,082)	992
Proceeds from long-term debt	100	—	855	—
Repayment of long-term debt	(100)	—	(855)	—
Cash dividends paid	(503)	(448)	(4,302)	(3,825)
Purchase of treasury stock	(12)	(8)	(101)	(68)
Net cash used in financing activities	(876)	(339)	(7,485)	(2,901)
Effect of exchange rate changes on cash and cash equivalents	1,105	104	9,444	889
Net increase (decrease) in cash and cash equivalents	9,863	607	84,296	5,190
Cash and cash equivalents at beginning of year	11,302	11,909	96,598	101,788
Cash and cash equivalents at end of year	¥ 21,165	¥ 11,302	\$ 180,894	\$ 96,598

The accompanying notes are an integral part of these statements.

CORPORATE GOVERNANCE

The Matsumoto Yushi-Seiyaku Group constantly endeavors to achieve the shareholders' maximum interest and the lasting stability of the Group under the management which strongly supports the law and the interest of stakeholders. We believe in an optimum scale of business for timely decisions as well as legal and social compliances.

The directors' meeting is held at least once a month to decide the basic policy and strategy of the Group. In the Group, directors, corporate auditors and the chiefs of department have a meeting once in a week. They check the compliance and the execution of business.

Comprising three Corporate Auditors, of which one is Outside Auditor, Corporate Auditors exchange views, deliberate, and decide on substantive issues relating to auditing. A standing statutory auditor attends other important meetings and watch the management.

Internal Auditing is a corporate function. A team is organized to audit when necessary. The Board of Corporate Auditors and the Independent Auditor may have meetings as need be to exchange opinions.

Seiryō Audit Corporation is contracted as an independent auditor to perform the financial audit in accord with the Commercial Code and Securities Law. The Partners and their assistants of Seiryō Audit Corporation designated to perform the audit for fiscal 2005 were as follows.

Designated partners:

Kazuo Uno, CPA

Hiroshi Takahashi, CPA

Assistants:

The independent auditor forms a team of assistants for performance of the audit in accordance with its audit plan. The team mainly comprises certified public accountants, junior accountants, and others.

MATSUMOTO YUSHI-SEIYAKU CO.,LTD. AND A SUBSIDIARY

Notes to Financial Statements Years Ended March 31, 2006 and 2005

1. Basis of Presenting Consolidated Financial Statements

Matsumoto Yushi-Seiyaku Co.,Ltd.(the "Company") maintains its accounts and records in accordance with the provisions set forth in the Commercial Code of Japan(the "Code") and the Securities and Exchange Law and in conformity with accounting principles and practices generally accepted in Japan, which are different from the accounting and disclosure requirements of International Accounting Standards. Such differences include those relating to inventory valuation at the lower of cost or market value.

The Company's overseas subsidiary maintains its accounts and records in conformity with generally accepted accounting principles and practices prevailing in its country of domicile.

The accompanying consolidated financial statements are prepared based on the consolidated financial statements of the Company and its subsidiary (the "Group") which were filed with the Director of Kanto Local Finance Bureau as required by the Securities and Exchange Law.

In preparing the accompanying consolidated financial statements, certain reclassifications and rearrangements 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.

The translation of the Japanese yen amounts into U.S. dollars is included solely for the convenience of the reader, using the approximate exchange rate at March 31, 2006, which was ¥117 to U.S.\$1.00. These translations for convenience should not be construed as representations that the Japanese yen amounts have been, could have been, or could in the future be, converted into U.S. dollars at this or any other rate of exchange.

2. Summary of Significant Accounting Policies

(a)Consolidation Principles

The consolidated financial statements include the accounts of the Company's subsidiary. All significant inter-company transactions and accounts are eliminated.

Investments in affiliates are accounted for by the equity method whereby the Group includes in net income its share of income or losses of these companies, and records its investments at cost adjusted for its share of income, losses or dividends received.

Generally, companies that are owned more than 50% fall under the category of subsidiaries and companies that are owned 20% or more but not more than 50% fall under the category of affiliates, respectively.

However, companies that are owned 40% to 50% may also fall under the category of subsidiaries and companies that are owned 15% or more but not more than 20% may also fall under the category of affiliates, respectively, if the Company substantially controls the investees' management or has significant influence and relationship with the investees.

(b)Translation of Foreign Currencies

Foreign currency receivables and payables are translated into Japanese yen at the exchange rates in effect on the balance sheet date, and translation gains or losses are charged to income in the year incurred.

Assets, liabilities, revenue and expenses of overseas subsidiary are translated into Japanese yen at the exchange rates in effect on balance sheet date and shareholders' equity is translated into Japanese yen at historical rates. Differences arising from translation are presented as "Minority interests" and "Foreign currency translation adjustments" in the accompanying consolidated balance sheets.

(c) Consolidated Statement of Cash Flows

For the purposes of cash flow statements, cash and cash equivalents comprise cash on hand, deposits held at call with banks, net of overdrafts and all highly liquid investments with maturities of three months or less.

(d) Short-term Investments and Investments in Securities

In accordance with the Accounting Standards for Financial Instrument, securities should be classified into four categories: trading securities, held-to-maturities securities, equity investments in affiliates and other securities. Equity and debt securities are classified as other securities.

Marketable equity and debt securities are stated at fair value with unrealized gains and losses, net of applicable income taxes, reported as a separate component of shareholders' equity. Gains and losses are credited or charged to income when realized, with cost determined by the weighted average method.

However, if the fair value falls below 50% of cost and if there is no prospect of recovery, the unrealized losses have to be charged to income. The Company charged ¥140 million (U.S.\$ 1,196 thousand) to income as loss from revaluation of securities in the fiscal year ended on March 31, 2005.

Other securities without readily determinable fair value are stated at weighted average cost.

Investments in securities include ¥2,757 million (U.S.\$23,564 thousand) and ¥2,757 million (U.S.\$23,565 thousand) of investment for Limited Liability Partnership of Investments on March 31, 2006 and 2005 respectively, because of the revision of the Securities and Exchange Law.

(e) Golf Club Membership

In accordance with the Accounting Standards for Financial Instruments, an impairment loss on deposits for golf club membership is required to be recognized when fair value is extremely lower than the cost.

The Company charged ¥ 33 million (U.S.\$ 279 thousand) to income in the fiscal year ended on March 31, 2005.

(f) Inventories

Finished products, work in process and purchased merchandise are stated at cost determined by the weighted average method. Raw materials are stated at the lower of weighted average cost or market value. Supplies and containers are stated at the most recent purchase prices.

The Company recorded loss on reduction of inventory amounting to ¥7 million (U.S.\$64 thousand) in the fiscal year ended on March 31, 2006.

(g) Property, Plant and Equipment

Property, plant and equipment are stated at cost. Depreciation is principally computed by the declining-balance method based on the estimated useful lives of the respective assets same as determined by Japanese Income Tax Law.

Costs of maintenance, repairs and minor renewals are charged to expenses in the year

incurred, although major renewals and improvements are capitalized.

Effective April 1, 1998, the Company adopted the straight line method of depreciation for buildings, which, previously, had been depreciated by the declining-balance method. This change was made owing to revision of Japanese Income Tax Law.

The company has adopted the new accounting standard for impairment of fixed assets since the year ended on March 31, 2006. The Company recorded impairment losses of ¥14 million (U.S.\$118 thousand) in the fiscal year ended on March 31, 2006. (Note 15)

(h) Intangible Assets

Amortization of intangible assets is computed by the straight-line method. Computer software is recorded as intangible assets as per the Securities and Exchange Law in Japan.

(i) Accrued Severance Indemnities

In accordance with the Accounting Standards for Retirement Benefit accrued severance indemnities are provided based on the amount of projected benefit obligation reduced by pension plan assets at fair value at the end of the period.

Employees' retirement benefits, covering employees of the Company, are provided through unfunded lump-sum benefit plans and funded noncontributory pension plans. Under the plans, eligible employees are entitled, under most circumstances, to severance payments based on compensation at the time of severance and year of service.

The Company records such accrued severance indemnities as at March 31. Yet its subsidiary does not record such accrued severance indemnities.

Actuarial losses shall be amortized over five years beginning with the next year.

(j) Research and Development and Computer Software

Research and development expenditure is charged to income when incurred.

Expenditure relating to computer software developed for internal use is charged to income when incurred. When it contributes to the generation of income or to future cost savings, such expenditure is capitalized as an asset and is amortized using the straight-line method over its estimated useful life, namely, 5 years.

(k) Allowance for Doubtful Accounts

In accordance with the Accounting Standards for Financial Instruments, allowance for doubtful accounts is provided by actual bad debt expense ratio to normal receivables and by specific examination of collectibility to bad debt.

(l) Consumption Tax

The consumption tax is imposed at the flat rate of 5% on the Company's sales to customers and purchases of goods and services. The consumption tax thus withheld on sales and paid on purchases by the Company is not included in the amounts of revenue and expense items. Under the consumption tax law, the tax paid on purchases can generally be deducted from the tax withheld.

(m) Accrued Employee Bonuses

As a general practice in Japan, bonuses are normally payable to employees in early summer and early winter covering the first and second half of the year, respectively. The Company records such accrued bonus liabilities as at March 31. Yet its subsidiary does not record

such accrued bonuses liabilities.

(n)Income Taxes

Deferred tax assets and liabilities are determined based on the differences between financial statements and the tax bases of the assets and liabilities and are measured using the enacted tax rates and laws which will be in effect when the differences are expected to be settled.

(o)Per Share Information

The computation of basic net income per share is based on net income available to common shareholders and the weighted average number of shares of common stock outstanding during each period. The average number of shares used in the computation was 11,184 thousand and 11,188 thousand for the periods ended March 31, 2006 and 2005, respectively.

Cash dividends per share shown in the statements of income are the amounts applicable to the respective years.

(p)Shareholders' Equity

Under the Code, at least 50% of the issue price of new shares is required to be designated as stated common stock.

The portion which is to be designated as stated common stock is determined by resolution of the Board of Directors. Proceeds in excess of the amounts designated as stated common stock are to be credited to capital surplus.

Under certain circumstances specified by the Code, the Company may issue upon approval of the Board of Directors, new shares of its common stock to existing shareholders. As the Code has been amended, from October 1, 2001, the Company may reduce capital surplus and legal retained earnings to 25% of stated common stock by approval of shareholders at a general meeting.

3. Short-term Investments and Investments in Securities

Short-term investment at March 31, 2006 and 2005 consisted of the following:

	Millions of yen		Thousands of U.S. dollars(Note 1)
	2006	2005	2006
Other securities:			
Bonds and debentures	¥ 432	¥ 74	\$ 3,692
Time deposits	830	940	7,094
	<u>¥ 1,262</u>	<u>¥ 1,014</u>	<u>\$ 10,786</u>

The following is a summary of other securities at March 31, 2006 and 2005 respectively:

Millions of yen				
March 31, 2006				
Other securities				
Cost	Gross unrealized gains	Gross unrealized losses	Book Value (Estimated fair value)	
Equity securities	¥ 2,689	¥ 3,308	¥ (12)	¥ 5,985
Bonds and debentures	300	132	-	432
Other	3,062	113	-	3,175
	<u>¥ 6,051</u>	<u>¥ 3,553</u>	<u>¥ (12)</u>	<u>¥ 9,592</u>
Less:Short-term investments				(432)
Add:Securities without readily determinable fair value				2,774
				<u>¥ 11,934</u>

Millions of yen				
March 31, 2005				
Other securities				
Cost	Gross unrealized gains	Gross unrealized losses	Book Value (Estimated fair value)	
Equity securities	¥ 2,713	¥ 1,454	¥ (67)	¥ 4,100
Debt securities	549	31	(0)	580
Other	8,409	7	(1,137)	7,279
	<u>¥ 11,671</u>	<u>¥ 1,492</u>	<u>¥ (1,204)</u>	<u>¥ 11,959</u>
Less:Short-term investments				(74)
Add:Securities without readily determinable fair value				6,322
				<u>¥ 18,207</u>

Thousands of U.S.dollars(Note 1)				
March 31, 2006				
Other securities				
Cost	Gross unrealized gains	Gross unrealized losses	Book Value (Estimated fair value)	
Equity securities	\$ 22,980	\$ 28,274	\$ (100)	\$ 51,154
Debt securities	2,564	1,128	-	3,692
Other	26,175	959	-	27,134
	<u>\$ 51,719</u>	<u>\$ 30,361</u>	<u>\$ (100)</u>	<u>\$ 81,980</u>
Less:Short-term investments				(3,692)
Add:Securities without readily determinable fair value				23,714
				<u>\$ 102,002</u>

4. Inventories

Inventories at March 31, 2006 and 2005 comprise the following:

	Millions of yen		Thousands of U.S. dollars(Note 1)
	2006	2005	2006
Finished goods	¥ 1,516	¥ 1,585	\$ 12,958
Work in process	289	297	2,471
Raw materials and supplies	1,095	1,118	9,357
	<u>¥ 2,900</u>	<u>¥ 3,000</u>	<u>\$ 24,785</u>

5. Short-term Bank Loans and Long-term Debt

The annual average interest rates applicable to short-term bank loans at March 31, 2006 is 0.66%

Long-term debt at March 31, 2006 and 2005 consisted of the following respectively:

	Millions of yen		Thousands of U.S. dollars(Note 1)
	2006	2005	2006
Loans from banks:			
Unsecured loans, maturing in 2009	¥ 100	¥ 100	\$ 855
Total	¥ 100	¥ 100	\$ 855
Less: current portion	-	100	-
Long-term debt, less current portion	<u>¥ 100</u>	<u>¥ -</u>	<u>\$ 855</u>

Aggregate annual maturities of long-term debt subsequent to March 31, 2006 are as follows:

Year ending March 31	Millions of yen	Thousands of U.S. dollars
<u>2009</u>	<u>¥ 100</u>	<u>\$ 855</u>
	<u>¥ 100</u>	<u>\$ 855</u>

6. Accrued Severance Indemnities

The following tables set forth the changes in benefit obligation, and plan assets of the Company at March 31, 2006 and 2005 respectively:

	Millions of yen		Thousands of U.S. dollars(Note 1)
	2006	2005	2006
Benefit obligation at end of years	¥ (1,679)	¥ (1,804)	\$ (14,349)
Fair value of plan assets at end of years	<u>1,414</u>	<u>1,325</u>	<u>12,085</u>
Benefit obligation in excess of plan assets	(265)	(479)	(2,265)
Unrecognized actuarial loss	<u>(70)</u>	<u>123</u>	<u>(600)</u>
Accrued severance indemnities	<u>(335)</u>	<u>(356)</u>	<u>(2,865)</u>

Benefit expenses of the Company included the following components for the year ended March 31, 2006 and 2005 respectively:

	Millions of yen		Thousands of U.S. dollars(Note 1)
	2006	2005	2006
Service cost	¥ 76	¥ 76	\$ 711
Interest cost	29	32	298
Expected return on plan assets	(46)	(26)	(241)
Amortization:Actuarial losses	62	48	447
Benefit expenses	<u>¥ 121</u>	<u>¥ 130</u>	<u>\$ 1,215</u>

Assumption used in the accounting for the defined benefit plans for the year ended March 31, 2006 and 2005 is as follows:

	2006	2005
Method of attributing benefit to periods of service	straight-line basis	straight-line basis
Discount rate	1.8%	1.8%
Long-term rate of return on fund assets	3.5%	2.0%
Amortization period for actuarial losses	5years	5years

7. Contingencies

The Group was contingently liable as guarantor of indebtedness of affiliates for ¥300 million (U.S.\$2,568 thousand) and ¥203 million (U.S.\$1,738 thousand) at March 31, 2006 and 2005 respectively.

8. Research and Development and Computer Software

Research and development expenditure charged to income was ¥1,232 million(U.S.\$10,533 thousand) and ¥1,241 million(U.S.\$10,603 thousand) for the year ended March 31, 2006 and 2005, respectively.

Capitalized expenditure for the development of computer software was as follows:

	Millions of yen		Thousands of U.S. dollars(Note 1)
	2006	2005	2006
Balance of beginning of year	¥ 7	¥ 7	\$ 63
Additions	7	3	59
Amortization	(3)	(3)	(29)
Balance at end of year	<u>¥ 11</u>	<u>¥ 7</u>	<u>\$ 93</u>

9. Income taxes

The Company is subject to several taxes based on income, which in the aggregate resulted in statutory tax rates of approximately 40.7% for the years ended March 31, 2006 and 2005. Foreign subsidiary is subject to income taxes of the country in which it operates.

The effective rate for the two years ended March 31, 2006 and 2005 differs from the Company's statutory tax rate for the following reasons:

	2006	2005
Statutory tax rate	40.7	40.7
Permanently nondeductible expenses	1.4	1.6
Permanently nontaxable dividends received	(0.4)	(0.5)
Per capital levy of residents tax	0.5	0.5
Tax on undistributed profits	1.4	1.4
Difference of tax rate of overseas subsidiary	(0.6)	-
Tax credit on research and development	(4.2)	(4.6)
Other	(0.2)	(0.7)
Effective tax rate	<u>38.6</u>	<u>38.4</u>

The significant components of deferred tax assets and deferred tax liabilities at March 31, 2006 and 2005 are presented below:

	Millions of yen		Thousands of U.S. dollars(Note 1)
	2006	2005	2006
Gross deferred tax assets:			
Accrued severance indemnities	¥ 136	¥ 130	\$ 1,166
Accrued employee bonuses	140	145	1,194
Accrued enterprise tax	59	44	505
Over-depreciation	3	6	29
Unrealized gains on inventories	18	18	158
Net unrealized holding losses on securities	55	55	468
Other	88	85	749
Total gross deferred tax assets	<u>499</u>	<u>483</u>	<u>4,269</u>
Gross deferred tax liabilities:			
Net unrealized holding profits on securities	1,221	102	10,434
Total gross deferred tax liabilities	<u>1,221</u>	<u>102</u>	<u>10,434</u>
Net deferred tax assets(liabilities)	<u>(721)</u>	<u>381</u>	<u>(6,166)</u>

In assessing the realizability of deferred tax assets, management of the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is entirely dependent upon the generation of future taxable income in specific tax jurisdictions during the period in which those temporary differences become deductible.

10. Segment Information

Information about operations in industry segments, geographic segments and sales to foreign customers of the Group for the years ended March 31, 2006 and 2005, is as follows respectively:

(1) Industry Segments

a. Sales and Operating Income

	Millions of yen				
	2006			Eliminations/ Corporate	Consolidated
Surfactant	Other	Total	-		
Sales to customers	¥ 14,967	¥ 8,526	¥ 23,493	¥ -	¥ 23,493
Intersegment	-	-	-	-	-
Total sales	14,967	8,526	23,493	-	23,493
Operating expenses	13,842	7,751	21,593	-	21,593
Operating income	<u>¥ 1,125</u>	<u>¥ 775</u>	<u>¥ 1,900</u>	<u>¥ -</u>	<u>¥ 1,900</u>

Millions of yen					
2005					
	Surfactant	Other	Total	Eliminations/ Corporate	Consolidated
Sales to customers	¥ 14,603	¥ 8,289	¥ 22,892	¥ -	¥ 22,892
Intersegment	-	-	-	-	-
Total sales	14,603	8,289	22,892	-	22,892
Operating expenses	13,315	7,595	20,910	-	20,910
Operating income	¥ 1,288	¥ 694	¥ 1,982	¥ -	¥ 1,982

Thousands of U.S.dollars					
2006					
	Surfactant	Other	Total	Eliminations/ Corporate	Consolidated
Sales to customers	\$ 127,926	\$ 72,872	\$ 200,798	\$ -	\$ 200,798
Intersegment	-	-	-	-	-
Total sales	127,926	72,872	200,798	-	200,798
Operating expenses	118,310	66,245	184,555	-	184,555
Operating income	\$ 9,616	\$ 6,627	\$ 16,243	\$ -	\$ 16,243

b. Assets, Depreciation and Capital Expenditure

Millions of yen					
2006					
	Surfactant	Other	Total	Eliminations/ Corporate	Consolidated
Assets	¥ 12,577	¥ 7,111	¥ 19,688	¥ 29,430	¥ 49,118
Depreciation	307	173	480	-	480
Impairment Losses	-	14	14	-	14
Capital expenditure	341	185	526	-	526

Millions of yen					
2005					
	Surfactant	Other	Total	Eliminations/ Corporate	Consolidated
Assets	¥ 10,919	¥ 6,304	¥ 17,223	¥ 28,040	¥ 45,263
Depreciation	284	164	448	-	448
Capital expenditure	343	188	531	-	531

Thousands of U.S.dollars					
2006					
	Surfactant	Other	Total	Eliminations/ Corporate	Consolidated
Assets	\$ 107,494	\$ 60,780	\$ 168,275	\$ 251,534	\$ 419,809
Depreciation	2,625	1,475	4,100	-	4,100
Impairment Losses	-	118	118	-	118
Capital expenditure	2,915	1,583	4,499	-	4,499

Notes: Surfactant consists of Spinning lubricants for artificial fibers, Sizing lubricants for spun yarn weaving, Antistatic agents for spinning and finishing. Other consists of Warp sizes for spun yarn weaving, Touch improvers.

(2)Geographic Segments

The domestic and foreign operations of the Group for the years ended March 31, 2005 and 2004 are summarized as follows:

	Millions of yen				
	2006				
	Japan	Indonesia	Total	Eliminations/ Corporate	Consolidated
Sales to customers	¥ 22,507	¥ 987	¥ 23,493	¥ -	¥ 23,493
Intersegment	234	43	277	(277)	-
Total sales	22,741	1,030	23,770	(277)	23,493
Operating expenses	21,031	838	21,869	(276)	21,593
Operating income	¥ 1,710	¥ 192	¥ 1,901	¥ (1)	¥ 1,900
Assets	¥ 19,290	¥ 600	¥ 19,890	¥ 29,227	¥ 49,118

	Millions of yen				
	2005				
	Japan	Indonesia	Total	Eliminations/ Corporate	Consolidated
Sales to customers	¥ 21,983	¥ 909	¥ 22,892	¥ -	¥ 22,892
Intersegment	226	24	250	(250)	-
Total sales	22,209	933	23,142	(250)	22,892
Operating expenses	20,250	907	21,157	(247)	20,910
Operating income	¥ 1,959	¥ 26	¥ 1,985	¥ (3)	¥ 1,982
Assets	¥ 16,782	¥ 632	¥ 17,414	¥ 27,849	¥ 45,263

	Thousands of U.S.dollars				
	2006				
	Japan	Indonesia	Total	Eliminations/ Corporate	Consolidated
Sales to customers	\$ 192,365	\$ 8,432	\$ 200,798	\$ -	\$ 200,798
Intersegment	1,997	368	2,365	(2,365)	-
Total sales	194,362	8,800	203,162	(2,365)	200,798
Operating expenses	179,748	7,165	186,912	(2,358)	184,550
Operating income	\$ 14,614	\$ 1,635	\$ 16,250	\$ (7)	\$ 16,243
Assets	\$ 164,875	\$ 5,129	\$ 170,004	\$ 249,805	\$ 419,809

(3)Sales to Foreign Customers

Sales to foreign customers for the years ended March 31, 2006 and 2005 are as follows:

	Millions of yen		
	2006		
	South-east Asia	Other	Total
Sales to foreign customers (A)	¥ 7,862	¥ 960	¥ 8,822
Total sales (B)	-	-	23,493
(A)/(B)	33.5%	4.1%	37.6%

	Millions of yen		
	2005		
	South-east Asia	Other	Total
Sales to foreign customers (A)	¥ 7,275	¥ 1,152	¥ 8,427
Total sales (B)	-	-	22,892
(A)/(B)	31.8%	5.0%	36.8%

	Thousands of U.S.dollars		
	2006		
	South-east Asia	Other	Total
Sales to foreign customers (A)	\$ 67,199	\$ 8,206	\$ 75,405
Total sales (B)	-	-	200,798
(A)/(B)	33.5%	4.1%	37.6%

11. Related Party Transactions

Principal transactions between the Company and its affiliates for the years ended March 31, 2006 and 2005 are summarized as follows:

	Millions of yen		Thousands of U.S.dollars
	2006	2005	2006
	¥	¥	\$
Sales(Nippon Quaker Chemical,Ltd.)	3,438	3,182	29,388

12. Subsidiary

The Company's subsidiary is as follows:

Name	Ownership Interest	Country of Incorporation
P.T.Matsumoto-Yushi Indonesia	49%	Indonesia

13. Subsequent Event

The following appropriations of the Company's retained earnings in respect of the year ended March 31, 2006 were proposed by the Board of Directors and approved by the shareholders at the annual general meeting held on June 28, 2006:

Appropriations	Millions of yen	Thousands of U.S.dollars
	¥	\$
Cash dividends (¥50.0 per share)	559	4,779
Bonuses to directors and corporate auditors	19	164
Total appropriations	578	4,943

14. Net income Per Share

	Millions of yen		Thousands of U.S dollars
	2006	2005	2006
	¥	¥	\$
Net income	1,753	1,540	14,987
Deduction			
Bonuses to directors and corporate auditors	19	19	164
Net income available to common shareholders	1,734	1,520	14,822
	Thousand Shares		
	2006	2005	
The weighted average number of shares of common stock outstanding	11,184	11,188	
	yen		U.S.dollars
	2006	2005	2006
Net income per share	¥ 155.06	¥ 135.90	\$ 1,325.30

15. Impairment Losses

The Group's assets for business use are grouped by shop. Assets that are currently idle and unsehduled in business use are grouped as idle assets. Properties for lease are grouped by each property. The Group reviews its fixed assets for impairment whenever events or changes in circumstance indicate that the carrying amount of an assets or asset group may not be recoverable. An impairment loss would be recognized if the carrying amount of an assets or assets group exceeds the sum of the undiscounted future cash flow expected to result from the continued use and eventual dispositionn of an assets or asset group. The impairment loss would be measured as the amount by which the carrying amount of the asset exceeds its recoverable amounts which is net sales value. Net sales value is zero as assessed assets group cannot be sold.

Use	Location(Prefecture)	Type of assets
For production of inorganic product	Yao(Osaka)	Machinary and equipment

Impairment losses for the year ended March 31, 2006 was as follows:

	Millions of yen	Thousands of U.S.dollars
	<u>¥ 14</u>	<u>\$ 118</u>