Kao Corporation



Key Drivers for Profitable Growth: Brand Equity, Superior R&D and TCR

Annual Report 2001

For the year ended March 31, 2001

Profile

Kao Corporation has served the needs of consumers for more than a century. Kao is one of the leading companies in Japan for personal care products, cosmetics, laundry and cleaning products, hygiene products, and functional food products.

The Company has also earned a reputation as a quality manufacturer of chemical products. Committed to a global approach to business, Kao has operations in 26 countries in Asia, North America, Europe and other parts of the world.

Contents

Financial Highlights

Kao Corporation and Consolidated Subsidiaries — Years ended March 31, 2001, 2000 and 1999

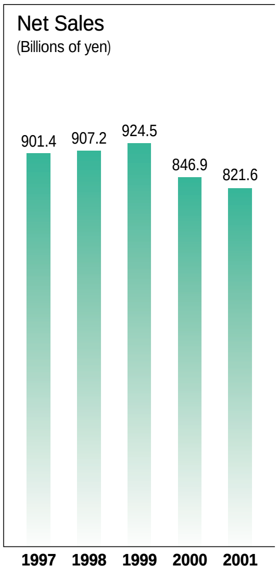
	Billions of yen			Millions of U.S. dollars	Change
	2001	2000	1999	**2001**	**2001**/2000
For the year:					
Net sales	**¥821.6**	¥846.9	¥924.5	**$6,631.4**	(3.0)%
Consumer Products	**607.8**	632.4	656.1	**4,905.8**	(3.9)
Cosmetics *Sofina*	**72.5**	70.8	74.4	**585.8**	2.4
Chemical Products	**167.8**	172.4	193.9	**1,355.1**	(2.6)
Subtotal	**848.2**	875.7	924.5	**6,846.6**	(3.1)
Eliminations	**(26.6)**	(28.7)	–	**(215.2)**	–
Net income	**59.4**	52.1	34.7	**479.6**	14.0
At year-end:					
Total assets	**¥783.7**	¥750.0	¥751.7	**$6,325.7**	4.5%
Total shareholders' equity	**462.9**	474.9	451.7	**3,736.8**	(2.5)
	Yen			U.S. dollars	Change
Per share:					
Net income	**¥ 96.69**	¥ 83.45	¥ 55.98	**$0.78**	15.9%
Cash dividends	**24.00**	20.00	16.00	**0.19**	20.0
Total shareholders' equity	**760.05**	765.59	727.01	**6.13**	(0.7)

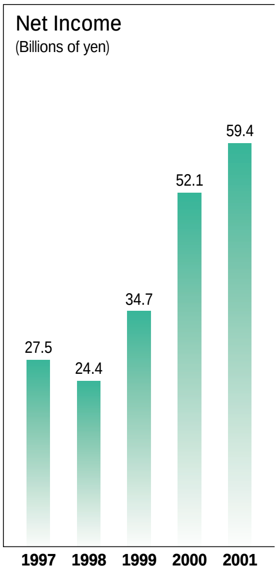
Notes: 1. The U.S. dollar amounts are translated, for convenience only, at the rate of ¥123.90=US$1, the approximate exchange rate at March 31, 2001.

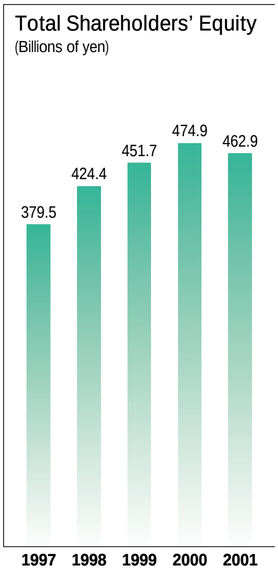
2. Net sales by business segment include intersegment sales starting from the year ended March 31, 2000 as defined in the notes to consolidated financial statements (Note 12). Consequently, net sales of Chemical Products include intersegment sales to Consumer Products and Cosmetics *Sofina*.

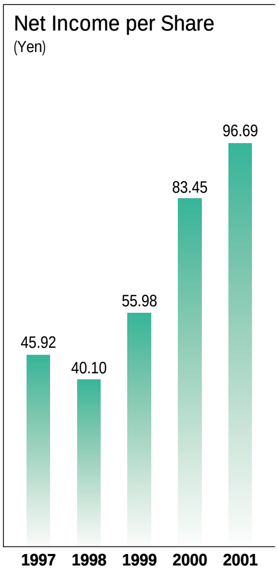
3. Net income per share is computed based on the weighted average number of shares outstanding during the respective years.

4. Cash dividends per share are the amounts applicable to the respective years, including dividends to be paid after the end of the year.









Message from the President

I am pleased to report that Kao continued to generate earnings growth in fiscal 2000, the year ended March 31, 2001. The Company achieved record net income for the third consecutive year, while posting record high operating income exceeding ¥100 billion for the first time. Our focus on core businesses and on building a solid foundation for consistent earnings growth is resulting in higher corporate value.

Kao achieved solid results despite the challenges we faced in our primary market of Japan, where price deflation continued. Two factors negatively affected sales compared with fiscal 1999: the impact of the strong yen and the effect of the consolidation of our domestic consumer products sales company. Consequently, consolidated net sales decreased 3.0 percent to ¥821.6 billion (US$6,631.4 million). Absent these factors, consolidated net sales would have increased 0.6 percent. Earnings benefited from new product introductions, the continuing success of Total Cost Reduction (TCR) activities and decreased depreciation expenses, while falling sales prices and increased pension expenses adversely affected earnings. Moreover, although the strong yen reduced overseas sales, the profitability of Kao's overseas operations improved. Operating income therefore increased 8.0 percent to ¥107.0 billion (US$864.4 million), and represented 13.0 percent of net sales, up 1.3 percentage points from 11.7 percent for fiscal 1999. Net income rose 14.0 percent to ¥59.4 billion (US$479.6 million) due to the increased operating income, foreign exchange gains and a decrease in restructuring charges. As a result, EVA® (Economic Value Added)* improved for the second consecutive year since its implementation. In view of these results, the Company has decided to increase annual dividends to shareholders by ¥4.00, to ¥24.00 (US$0.19) per share, the eighth consecutive increase in annual cash dividends.

Management Strategies Geared to Growth

The prolonged recession in Japan has changed consumer purchasing patterns. Consumers are buying only what they really need or want, and as a result, sales volume has been flat or decreased slightly. At the same time, excess capacity of retailers and more intense competition from our peer companies have led to continued downward pricing pressure. The overall market size of our industry has therefore decreased in yen terms. In response to these difficult conditions, Kao has implemented a number of management initiatives geared to embracing market realities, offering powerful brands backed by its unique, innovative technologies, and finding new ways to generate growth. Results from the past fiscal year once again reflect our success in achieving earnings growth. Our continuing efforts center on three core capabilities: understanding consumers' real needs and wants; efficiently applying research and development expertise; and effectively marketing our own products. Our success at raising market share, concurrently building our position in existing markets while creating new ones, attests to the effectiveness of our drive to consistently meet and exceed consumer expectations.

Reinforcing Core Businesses

Kao concentrates on its core competencies in consumer products, cosmetics and chemical products, where it deploys its technological strengths to increase brand equity and customer trust while systematically improving operating efficiency. Operations in Japan generate 79 percent of sales and 88 percent of operating income. Therefore, it is essential for us to build stronger domestic operations as the foundation for profitable growth, while we pursue global expansion. Since the 1960s, Kao has worked to improve domestic logistics, as an organic system encompassing purchasing, production, sales and distribution. During fiscal 2000, Kao moved to increase the effectiveness of its supply chain management program, while introducing functional, value-added products in the consumer products and cosmetics businesses. New product introductions included *Attack Sheet-type* compact laundry detergent, *Humming 1/3 Anti-bacterial Plus* fabric softener and *est*, a cosmetics brand designed specifically for the department store segment. Several new and improved products were also added to the *Bioré* brand. In the chemical products business, Kao continued to work to further strengthen fatty

* EVA is a registered trademark of Stern Stewart & Co.

chemicals operations, while increasing sales of such specialty chemicals as copier and printer toner and related products, and aroma chemicals.

New Business Development

New business development during fiscal 2000 also made a positive contribution. Our presence in the health care market, including functional food products, over-the-counter drugs and nursing care products, carries outstanding potential and is developing smoothly in Japan. The success of *Healthy Econa Cooking Oil – For Prevention of Fat Deposits* continued, with sales double those of fiscal 1999. As an extension of the hit *Healthy Econa Cooking Oil* line, Kao introduced the *Healthy Econa Dressing* series in February 2001. The launch of *Healthy Econa Cooking Oil – For Lower Cholesterol* in March 2001 is expected to strengthen Kao's leading position in the market for functional healthy oil. During the fiscal year, Novartis Kao Co., Ltd., a joint venture with Novartis Consumer Health SA, launched three new products as planned.

Enhancing Global Business

Outside Japan, Kao is steadily undertaking strategic globalization initiatives. Efforts to strengthen the earnings structure of companies in each region have been effective in countering the increasingly competitive international operating environment. In Thailand, we established Kao Consumer Products (Southeast Asia) Co., Ltd. to serve as our ASEAN regional headquarters and to optimize manufacturing, product development and marketing in the region. In China, normalization of inventory at distributors, which led to weak performance in fiscal 1999, laid the groundwork for recovery in consumer products operations during the past fiscal year. Kao also allocated significant investment to several chemical products subsidiaries around the world to support growth and improved profitability in sectors including fatty alcohols, copier and printer toner and related products, and aroma chemicals.

The acquisition of the *ban* antiperspirant/deodorant brand through The Andrew Jergens Company has given Kao access to a large new market in North America, where it will take advantage of synergy with its existing skin care business. Kao expects to increase the brand value of *ban* with superior R&D expertise and active marketing investment. Kao also announced a strategic alliance with

Takuya Goto, President

➥ Our focus on core businesses and efforts to improve operating efficiency led to record high operating income exceeding ¥100 billion for the first time in fiscal 2000.

➥ Kao's unique ability to link R&D to meeting emerging consumer needs and market innovative products is the engine of long-term growth.

➥ Our strategic priorities for greater corporate value are building stronger domestic operations through reinforcement of existing businesses and development of new ones such as health care, while pursuing global expansion.

Archer-Daniels-Midland Company (ADM) of the United States covering the manufacture, marketing and sales of diacylglycerol oil, the primary ingredient in *Healthy Econa Cooking Oil*, in international markets except Asia, where Kao will market the oil independently.

Improved Group Management

During fiscal 2000, Kao continued its drive to improve Group management and corporate governance, which will lead to increased corporate value. A core theme was speedier decision making, which was the rationale guiding the reduction in the size of the Board of Directors in June 2000, together with delegating more authority to its business units. As the first step toward improved corporate governance, the Advisory Committee started work on its function of enhancing transparency by reviewing and providing advice during management's decision-making process for major issues.

Furthermore, Kao plans to review its compensation system for Board members to further align their interests with those of shareholders and facilitate an increase in corporate value. Specifically, this will include the introduction of a stock option plan for directors and expansion of the performance-linked portion of compensation. In addition, the Company also plans to increase the number of external statutory auditors to enhance auditing. These moves will help reinforce management efficiency by speeding up decision-making and clarifying the responsibilities and accountability of directors.

Human Resource Value

Kao offers employees an environment in which they are able to develop their potential and excel, while engaging in forthright and open exchanges of ideas and supporting each other's improvement. Our corporate culture encourages employees to express openly their dissatisfaction with the status quo and seek ways to promote improvement. We strive to create an environment that engenders employee enthusiasm and commitment in three areas: continuous efforts to offer consumers a better quality of life; value-creating product development; and continuing innovation for improvement. The Company believes that employees who have embraced this mindset are one of its greatest resources for sustainable growth. Results of this conviction have included numerous value-added and market-creating products from R&D and annual cost reductions of ¥10.5 billion through TCR activities during fiscal 2000 in Japan.

Significant results have been achieved in Japan and at Andrew Jergens, a U.S. subsidiary, where EVA-based incentive compensation systems for executives and employees have been implemented. EVA is currently used as a main management measure at the corporate level, and in making daily operating decisions at the tactical level. One of the most important benefits of EVA-based management is promoting management from the shareholders' perspective. As a result, this management system serves to reinforce Kao's longstanding emphasis on profitability. Following successful implementation in Japan and at Andrew Jergens, a rollout to several subsidiaries outside Japan is under way.

Commitment to Society and the Environment

Kao seeks to satisfy all stakeholders through activities such as sound disclosure to maintain management transparency, compliance with our code of ethics and basic principles for corporate activities, and environmental protection. The Company continuously works to improve environmental management. Our commitment to society and stakeholder satisfaction was affirmed at the end of 2000 when the *Nihon Keizai Shimbun* newspaper designated Kao as one of 15 "Twenty-first Century Companies." The newspaper chose Kao because of its flexible response to a changing environment and consumer-oriented value creation that go beyond the conventional wisdom.

Kao has firmly in place the tools required to continue building the value of the corporation, and the capabilities necessary to use them effectively. We intend to maintain a clear focus on justifying the trust of our shareholders, customers and society.

June 28, 2001

Takuya Goto

Takuya Goto
President

Key Drivers for Profitable Growth: Brand Equity, Superior R&D and TCR

A primary Kao objective is sustained profitable growth that increases corporate value over the long term to the benefit of shareholders and all other stakeholders. We view our brands as a guarantee of quality, value and reliability. Moreover, our superior research and development enable us to generate products that offer excellent value and outstanding performance. Through new product launches and improvements, Kao strives to expand brand equity, which is a driving force for profitable growth. At the same time, Kao works to enhance profitability through Total Cost Reduction (TCR) activities. Our ability to achieve profitable growth draws strength from the pursuit by Kao employees of innovation, driven by dissatisfaction with the status quo.

Pursuit of Innovation: a Key Element of Kao's Corporate Culture

Kao's corporate culture embraces continuous innovation driven by dissatisfaction with the status quo. More than simply a matter of product innovation to meet consumer needs, this approach encompasses overall operational systems as the Company works to achieve the highest level of stakeholder satisfaction in expanding corporate value.

Constant Product Innovation

Kao has numerous category number one brands in its portfolio in Japan that consumers have long trusted. *Humming* fabric softener has been a market leader for more than 30 years, *Bioré* skin care products for 20 years, and *Attack* compact laundry detergent for 14 years. Brands are the key instrument to building a long-lasting relationship with consumers.

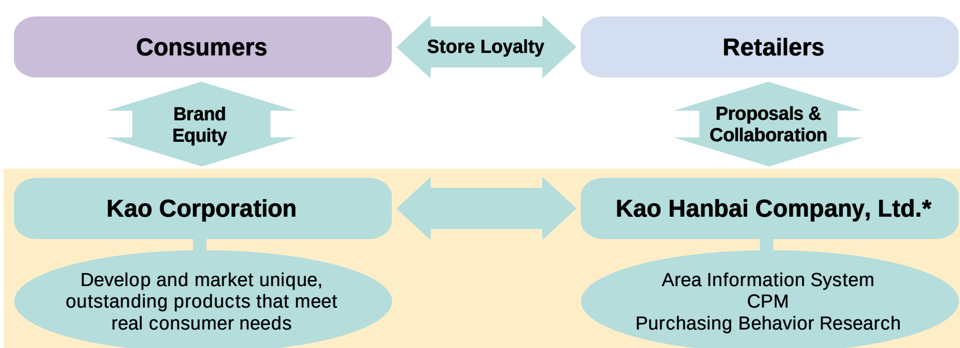
These and other brands have remained successful because Kao constantly improves its products to delight consumers and meet their changing expectations. This ability to stay one step ahead in pleasing consumers and enhancing their lives is based on the commitment of Kao employees to innovation.

Constant Operational Innovation

Initiated in 1986, Kao's Total Cost Reduction (TCR) activities aim to innovate operations through a complete review of company-wide operations.

In addition, Kao complements its focus on introducing high-value-added products with a nationwide sales system in Japan and activities to energize the retail environment and target markets.

Kao's Proposal-Based Sales Activities



* Domestic consumer products sales company

Continuous Innovation of *Attack*

Attack, one of Kao's flagship brands, was the world's first compact laundry detergent when it was launched in 1987. Its key ingredient alkaline cellulase, which Kao developed, offers outstanding whitening and stain removal power. *Attack* embodied the strong interest consumers had expressed in a light, efficient and easy-to-use detergent, and quickly became the leading detergent brand in the Japanese market. Constant improvement of product features, including further compactness, has driven the ongoing evolution of this brand and supported its position as the leading detergent brand in Japan. Following the introduction of a new sheet-type product in October 2000, Kao's unique technologies have enabled a thorough improvement of *Attack* in April 2001, which is expected to further expand *Attack*'s brand equity.

Improved *Attack*

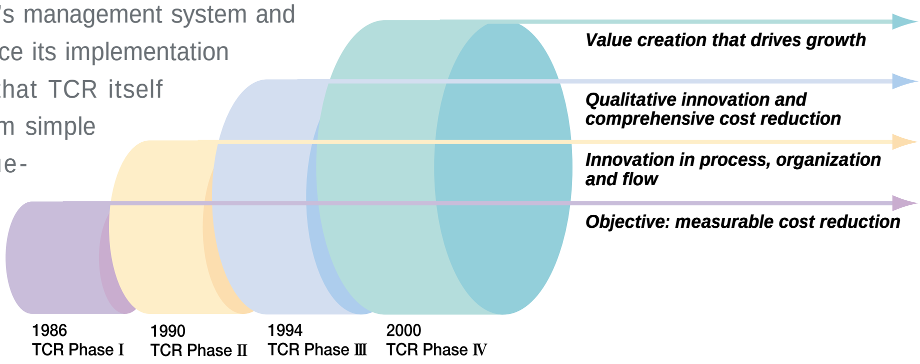
- Dissolves five times faster than conventional *Attack* and uses highly efficient nonionic surfactant for better stain removal. Applications for 53 patents have been submitted.
- The formula and manufacturing process have been re-engineered to reflect changing consumer needs and new washing machine functions.

Attack Sheet-type

- The world's first sheet-type laundry detergent.
- Individually packaged for a single load in water-soluble film of 0.03mm.
- Easy-to-use sheets can simply be dropped into the washing machine.

Progress in Ongoing TCR

TCR is an integral component of Kao's management system and has achieved considerable results since its implementation in 1986. Its noteworthy feature is that TCR itself continues to evolve, stepping up from simple cost reduction activities to value-creating initiatives. TCR has played an important role in Kao's ability to innovate and adapt to change, contributing to profitable growth.



Proposal-Based Sales Activities to Energize Retail Environment

For more than 20 years, Kao has been working on improving the supplier/retailer partnership through its consumer products sales company in Japan. In 1995, Kao started development of cooperative activities, which are now generally called Efficient Consumer Response. Kao has been making specific proposals to domestic retail chains and outlets to clearly define expectations and tasks such as raising shelf efficiency.

Kao has recently developed a Category Profit Management (CPM) system in cooperation with consulting firm PricewaterhouseCoopers. This system is designed to enhance retail inventory management and optimize shelf space, and therefore is expected to improve supply chain management.

Kao's proposal-based sales activities geared toward the benefit of both Kao and retailers have helped gain their confidence. Thus, collaboration with retailers fosters Kao's strength in Japan.

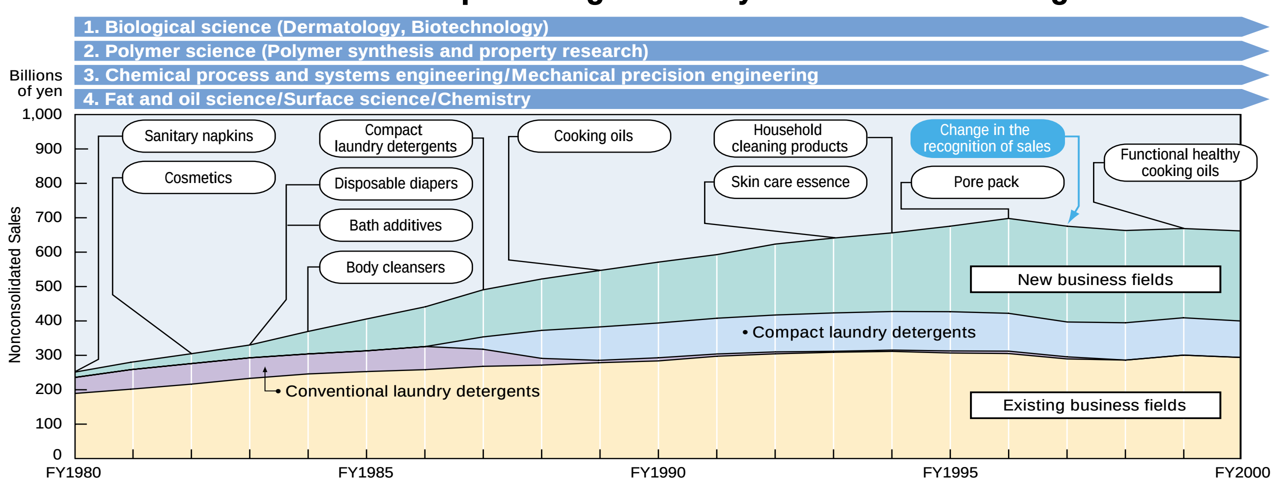
Superior R&D Capabilities:
a Core Competency

A primary Kao strength is its ability to develop innovative new products. Kao devotes significant management resources to R&D because the Company considers it the source of continuous profitable growth. For the past several years, Kao has deployed 4 to 5 percent of net sales to R&D in a successful effort to deliver new value to consumers.

The Source of Innovative R&D

Fatty chemicals, the basic raw materials for detergents, shampoo and other products, are mainstay products in Kao's chemical products business. Our product development is differentiated by access to these materials, in tandem with our intensive basic research. Our R&D has also produced a competitive advantage in developing key chemicals and technologies such as moisturizing agents for skin care and absorbent polymers and non-woven fabrics for use in disposable diapers and other products. Moreover, Kao's demonstrated ability to link research and development to meeting emerging consumer needs supports the Company's success at developing innovative and unique products.

Innovative Products Developed Using Kao's Key Chemicals/Technologies



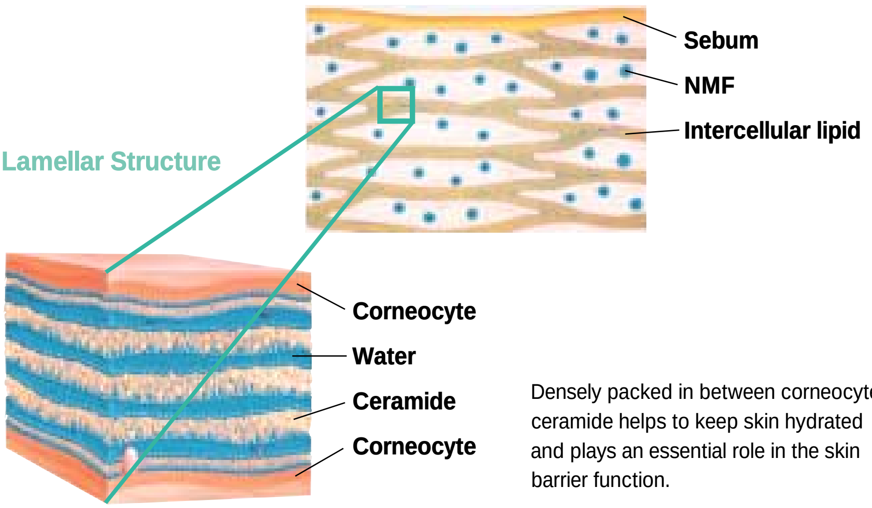
A Growth Strategy Based on Creating New Markets

Kao endeavors to use knowledge cultivated over many years of R&D to develop highly functional and effective new products. A representative example, *Healthy Econa Cooking Oil* (now called *Healthy Econa Cooking Oil — For Prevention of Fat Deposits*), is the result of 15 years of R&D. Designed to help prevent fat from accumulating in the body, it was the first edible oil to be licensed by Japan's Ministry of Health and Welfare (currently the Ministry of Health, Labour and Welfare) as a "Food for Specified Health Use." *Healthy Econa Cooking Oil* has achieved sales of ¥10 billion in the second year since its launch while creating the new, high-margin healthy oil market segment.

Business Development Supported by Key Chemicals

A synthetic ceramide developed by Kao is a key chemical in *Sofina* cosmetics. For many years, Kao has conducted dermatological research on the mechanism of moisture retention in the skin. Following the launch of *Sofina* in 1982, the Company focused its attention on the natural ceramide that is a primary component of intercellular lipid. After determining its moisture retention mechanism, Kao succeeded in developing a synthetic ceramide. *Sofina* skin care products have been well received by consumers for their excellent moisturizing effect, earning support as high-quality, scientifically advanced products.

Function of Ceramide Structure



Densely packed in between corneocytes, ceramide helps to keep skin hydrated and plays an essential role in the skin barrier function.

Using Diacylglycerol to Create and Expand Markets

Kao has long been involved in the edible oils market, having introduced *Econa* industrial-use edible oil in 1928, and has continued R&D for edible oils. The application of R&D capabilities to expertise in industrial-use edible oils resulted in the 1999 launch of *Healthy Econa Cooking Oil*.

The key ingredient is diacylglycerol, a natural ingredient that is present in small amounts in conventional edible oils. One of its major features, approved by Japan's Ministry of Health, Labour and Welfare, is prevention of fat deposits. Kao developed production technology for this ingredient. The *Healthy Econa* brand offers new functionality that meets heightened health consciousness among consumers, which has made it a hit product.

In addition, the U.S. Food and Drug Administration accepted Kao's determination of diacylglycerol in December 2000 as "Generally Recognized As Safe" (GRAS). The U.S. market has 35 million middle-aged and older consumers who are overweight, approximately 10 times as many as in Japan, and Kao is therefore moving proactively to build its diacylglycerol business in the United States. A strategic alliance with U.S.-based Archer-Daniels-Midland Company will support speedy market penetration, followed by global development of the diacylglycerol market.

Increasing Corporate Value: Portfolio Management that Engenders Profitable Growth

Kao's strategic priorities for increasing corporate value are strengthening and expanding core businesses, using them as a platform for building new businesses, and reinforcing overseas business.

A Stronger Operating Base in the Domestic Market

Downward price pressure and intensifying competition have continued in Kao's mainstay consumer products market in Japan, which has made the domestic operating environment increasingly challenging. Kao is managing these market realities by focusing on its core strengths: the ability to discover consumer needs; superior research and development; and a strong sales force. This focus has resulted in measurable gains in competitiveness in the domestic market. Kao endeavors to strengthen top brands and build number two or three brands into market leaders.

New Businesses: A Focus on Health Care

Cleanliness, beauty and health are Kao's primary business domains. One of Kao's main strategies for growth entails building its market presence and generating profitable growth in the high-potential health care segment.

Kao has built up its presence in the healthy cooking oil market. The Company is striving to further strengthen and expand its market position with the introduction of *Healthy Econa Cooking Oil — For Lower Cholesterol*, which helps lower the level of cholesterol in the blood while helping prevent fat deposits in the body through continued use.

The formation of joint venture Novartis Kao Co., Ltd. in July 2000 melds the superior health care R&D capabilities of Novartis with Kao's expertise in understanding and meeting consumer needs.

Overseas Growth Strategy

In working to profitably expand global operations, Kao is emphasizing reinforcement of the consumer products business in China and other Asian markets with future growth potential. Another priority is the North American personal care market, where Kao is devoting management resources. Acquisitions and strategic alliances are an important component of Kao's global business development strategy.

At the same time, Kao has created a global production and marketing network in the chemical products business. Kao will strive to build a stronger earnings structure by offering unique and outstanding products and emphasizing higher-margin operations.

➥ Expanding Brand Equity through Product Launches

Kao has launched numerous new and improved products in its brand portfolio. Deploying its innovative product development ability, Kao has been successful in launching new products that meet emerging consumer needs or exceed their expectations. Kao works to generate value with unique and outstanding products, which benefit both consumers and retailers.

Kao is concentrating its management resources to take full advantage of the opportunities to build brand equity that new and improved products present. Recent new product launches for the *Attack*, *Bioré*, *Humming*, *Family* and *Laurier* brands have successfully expanded brand equity in Japan.

Success in Expanding the Equity of the *Bioré* Brand

➥ Reinforcing the Skin Care Business in North America

In North America, Kao is developing its skin care business through a subsidiary, The Andrew Jergens Company. In September 2000, Kao acquired the *ban* antiperspirant/deodorant brand* through Andrew Jergens. Kao intends to apply its R&D strengths to add value to the *ban* brand and develop related new products. Looking forward, the Company will speed development of its presence in the North American skin care market by using the *Bioré*, *Jergens*, *Curél* and *ban* brands appropriately and effectively to optimize Kao's innovative skin care technology.

* The *ban* brand is sold in 17 countries in the Americas and Asia; however, Japan is not included in the acquisition agreement.

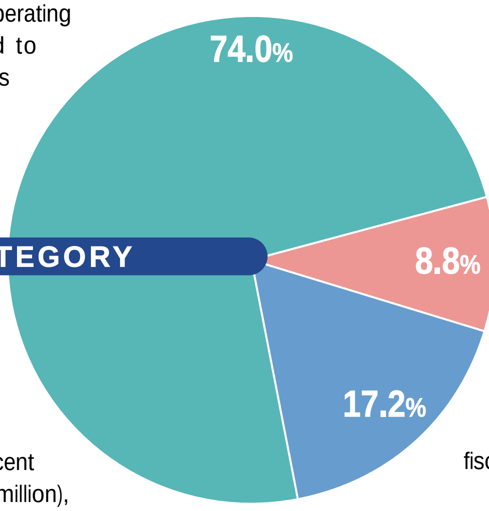
Kao at a Glance

• **Net sales**	**¥821.6 billion**	**(US$6,631.4 million)**	**-3.0% year-on-year**
• **Operating income**	**¥107.0 billion**	**(US$864.4 million)**	**+8.0% year-on-year**
• **Net income**	**¥59.4 billion**	**(US$479.6 million)**	**+14.0% year-on-year**

Consumer Products

Net sales decreased by 3.9 percent year-on-year to ¥607.8 billion (US$4,905.8 million), while operating income rose by 4.9 percent to ¥86.1 billion (US$695.0 million). Excluding the effect of both the consolidation of a domestic consumer products sales company and the negative currency translation, net sales declined by 0.3 percent from the previous fiscal year. In the challenging operating environment, the Company continued to focus on increasing the value of its brands by improving existing products while launching new products that meet emerging consumer needs.

SALES BREAKDOWN BY CATEGORY



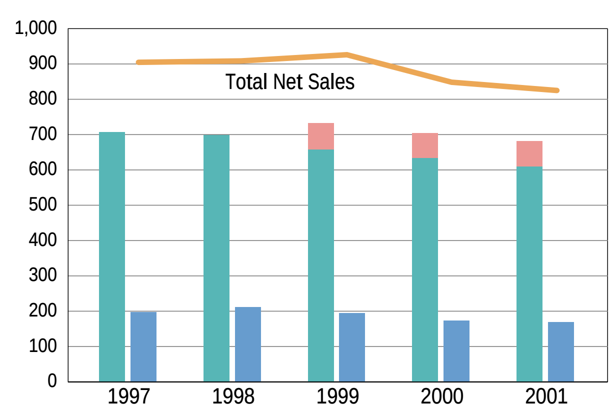
Cosmetics *Sofina*

Net sales increased by 2.4 percent to ¥72.5 billion (US$585.8 million) and operating income rose 29.3 percent to ¥2.8 billion (US$22.8 million) for this segment. Measures to counter harsh market conditions included new product introductions and improvements in the *Sofina* product lineup, as well as the launch of the new *est* brand. Kao completed inventory adjustments at retailers in the first half of the fiscal year.

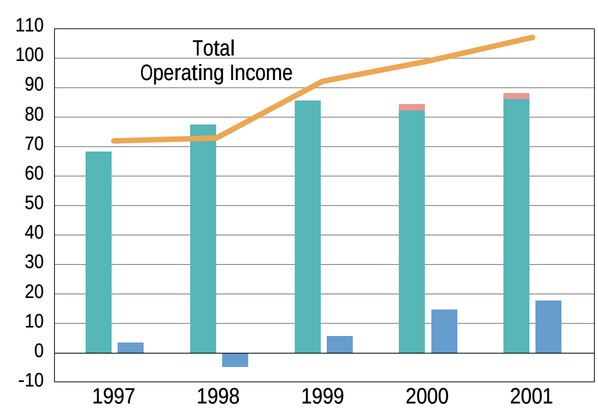
Chemical Products

Net sales decreased by 2.6 percent to ¥167.8 billion (US$1,355.1 million), while operating income rose by 20.2 percent to ¥17.7 billion (US$143.0 million). Excluding the negative currency translation, net sales in this segment grew 1.8 percent year-on-year. Key growth drivers included fatty chemicals in Asia and such specialty chemicals as copier and printer toner and related products, and aroma chemicals.

NET SALES (Billions of yen)



OPERATING INCOME (Billions of yen)



Consumer Products   Cosmetics *Sofina*   Chemical Products

(Years ended March 31)

Note: Separate information for net sales and operating income of Cosmetics *Sofina* is presented starting from the fiscal years ended March 31, 1999 and 2000, respectively.

MAJOR PRODUCTS

Personal Care Products in Japan

- Soaps
- Facial cleansers
- Body cleansers
- Skin care
- Men's cosmetics
- Hair enhancer tonics
- Shampoos, conditioners and hair treatment products
- Hair styling agents
- Hair coloring agents
- Bath additives
- Toothpaste
- Toothbrushes

Laundry and Cleaning Products in Japan

- Laundry detergents
- Fabric softeners
- Bleach
- Laundry finisher
- Dishwashing detergents
- Household cleaning detergents
- Paper cleaning products
- Car care products

Hygiene Products in Japan

- Sanitary napkins
- Disposable diapers
- Baby wipes
- Incontinence products
- Hygiene care products

Food Products in Japan

- Cooking oils
- Frying oils
- Dressings
- Packaged cake mixes

Cosmetics *Sofina*

- Facial cleansers
- Basic care
- Special care
- Foundation
- Make-up

Consumer Products in Asia and Oceania

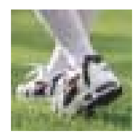
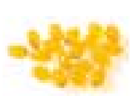
- Soaps
- Facial cleansers
- Body cleansers
- Shampoos, conditioners and hair treatment products
- Hair styling agents
- Laundry detergents
- Fabric softeners
- Bleach
- Dishwashing detergents
- Household cleaning detergents
- Paper cleaning products
- Sanitary napkins
- Disposable diapers
- Toothpaste
- Toothbrushes

Personal Care Products in North America and Europe

- Shampoos, conditioners and hair treatment products
- Hair styling agents
- Hair coloring agents
- Soaps
- Lotions
- Body cleansers
- Facial care
- Antiperspirant/deodorant

Chemical Products

- Fatty acids
- Fatty alcohols
- Fatty amines
- Glycerin
- Edible oils
- Concrete additives
- Asphalt emulsifiers
- De-inking agents
- Fragrances
- Agrochemical additives
- Disinfectant cleaners
- Water treatment chemicals
- Cleaners for electronic parts
- Plastics additives
- Rubber processing agents
- Copier and printer toner and related products
- Polyurethane for shoe soles


Personal Care Products in Japan

***Bioré Facial Foam*, which features a mildly acidic formulation in line with the natural pH of healthy skin, expanded its market share. New product *Bioré Facial Foam Moisture Cream-in* also performed well.**

Focal Points

- Differentiate products with unique technology to offer consumers added value and greater functionality.
- Reinforce market positions of major brands through new and improved product introductions, supported by effective marketing strategies.
- Continue reducing costs and effectively allocating resources to improve profitability.

Operating Environment and Performance

Overall, the Japanese personal care market contracted marginally in yen terms due to continued downward pricing pressure, although sales volume rose slightly. Competition has become increasingly stringent as global peer companies introduce their brands in Japan. The facial cleanser, body cleanser, hair lightening and coloring products segments grew, while the shampoo/conditioner segment remained soft due to price deflation.

Kao's sales of personal care products declined slightly from the previous fiscal year. Competitive market conditions necessitated additional promotional and advertising spending on selected brands, while successful cost reductions continued.

Fiscal 2000 Initiatives and Results

Kao increased its share of the facial and body cleansers segment, where consumers have responded positively to a mildly acidic formulation in line with the natural pH of smooth, healthy skin. *Bioré Body Care Foam* and *Bioré Facial Foam* benefited from investment in advertising to inform consumers about the benefits of mild acidity. Adding *Moisture Cream-in* line extensions to both facial and body cleansers also helped to build market share.

In the expanding hair lightening and coloring segment, the spring 2000 launch of *Blauné Aroma Hair Color*, made with an ammonia-free formula and a new technology that facilitates long-lasting performance, has contributed to steady market share growth. A new hair color advice system serves to enhance communication with consumers.

Shampoo/conditioner is a major personal care category, and the launch of improved *Essential Damage Care* helped Kao maintain its market share. Sales, however, were down because of the larger proportion of pouch refills in the sales mix, while increased sales of promotional products and discounted bundled products resulted in lower unit sales prices. Among other hair care categories, Kao maintained the top share in the hairspray segment, although the market is shrinking as casual hairstyles become more popular.

Kao's efforts to enhance its sales activities with a focus on health and beauty care products resulted in strong growth in sales through drug stores. The portion of toiletry products sold through this channel rose significantly.

Fiscal 2001 Issues and Objectives

Kao will further strengthen the *Blauné* hair coloring line for gray hair and introduce *Lavenus Color Appeal*, a hair lightening product targeted at younger consumers. In the shampoo/conditioner category, Kao will work to increase market share by reinforcing major brands *Essential*, *Merit* and *Lavenus*. The benefits of mild acidity, which is closer to the pH of smooth and healthy skin, will continue to be a core theme for *Bioré* facial and body cleansers. New products in the skin care category will include pore care and UV care products for the *Bioré* brand.

Solid Performers

Consumers responded favorably to the ammonia-free formula and long-lasting performance of *Blauné Aroma Hair Color*.

The improved *Essential Damage Care* shampoo/conditioner answered rising consumer interest in products that treat damaged hair, thus helping Kao maintain its share of the shampoo/conditioner market.

Laundry and Cleaning Products in Japan

Developed as an easy-to-use product for effective household cleaning, *Quickle Wet-type Floor Care Sheets* thoroughly clean and disinfect floors without a wet cloth or conventional mop and bucket.

Focal Points

- Emphasize raising consumer loyalty to major brands.
- Employ effective marketing strategies and continue to reduce costs to counter increasing price competition.
- Continue optimizing R&D capabilities to add value and functionality to products in order to activate the market.

Operating Environment and Performance

The overall laundry and cleaning products market contracted slightly. Unit prices for laundry detergent have fallen as a result of a competitive environment among both retailers and manufacturers. Dishwashing detergent market sales declined, affected by changes in consumer lifestyles that have reduced usage and lower unit prices due to the trend toward economy-sized packaging. Adding anti-bacterial functions to dishwashing detergents negatively impacted the kitchen disinfectant products market.

Kao's numerous products with high market shares continued to dominate the domestic laundry and cleaning products market. Although sales excluding exports decreased slightly, sales volume remained essentially unchanged year-on-year. Kao improved profitability despite stiff competition by maintaining market leadership in key categories and continuing Total Cost Reduction (TCR) activities.

Fiscal 2000 Initiatives and Results

New Beads laundry detergent, relaunched in 1999, has grown as Kao's second brand after *Attack*, one of the Company's most successful products. The combined success of these two detergents has increased Kao's leading market share. Although *New Beads* posted steady growth, a contracted gift market adversely affected sales, resulting in a year-on-year sales decline for laundry detergents. *Attack Sheet-type* laundry detergent was launched as a line extension in fall 2000 and leads the market for new types of detergents.

Kao's sales of fabric softeners were brisk, and its market share was substantially improved by the launch of *Humming 1/3 Anti-bacterial Plus*, following *Floral Humming 1/3*. The product strengthened the position of the *Humming* brand by adding value to the existing product lineup. However, sales of other laundry finishing products decreased due to the shrinking market.

In the dishwashing detergent category, *Family Pure* and newly launched *Family Pure Mild* contributed to higher market share. Their pleasant herbal fragrance and deodorizing effect generated solid consumer response. Other kitchen detergents, including disinfectants, performed poorly.

The *Quickle Wiper* line of household cleaning mop kits and sheets has already achieved optimal household penetration. Kao therefore revitalized the brand with new *Quickle Wet-type Floor Care Sheets* in spring 2000 and improved *Quickle Dry-type Floor Care Sheets* in February 2001. However, exports of household cleaning mop kits and sheets, which are marketed in North America and Europe by S.C. Johnson & Son, Inc., decreased due to the transfer to license-based production overseas.

Fiscal 2001 Issues and Objectives

A primary theme for fiscal 2001 will be further strengthening core products to fortify brand loyalty. New and improved products will drive market share gains in the competitive environment. *Attack* laundry detergent was improved in April 2001 with tiny air pockets infused into micro-particles that quickly dissolve in water to rapidly penetrate stains and thoroughly clean clothes. Kao will also focus on increasing market share of products that are number two in their categories. *Family Power Gel*, launched in March 2001, is expected to help reinforce Kao's position in the dishwashing detergent market.

Solid Performers

The anti-bacterial properties of *Humming 1/3 Anti-bacterial Plus* have made the product popular with consumers who dry their laundry inside or in the shade.

New Beads, with its gentle lily-of-the-valley fragrance, has become Kao's number-two laundry detergent brand.

Family Pure and *Family Pure Mild*, which feature a pleasant herbal fragrance, deodorizing ingredients and a stylish package design, have expanded Kao's share of the dishwashing detergent market.

Hygiene Products in Japan

Slim and absorbent ***Laurier Super Slim Guard*** **has increased Kao's share of the expanding market for ultra-thin-type sanitary napkins for daytime use.**

Focal Points

- ➥ Reinforce growing categories to counter overall market contraction.
- ➥ Offer innovative, value-added products that respond to changing consumer requirements.
- ➥ Increase competitiveness and improve profitability by raising operating efficiency.

Operating Environment and Performance

The overall hygiene products market shrank from the previous fiscal year. Sanitary napkin sales and volume declined due to falling prices, a continuing decrease in the relevant consumer population and fewer units used resulting from improved product performance. However, the market for heavy flow and overnight use products grew. The disposable baby diaper market contracted because of strong price competition, although volume remained flat. Sales and volume of adult incontinence products continued to grow, but slowed due to falling prices.

At Kao, lower sales led to a year-on-year decline in operating income despite the shift toward value-added products, continuing cost-reduction efforts and increased productivity. In sanitary napkins and disposable baby diapers, high value-added products performed well, although pricing pressure materially affected sales. Higher sales of adult incontinence products partially offset the shortfall in this segment.

Fiscal 2000 Initiatives and Results

In the sanitary napkin category, Kao continued to pinpoint customer needs and focus on value-added products to increase competitiveness in both performance and prices. The *Laurier Super Guard* series increased Kao's share of the growing market for heavy flow and overnight use products. Kao also entered the expanding market for ultra-thin-type sanitary napkins for daytime use by launching *Laurier Super Slim Guard*, which can be worn even on heavy flow days. In spring 2000, Kao introduced *Laurier Dry Cotton Sheets*, which incorporate activated charcoal as a deodorant for comfortable protection with a drier, cleaner feeling. The Company also improved *Laurier Pantyliners*. These two daily hygiene products drove strong share gains.

The complete renewal of the *Super Merries* line of disposable baby diapers in October 2000 generated solid market share gains. Major improvements included greater absorbency, better leakage prevention, diaper rash prevention and a new package design. However, significantly lower sales prices reduced overall diaper sales, although the growing pants-type segment partially offset the decline.

Sales of adult incontinence products continued to grow with the contribution of the pants-type *Relief*, in line with expanding consumer demand. Kao continued to focus on the development of products that reduce the workload of caregivers while increasing the comfort of people who receive nursing care. Product development concepts emphasized more hygienic nursing care, exemplified by *Relief Odor-Free Guard*, the first product for slight incontinence problems that uses activated carbon to eliminate odors.

Fiscal 2001 Issues and Objectives

Kao will strengthen standard-type sanitary napkin lines with new product introductions. *Laurier Dry Cushion with Wings* for daytime use and *Laurier Super Overnight* were both launched in March 2001. In spring 2001, Kao also launched a line of new products to facilitate more hygienic nursing care.

Solid Performers

Relief Odor-Free Guard is the first product for slight incontinence problems that uses activated carbon to eliminate odor. In addition, its absorbency and the incorporation of breathable material increase comfort.

The *Merries* line of disposable baby diapers has been completely renewed to feature a new package design, greater absorbency, better leakage prevention, and protection against diaper rash.

Food Products in Japan

Focal Points

- Strengthen the *Econa* brand franchise through line extensions and a co-branding program.
- Use the recommendations of a nationwide organization and health care professionals to promote benefits of diacylglycerol oil.

Sales of *Healthy Econa Cooking Oil – For Prevention of Fat Deposits* continued to increase, expanding Kao's share of the healthy cooking oil market.

Operating Environment and Performance

While the cooking oil market remained flat during fiscal 2000, the shift toward healthier, more functional products continued, with sales of such products growing to account for more than 15 percent of the market. Sales of *Healthy Econa Cooking Oil – For Prevention of Fat Deposits* doubled over the previous fiscal year, contributing to increased earnings.

Fiscal 2000 Initiatives and Results

As part of an aggressive, multifaceted advertising program, Kao highlighted *Healthy Econa Cooking Oil*'s license from the Ministry of Health, Labour and Welfare as a "Food for Specified Health Use," and its designation as "reliable and safe" by a nationwide organization that promotes medical check-ups. Promotional activities extended to the Internet with a website* for the product that also provides information about the health benefits of main ingredient diacylglycerol. This effort complemented an ongoing program to inform health care professionals of the positive effects of diacylglycerol.

Kao also implemented a co-branding program with leading processed food manufacturers, under which their products display the phrase "Made with *Healthy Econa Cooking Oil*" on their packages. This program, which has been successful in increasing *Healthy Econa Cooking Oil*'s market penetration, was carried out in cooperation with the chemical products division where the related sales were recorded.

*In Japanese only

Fiscal 2001 Issues and Objectives

Kao expanded the *Econa* brand with the February 2001 launch of *Healthy Econa Dressing* and the March 2001 launch of *Healthy Econa Cooking Oil – For Lower Cholesterol*. These new products will contribute to further strengthening the *Econa* brand during fiscal 2001.

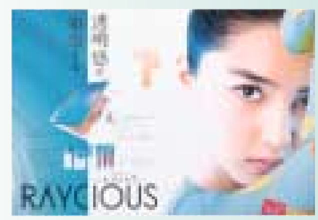
Cosmetics *Sofina*

Focal Points

- Minimize inventory at retailers and reinforce core segments where Kao has a demonstrated competitive advantage.
- Stimulate consumer interest through product improvements and build the new *est* brand.

New cosmetics brand *est*, which incorporates the dermatological excellence of *Sofina*, is sold through beauty counseling to offer more effective skin care tailored to each user's needs.

Solid Performers



The addition of new liquid foundation helped further strengthen the *Sofina Raycious* line.

Operating Environment and Performance

The overall cosmetics market was flat during fiscal 2000. The lower-priced cosmetics market remained steady, while the prestige cosmetics market remained at the low level of the previous fiscal year. Supported by the launch of a new brand and renewals, Kao achieved sales growth.

Fiscal 2000 Initiatives and Results

Kao completed inventory adjustments begun in fiscal 1999 and adjusted SKUs in its cosmetics portfolio. To benefit from the resulting efficiency, Kao strengthened core categories, increasing sales by introducing *UV Cut* products for the *Sofina Very Very*, *Sofina Emolliel* and *Sofina Vital Rich* lineups in the basic care category and improving *Sofina Finefit* in the foundation category. Advertising was focused on selected lines of products under the *Sofina* brand.

The August 2000 expansion of the *Sofina Raycious* line with a new liquid foundation, targeting women in their twenties, was the central driver of sales growth. In addition, *est*, a new cosmetics brand that incorporates the dermatological excellence of *Sofina*, was launched in October 2000. This new brand is sold exclusively through beauty counseling at department stores.

Moreover, Kao offered new skin care solutions. *Sofina Very Very Powdery Pore Care* is one of the special care products for younger consumers with oily skin problems such as acne.

In the color makeup category, new products such as *AUBE Rouge Livelish* and *AUBE W Perfect Mascara*, in tandem with well-timed promotional activities, contributed to higher market share in spring 2001.

Fiscal 2001 Issues and Objectives

Kao will continue to strengthen basic care and foundation product lines while developing new products that meet emerging consumer expectations. Another focus will be building the momentum of the *est* brand.

Consumer Products in Asia and Oceania

***Attack Color*, which helps keep colored fabrics bright, has contributed to an increase in market share for the *Attack* brand.**

Focal Points

- Further build brand equity and enhance market penetration.
- Improve profitability by maximizing the benefits of regionally based management and emphasizing efficiency.
- Share know-how and best practices on business reforms among the affiliates to speed up innovations.

Operating Environment and Performance

Price competition increased sharply due to heightened competition among global peer companies and the market entry of global retailers. The slowdown in the U.S. economy also impacted the region.

Despite the challenging environment in Asia and Oceania, Kao generated modest sales growth before negative currency translation, while the strong yen resulted in a slight decline in sales in yen terms. Operating income increased as a result of business reforms.

Fiscal 2000 Initiatives and Results

In fiscal 2000, Kao reorganized its management structure into three regions: China including Hong Kong; Taiwan; and ASEAN.

In China, inventory adjustment at distributors initiated in fiscal 1999 was completed. Improvements to *Sifoné* shampoo, *Attack* compact laundry detergent and *Laurier* sanitary napkins contributed to recovery from sluggish fiscal 1999 sales, and the launch of *Kao White* soap generated promising sales. Efforts to strengthen sales in South China (Guangzhou Province) expanded Kao's market share for shampoo, laundry detergent and sanitary napkins. Moreover, building an image for *Lavenus* that stresses its Tokyo origins contributed to its good performance in Hong Kong.

Sales in Taiwan were down primarily due to the poor performance of disposable baby diapers in the severe market environment, partially offset by good performance in facial cleansers, body cleansers and sanitary napkins. Initiatives to revitalize diapers are under way.

In ASEAN countries, sales in Indonesia, which are accounted for using the equity method, continued to climb. Sales in Thailand were flat in yen terms but increased on a local currency basis, and the success of profit management reforms such as the consolidation of SKUs, review of sales activities, and reduction of distribution costs contributed to an increase in operating income.

Sales of *Attack Color* in Thailand have remained strong since its 1999 launch, and introductions in Malaysia, Singapore and Indonesia have built on existing product sales. Despite intense competition, the *Laurier* sanitary napkin line held its market-leading position in Indonesia, Thailand and Malaysia.

Kao Consumer Products (Southeast Asia) Co., Ltd. was established in Thailand to promote unified management in the ASEAN region, strengthen marketing and product development, and optimize in-market production. Initiatives included preparations for standardization of specifications for certain products in fiscal 2001.

Fiscal 2001 Issues and Objectives

Goals include building a foundation for sales growth. Kao will clearly define priorities in sales areas and brands in the Chinese market, and future development will focus on the four categories of detergents, shampoos/conditioners, skin care and sanitary napkins. Business reform in Thailand during fiscal 1999 helped improve the cost structure in fiscal 2000, and the resulting know-how and practices will be ported to other countries during fiscal 2001. Throughout ASEAN, Kao will counter pressure from global retailers by strengthening category management and key account management.

Solid Performers

Popular for its absorbency and soft texture, *Laurier* remains the number-one sanitary napkin brand in Indonesia, Thailand and Malaysia.

The logo of *Bioré* brand products has been standardized to promote a unified brand image.

Personal Care Products in North America and Europe

Measures to upgrade *Bioré* from a line of facial cleansers to a total facial care brand are under way.

Focal Points

➥ Build comprehensive coverage of key skin care market in North America.

➥ Add value to acquisitions through synergy between Andrew Jergens' marketing expertise and Kao's technological capabilities.

➥ Continue to enhance profitability by optimizing the benefits of reforms at Goldwell.

In North America, subsidiary The Andrew Jergens Company markets skin care brands such as *Jergens*, *Bioré* and *Curél*, and the acquisition of the *ban* brand in fiscal 2000 supports its objective of becoming a comprehensive skin care company. Goldwell GmbH, headquartered in Germany, concentrates on global marketing of hair care products for beauty salons. Guhl Ikebana GmbH markets premium hair care products in Europe.

Operating Environment and Performance

In North America, premium facial cleansers were a key driver in the facial care market. The pore cleansing strip market has contracted sharply from its peak, but remained stable. Polarization between premium and value lotions continued in the hand and body lotion market. The hair color market expanded throughout the world, both in the professional and mass markets.

At Andrew Jergens, sales of pore cleansing strip products, including exports, suffered due partly to measures to normalize inventory at distributors, causing the *Bioré* line to fall short of prior-year levels. Overall, however, sales improved year-on-year due to healthy sales of *Jergens* lotions and *Curél*, as well as the addition from the acquisition and continuing smooth integration of the *ban* brand. A new premium line of moisturizers, *Jergens Firming Lotion*, also drove sales growth. Operating income also rose due mainly to rationalization of marketing spending.

At Goldwell, brisk sales of hair color products supported an increase in total sales. In addition, restructuring efforts initiated in fiscal 1999 enabled substantial improvement in operating income. At Guhl, sales of the *Brilliant* coloring shampoo/conditioner line increased, and the new *Guhl Living Color* hair color line launched during fiscal 2000 also performed well.

Fiscal 2000 Initiatives and Results

Andrew Jergens implemented measures to upgrade *Bioré* from a cleansing brand to a total facial care brand that includes moisturizers. A representative step was the launch of a new product designed to treat problem skin in young people, *Bioré Blemish Bomb Acne Treatment*. This helped restore consumer interest and confidence in *Bioré* as a total facial care brand.

Goldwell moved to increase marketing efficiency through the global rollout of marketing initiatives to its subsidiaries. Improvements of existing products were carried out and new color variations were added to the *Topchic* line.

Fiscal 2001 Issues and Objectives

Kao is applying its skin care technology to build the *Bioré*, *Jergens*, *Curél* and *ban* brands in the North American market. In January 2001, the new daytime treatment *Bioré Blemish Double Agent* was launched. Kao also intends to use its technologies in tandem with Andrew Jergens' marketing to build the *ban* brand in the U.S. antiperspirant/deodorant market. Goldwell will combine its capabilities with Kao's technological expertise in order to play a larger role in the expanding hair color market.

Solid Performers

Goldwell's hair care products for beauty salons

Guhl's premium hair care products

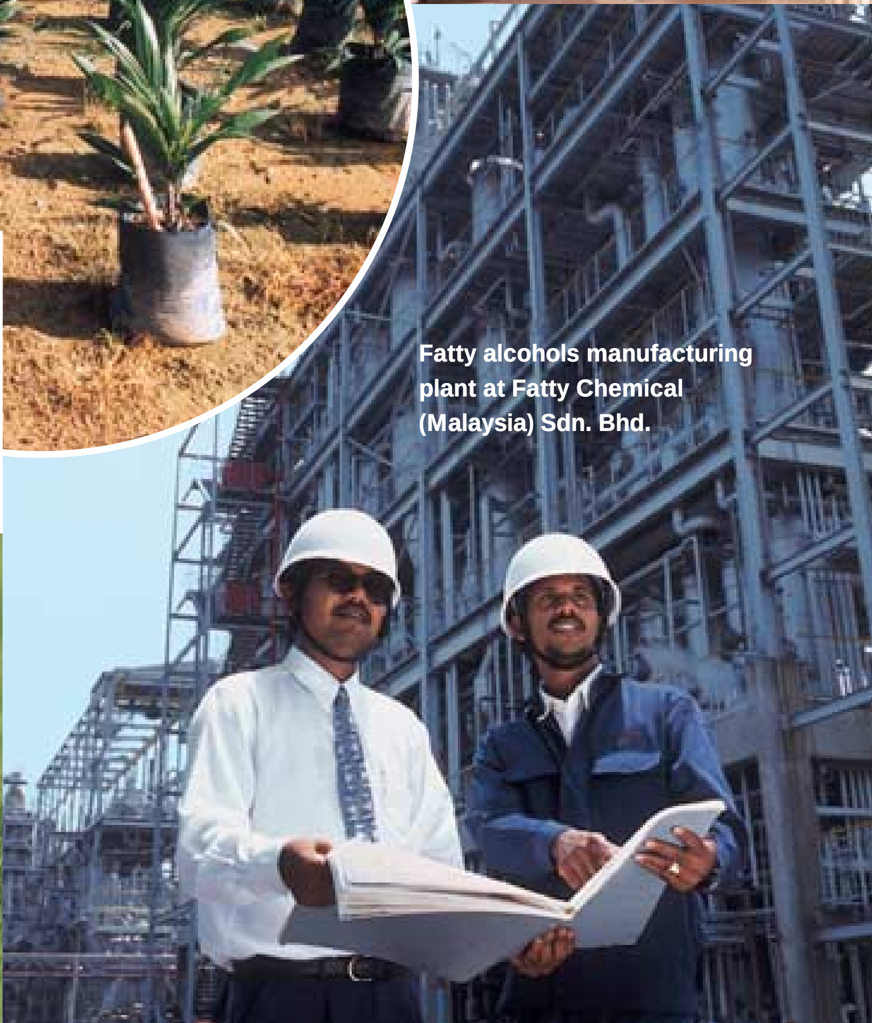
The *ban* brand antiperspirant/deodorant products

Chemical Products


Production facilities for aroma chemicals at Kao Corporation S.A., in Spain


Copier and printer toner and related products


Fats and oils extracted from palm kernels are used to produce fatty alcohols.


Fatty alcohols manufacturing plant at Fatty Chemical (Malaysia) Sdn. Bhd.


Shoe soles incorporate polyurethane that utilizes Kao's technology.

Focal Points

- Maintain strength in core businesses and increase specialization.
- Benefit from global production network and development capabilities to meet market requirements.
- Selectively concentrate on high-margin products and businesses where Kao is positioned to develop and excel.

Operating Environment and Performance

Although the rise in crude oil prices increased the cost of petrochemicals, prices for raw materials used in the production of fatty chemicals and edible oils remained favorable. The Japanese market has been weaker since summer 2000, and the slowdown in the U.S. economy has impacted Asian economies.

Fiscal 2000 Initiatives and Results

While Kao's sales in Japan decreased marginally year-on-year, earnings grew as a result of efforts to concentrate management resources on key businesses and the stabilization of low raw materials prices. Overseas sales grew strongly on a local currency basis, but were lower in yen terms due to the negative currency translation. The fatty chemicals and edible oils business, based mainly at Fatty Chemical (Malaysia) Sdn. Bhd., and strong sales of specialty chemical products, such as copier and printer toner and related products as well as aroma chemicals, drove record high earnings.

Fatty alcohols, glycerin and tertiary amines performed well worldwide. The edible oils business reached an optimal size in Japan. Sales of a newly developed conditioning and coagulating agent for tofu (bean curd) expanded, and diacylglycerol oil was supplied to food companies that manufacture co-branded products using *Healthy Econa Cooking Oil*.

Kao's copier and printer toner and related products meet requirements for performance at higher speeds and lower fusing temperatures, and sales have climbed steadily, generating solid profits. Kao has already strengthened the global management of its toner business through its flexible worldwide production network of facilities in Japan, the United States and Europe. Moreover, the Company has worked to enhance Asian operations by establishing in-market production and sales for such products as plastic additives and ethylene bis-stearamide (EBS) wax.

Sales of the synthetic fragrance lacton remained favorable. In the toiletry segment, ether sulfate, a raw material for shampoo, contributed negatively due to excess production capacity in the market.

Sales of de-inking agents in the pulp and paper segment were favorable, but sales of the *Mighty* line of concrete additives dropped due to reduced investment in public works projects in Japan, Thailand and the Shanghai metropolitan area in China.

Kao has made progress in consolidating management of operations in Europe with the establishment of Kao Chemicals Europe, S.L. in Spain. Specific outcomes have included joint purchasing and shipping, and partial integration of product lines.

Fiscal 2001 Issues and Objectives

Kao will promote its business activities from a standpoint of selectivity and focus in three core business fields: fatty chemicals, surfactants and specialty chemicals. Kao will further strengthen its global production network with the completion of production facilities for toner binder in Spain in 2001. Other investments include increased production capacity of synthetic fragrances in Spain, expanded production facilities for fatty alcohols at Fatty Chemical (Malaysia) Sdn. Bhd., and ester production facilities for toiletries at Kao Chemical Corporation Shanghai.

Solid Performers

Kao's copier and printer toner and related products are highly evaluated for their superior quality.

Aroma chemicals are sold to leading companies in addition to being used in Kao products.

Environmental Activities

The "3 Rs" Approach:

Reduce

Improved product performance allows greater concentration and smaller amounts required for a single load, while more compact packaging reduces waste.

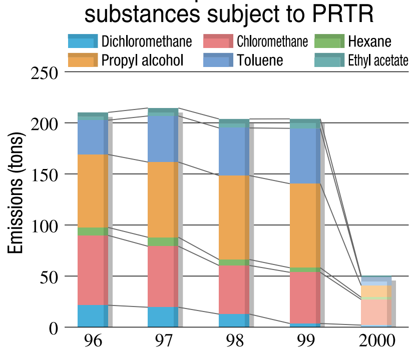
Reuse

Kao offers easy-to-use refill pouches in a variety of formats, such as hook-type (left) and press-line-processed type (right).

Recycle

Cartons and measuring spoons for *Attack* laundry detergent are made from 100% recycled materials.

Emissions and planned reductions of substances subject to PRTR



Environmental Philosophy and Policies

The development of products that will minimize impact on our air, earth and water is an integral part of Kao's basic philosophy as a manufacturer, and environmental protection is one of our most important tasks. The Company's efforts are based on the "3 Rs" approach: reduce, reuse, and recycle. Current activities center on the "reduce" approach.

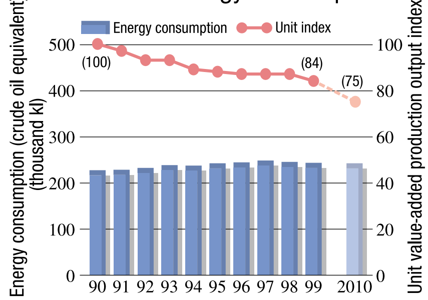
Production Process

By the end of April 2001, all of Kao's domestic plants had obtained ISO 14001 certification, an international standard for environmental management systems. This management system will help Kao improve all environment-related performance. Overseas, in addition to Kao (Taiwan) Corporation, which is already ISO 14001-compliant, Kao Chemicals GmbH in Germany is expected to acquire certification during fiscal 2001.

Moreover, company-wide environmental protection projects based on the principles of the "3 Rs" approach, such as resource and energy savings and industrial waste reduction, were incorporated into TCR activities. Aimed at reducing the burden on the environment without diminishing the basic functions and quality of Kao products or their containers, these TCR activities integrate environmental and corporate management.

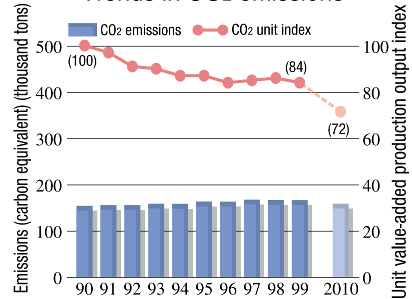
Reductions of CO_2 emissions and energy consumption are shown below. Although the absolute amount has not substantially changed, factoring in the increase in value-added production output shows a steady decrease in the unit energy consumption index. Kao has already achieved the target values set by the Japan Federation of Economic Organizations.

Trends in energy consumption



*Unit value-added production output = energy consumption/ value-added production output

Trends in CO_2 emissions



Pollutant Release and Transfer Register (PRTR)

During fiscal 1999 in Japan, Kao handled 58 of the 284 chemical substances listed by the Japan Chemical Industry Association (JCIA) as subject to PRTR reporting, and has reduced total annual emissions to less than one ton at each site. Reporting under the Chemical Substance Management Promotion Law in Japan will be required starting with fiscal 2001 data. Kao currently handles 51 of the substances on this list, which is different in part from that of the JCIA.

Product Safety

At Kao, ensuring product safety begins from the grand design stage. Selection of raw materials and product formula are based on four Company criteria: product safety standards; a list of restricted materials; safety standards for preservatives; and safety standards for fragrances. When developing new products, they are divided into those that rinse off for disposal, such as detergent, and those that do not, such as facial cream. Products are then evaluated by category for their impact on health and the environment. A safety commission makes a final pre-launch review, and Kao carries out post-marketing surveillance.

Original information on safety accumulated by Kao is archived in a database and managed systematically. The Company uses it for Material Safety Data Sheets (MSDS), which are prepared in compliance with Japanese Industrial Standards (JIS) and other relevant laws. Kao has published approximately 6,000 MSDS, which are provided to customers and kept in a database for use in employee training. English-language MSDS are also prepared in compliance with the regulations of the United States and the European Union.

Packaging and Contents

The consumer switching rate to refills (the percentage who purchase refill pouches or replacement bottles) for most Kao products in Japan exceeds 60 percent, contributing to a reduction in the amount of packaging waste. Kao's contribution to reducing waste and saving resources through promotion of refill products was recognized in an award from the Minister of International Trade and Industry (current Minister of Economy, Trade and Industry) in October 2000.

New Kao technologies include the world's first Paper-bottle Molding System, which uses waste paper to produce sealable bottles in various shapes that are as strong as plastic bottles.

A noteworthy content-related development is a new manufacturing process for ether that converts more than 99 percent of raw materials into ether, and the only waste product discharged is water.

Environmental Accounting

To conduct effective environmental management, Kao internally compiles data on investments and expenses related to environmental protection as well as their environmental preservation and economic effects. Since fiscal 1999, the Company has disclosed parent-company results in accordance with Japanese Environment Agency (current Ministry of the Environment) guidelines. Environmental preservation costs during fiscal 1999 included capital expenditures of ¥1,452 million, consisting primarily of water pollution prevention and new packaging development. Related expenses totaled ¥7,937 million, which included depreciation of ¥2,202 million. The economic effect was calculated only in terms of direct cost reductions and amounted to ¥1,692 million.

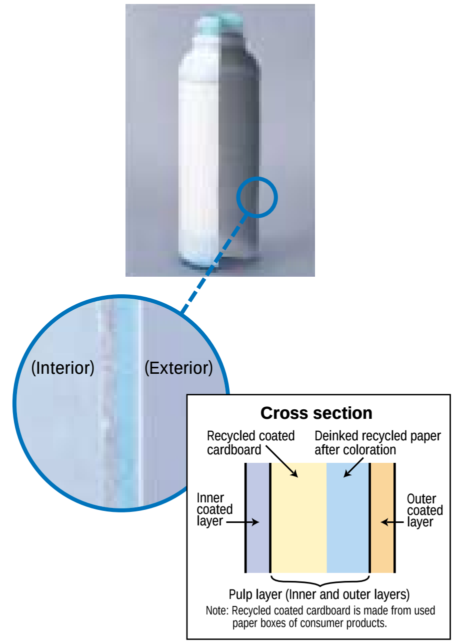
International Activities

Kao Specialties Americas LLC and High Point Textile Auxiliaries LLC have been recognized as the 23rd "Carolina Star Site" in the State of North Carolina in the United States. This designation is granted by the Occupational Safety and Health Division of the North Carolina Department of Labor (OSHNC) to companies with comprehensive and successful safety and health programs, established and implemented through a cooperative relationship among management, labor and the OSHNC. In addition, Quimi-Kao, S.A. de C.V. in Mexico was awarded Clean Industry certification by the Mexican government, which allows the company to use the Clean Industry logo in corporate identity materials.

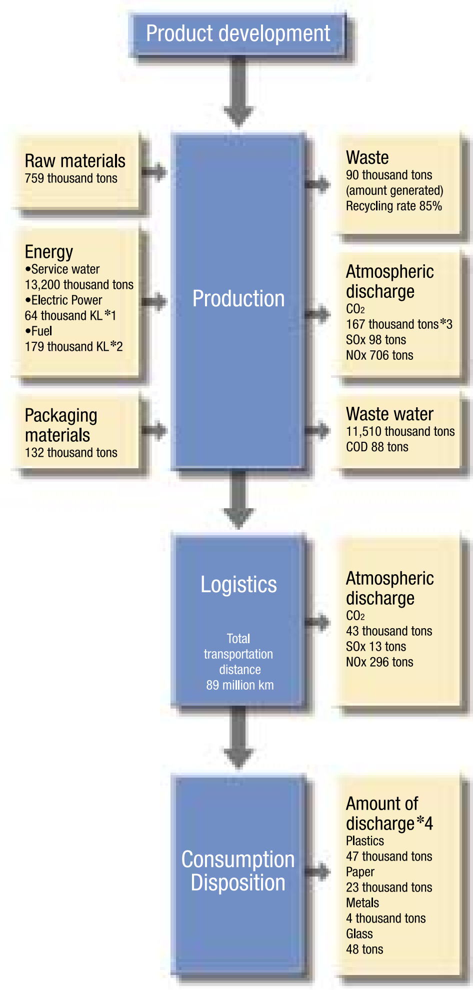
Kao's Basic Position Regarding the Environment

Kao took its long-standing commitment to manufacturing products in an environmentally responsible manner one step further with the introduction of Responsible Care activities in 1995. Since then, the Company has built a comprehensive management system encompassing environmental protection, occupational health and safety, disaster prevention and raw materials and product safety. The basic philosophy underlying these activities is a commitment to the environment, safety and health throughout the whole life cycle of products, from product development, manufacturing and distribution to final consumption and disposal.

Paper-bottle Molding System



Substance flow through business activities (in 1999)



*1) Equivalent to the amount of crude oil
*2) Equivalent to crude oil
*3) Equivalent to carbons
*4) The amount of each packaging material generated by households

Board of Directors and Corporate Auditors

President
and Representative Director
Takuya Goto

Senior Managing Director
and Representative Director
Toshio Hoshino

Managing Director
and Representative Director
Takahiko Kagawa

President
Takuya Goto*

Senior Managing Director
Toshio Hoshino*

Managing Directors
Takahiko Kagawa*
Masanori Sakata
Kunihiko Hachiya
Yasuo Idemitsu

Directors
Toshio Hirasaka
Moriyasu Murata
Akio Tsuruoka
Shigeo Yamada
Shozo Tanaka
Masatoshi Kitahara
Tadao Matsumoto
Kuniaki Watanabe
Nobuatsu Higuchi
Naotake Takaishi
Iwao Inoue
Tetsuya Imamura

Corporate Auditors
Kikuhiko Okamoto
Katsuhiko Hiraoka
Takashi Tajima
Hidejiro Matsuda

(As of June 28, 2001)

*Representative Director

Management's Discussion and Analysis

Six-Year Summary

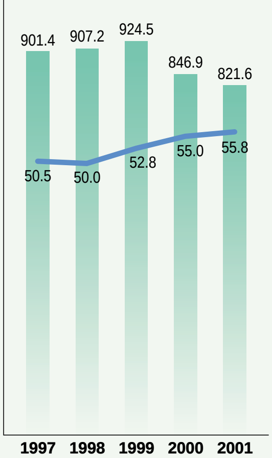
Kao Corporation and Consolidated Subsidiaries

Years ended March 31

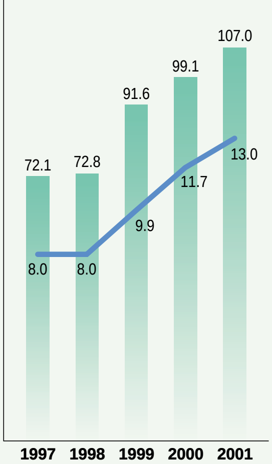
	Millions of yen					
	2001	2000	1999	1998	1997	1996
For the year:						
Net sales	**¥821,629**	¥846,922	¥924,596	¥907,249	¥901,402	¥835,597
Consumer Products	**607,826**	632,423	656,197	696,800	705,332	675,883
Cosmetics *Sofina*	**72,579**	70,890	74,450	—	—	—
Chemical Products	**167,893**	172,401	193,949	210,449	196,070	159,714
Subtotal	**848,298**	875,714	924,596	907,249	901,402	835,597
Eliminations	**(26,669)**	(28,792)	—	—	—	—
Japan	**655,470**	673,456	672,123	674,640	696,022	673,051
Asia and Oceania	**84,137**	86,176	104,694	101,726	83,588	69,589
North America and Europe	**105,287**	111,043	178,933	162,092	148,171	118,004
Subtotal	**844,894**	870,675	955,750	938,458	927,781	860,644
Eliminations	**(23,265)**	(23,753)	(31,154)	(31,209)	(26,379)	(25,047)
Operating income	**107,099**	99,182	91,664	72,868	72,101	66,509
Net income	**59,427**	52,147	34,714	24,495	27,594	24,531
Capital expenditures	**60,741**	37,564	69,016	59,012	65,283	79,254
Depreciation and amortization	**58,856**	67,270	71,202	81,405	73,592	70,623
Cash flows	**104,702**	108,158	96,310	97,046	93,073	87,950
Research and development expenditures	**37,049**	38,062	36,062	37,843	37,929	37,544
(% of Sales)	**4.5%**	4.5%	3.9%	4.2%	4.2%	4.5%
Advertising expenditures	**65,758**	64,354	71,752	65,404	61,012	58,592
(% of Sales)	**8.0%**	7.6%	7.8%	7.2%	6.8%	7.0%
At year-end:						
Total assets	**783,760**	750,016	751,725	778,762	807,124	756,849
Total shareholders' equity	**462,988**	474,979	451,777	424,430	379,552	359,812
	Yen					
Per share:						
Net income	**¥ 96.69**	¥ 83.45	¥ 55.98	¥ 40.10	¥ 45.92	¥ 40.85
Cash dividends	**24.00**	20.00	16.00	15.00	14.00	12.50
Total shareholders' equity	**760.05**	765.59	727.01	684.90	631.54	598.71
Weighted average number of shares outstanding during the period (in thousands)	**614,608**	624,917	620,171	610,857	600,978	600,454
Key financial ratios:						
Return on sales (%)	**7.2**	6.2	3.8	2.7	3.1	2.9
Return on equity (%)	**12.7**	11.3	7.9	6.1	7.5	7.0
Equity ratio (%)	**59.1**	63.3	60.1	54.5	47.0	47.5

Notes:
1. Net sales by business segment include intersegment sales starting from the year ended March 31, 2000, as defined in the notes to consolidated financial statements (Note 12). Consequently, net sales of Chemical Products include intersegment sales to Consumer Products and Cosmetics *Sofina*.
2. Cosmetics *Sofina* results for 1998 and prior years are consolidated under Consumer Products.
3. Net sales by geographic segment include intersegment sales.
4. Due to the change in the presentation requirements in Japan, certain reclassifications have been made to operating income for 1998 and prior years to conform to the presentation of the current year's results.
5. Cash flows are defined as net income plus depreciation and amortization minus cash dividends.
6. Net income per share is computed based on the weighted average number of shares outstanding during the respective years.
7. Cash dividends per share are the amounts applicable to the respective years, including dividends to be paid after the end of the year.

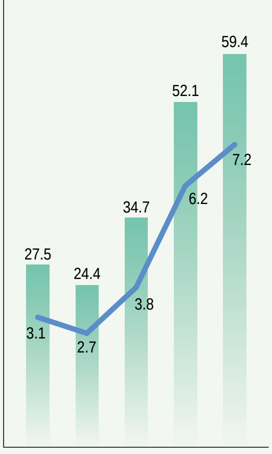
Net Sales/
Gross Profit Ratio
(Billions of yen, %)



Operating Income/
Operating Income Ratio
(Billions of yen, %)



Net Income/
Return on Sales
(Billions of yen, %)



Analysis of Income Statements

For the fiscal year ended March 31, 2001, consolidated net sales decreased 3.0 percent to ¥821.6 billion (US$6,631.4 million). A negative currency translation effect of ¥18.2 billion on overseas sales due to the strong yen affected net sales. In addition, due to a difference in accounting for sales at a newly consolidated domestic consumer products sales company, net sales decreased by ¥11.9 billion. Most of this amount consists of post-sales rebates paid to retailers, which were recorded as part of the parent company's sales commission expenses. Excluding these two factors, consolidated net sales would have risen 0.6 percent year-on-year. A decline in consumer products sales in Japan also negatively contributed to decreased sales.

Cost of sales amounted to ¥363.1 billion (US$2,930.8 million). The cost of sales ratio decreased 0.8 percentage points to 44.2 percent. Major factors behind this improvement included TCR activities and lower prices for raw materials. The decrease in cost of sales helped mitigate the impact of lower sales on gross profit, which decreased 1.6 percent to ¥458.5 billion (US$3,700.6 million).

Selling, general and administrative expenses (SG&A) decreased ¥15.1 billion, or 4.1 percent to ¥351.4 billion (US$2,836.2 million). Because of the new consolidation of the sales company, ¥86.2 billion in sales commissions paid to this company by the parent company were eliminated in consolidation. At the same time, the sales company's expenses, which were previously not recorded, increased SG&A expenses by ¥72.5 billion, and mainly consisted of personnel expenses such as salary and bonuses, freight-out expenses, and sales promotion costs. The result was a net decrease of ¥13.7 billion in SG&A expenses. However, as mentioned earlier, net sales also decreased by ¥11.9 billion due mainly to the effect of post-sales rebates. In other expenses, pension expenses increased, while depreciation expenses decreased.

Operating income therefore increased 8.0 percent to ¥107.0 billion (US$864.4 million). Operating income from operations in Japan increased 2.9 percent to ¥94.3 billion (US$761.3 million), while operating income from overseas operations increased 72.5 percent to ¥12.7 billion (US$102.6 million). Strong gains in profitability overseas were particularly pronounced in the personal care products business in North America and Europe and in the chemical products business worldwide. The Company benefited measurably from the improved operating efficiency, competitiveness and profitability engendered by business reform at overseas subsidiaries. The ratio of operating income to net sales rose to 13.0 percent from 11.7 percent for the previous fiscal year, as a result of the effectiveness of management initiatives to improve profitability.

Other expenses decreased 12.9 percent year-on-year to ¥5.2 billion (US$42.2 million). The Company booked a foreign exchange gain for the fiscal year under review, compared to a loss in the previous fiscal year, and decreased restructuring charges compensated for an extraordinary loss related to retirement benefits in Japan.

Consequently, income before income taxes and minority interests increased 9.3 percent to ¥101.8 billion (US$822.2 million), and net income increased 14.0 percent to ¥59.4 billion (US$479.6 million). Net income per share rose to ¥96.69 (US$0.78) from ¥83.45 for the previous fiscal year, and Kao increased cash dividends per share by ¥4.00 to ¥24.00 (US$0.19).

Costs, Expenses and Income as Percentages of Net Sales

	2001		2000		1999
Cost of sales	**44.2%**		45.0%		47.2%
Gross profit	**55.8**	**(0.8)**	55.0	(2.2)	52.8
Selling, general and administrative expenses	**42.8**	**(-0.5)**	43.3	(0.4)	42.9
Operating income	**13.0**	**(1.3)**	11.7	(1.8)	9.9
Income before income taxes and minority interests	**12.4**	**(1.4)**	11.0	(4.5)	6.5
Net income	**7.2**	**(1.0)**	6.2	(2.4)	3.8

Note: Figures in parentheses represent change in percentage points from the previous year.

Information by Business Segment

In accordance with a change in the Company's policy of segmentation mentioned in the notes to consolidated financial statements (Note 12), the segment information by business for the previous fiscal year has been restated. The following commentary is based on this change.

Consumer Products

Consumer products sales decreased 3.9 percent to ¥607.8 billion (US$4,905.8 million). In Japan, domestic sales decreased 3.5 percent year-on-year in nominal terms, while they decreased 1.2 percent from the previous fiscal year in real terms, excluding the effect of the consolidation of the consumer products sales company. Overseas, net sales on a local currency basis grew 3.5 percent over the previous fiscal year, although the effect of the strong yen led to a decrease in overall net sales. In terms of operating income, domestic and overseas operations achieved a total earnings growth of ¥4.0 billion, amounting to ¥86.1 billion (US$695.0 million), an increase of 4.9 percent.

Japan

In the consumer products market in Japan, prices continued to move downward, particularly in the second half of the term, and demand in real terms slumped below the level of the previous fiscal year. In this operating environment, sales of consumer products, excluding the effect from the consolidation of the sales company, declined 1.2 percent.

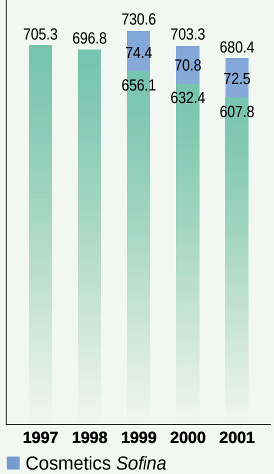
In terms of operating income, a decrease in selling prices and an increase in marketing expenses contributed negatively. A significant increase in pension expenses also dampened profitability. Nevertheless, favorable natural oil raw material prices and the Company's cost reduction measures and raised operating efficiency, in addition to the decrease in depreciation expenses, led to growth in operating income.

In personal care products in Japan, Kao activated the facial and body cleanser markets with products with a mildly acidic formulation. New products such as *Bioré Facial Foam Moisture Cream-in* and *Bioré Body Care Foam Moisture Cream-in* performed well. In hair care products, the Company improved and marketed *Essential Damage Care* shampoo/conditioner, which generated solid consumer response. Despite this, an overall drop in market prices caused sales to drop below the level of the previous fiscal year. At the same time, we expanded our share of the hair color market by the addition of *Blauné Aroma Hair Color* launched during the previous fiscal year, and sales increased as a result.

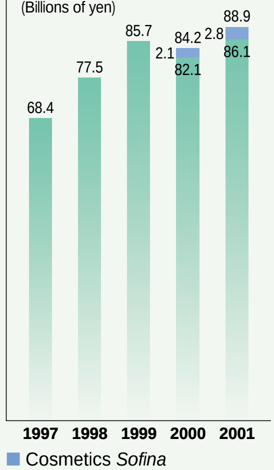
The laundry and cleaning products category in Japan faced intense competition. In this environment, such new products as *Humming 1/3 Anti-bacterial Plus* fabric softener, *Quickle Wet-type Floor Care Sheets* household cleaning sheets and *Family Pure Mild* dishwashing detergent were brought to market during the term. Although steady sales growth was posted for *New Beads*, a contraction of the gift market adversely affected sales and contributed to the year-on-year sales decline in laundry detergent. At the same time, exports of household cleaning mop kits and sheets, which are marketed in North America and Europe by S.C. Johnson & Son, Inc., decreased significantly due to the transfer to license-based production overseas.

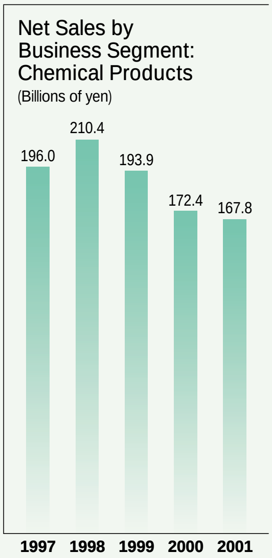
The hygiene and other products category had mixed results. The overall sanitary napkin market shrank due to a decline in the relevant consumer population in Japan, upgrading of product performance that led to fewer units being used, and falling prices. As a result, sales declined from the previous fiscal year. Sales of the Company's disposable baby diapers, *Merries* tape-type and pants-type, declined despite improvements made in product performance, as stiffening price competition and a sharp fall in prices made the environment extremely difficult. On the other hand, there was a slight increase in sales of adult incontinence products, which were spurred by the launch of *Relief Odor-Free Guard*, which uses an original technology to eliminate odors.

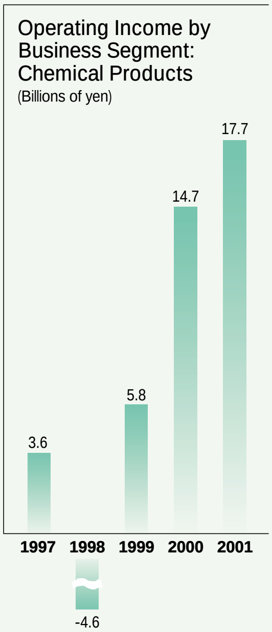
Net Sales by Business Segment: Consumer Products/Cosmetics *Sofina*
(Billions of yen)



Operating Income by Business Segment: Consumer Products/Cosmetics *Sofina*
(Billions of yen)







In addition, *Healthy Econa Cooking Oil – For Prevention of Fat Deposits*, a unique product that helps prevent fat from accumulating in the body, continued to win widespread support from consumers and contribute greatly to sales. With an eye toward expanding the market for healthy cooking oils, Kao brought out the second product in the *Healthy Econa* series, *Healthy Econa Cooking Oil – For Lower Cholesterol*, which helps lower the level of cholesterol in the blood and inhibits the accumulation of fat in the body. The Company also launched the *Healthy Econa Dressing* series.

Asia and Oceania

Influenced by the economic slowdown in the U.S., the outlook for the Asian economy has become unclear. In the consumer products market, while growth in demand was virtually stagnant, intense competition among global peer companies continued. In addition, new entries into the market by global retailers led to fierce price competition.

In the consumer products business in Asia and Oceania, inventory adjustment at distributors was completed in China. While sales before the currency translation effect achieved modest growth, sales in yen terms declined slightly.

The Company focused on core brands to strengthen brand power, and consequently, operating income for the region increased year-on-year in yen terms.

With an eye on trends in the ASEAN Free Trading Area (AFTA), we have established a subsidiary in Thailand as a regional headquarters that will enable us to integrate and upgrade product development and marketing, and utilize optimal production locations in the ASEAN region.

North America and Europe

In North America, sales of The Andrew Jergens Company grew slightly. Favorable performance by *Curél* premium skin care and new products in the *Jergens* lotions lineup contributed as growth drivers, which were offset by a continuing decrease in sales of pore cleansing strip products. To build a stronger base in the skin care products business, we acquired the *ban** antiperspirant/deodorant brand in the United States. Andrew Jergens achieved healthy growth in operating income as a result of a strong performance by premium-priced products and more effective control of fixed expenses.

In Europe, Goldwell GmbH, which markets hair care products for beauty salons internationally, and Guhl Ikebana GmbH, which markets premium hair care products, both posted healthy sales growth. The effect of restructuring at Goldwell bolstered steady growth in operating income.

Cosmetics *Sofina*

Sales of *Sofina* cosmetics were ¥72.5 billion (US$585.8 million), an increase of 2.4 percent. The prestige cosmetics market is recovering slowly from a major contraction, remaining flat throughout the year.

In these general market conditions, we brought out *est*, a new brand for exclusive marketing through department store channels in the basic skin care category. This product embodies unique superior technology based on dermatological research promoted by *Sofina*. New items were also added to the *Sofina Raycious* foundation series. Along with *Sofina Finefit*, this new introduction bolstered foundation sales, which increased over the level of the previous term. Although sales in the first half of the term decreased year-on-year due to our effort to streamline inventories at retailers, we achieved significant growth in the second half of the fiscal year under review.

Operating income improved to ¥2.8 billion (US$22.8 million) despite the expenses related to the retail destocking measures and an increase in pension expenses.

*Japan is not included in the agreement for the acquisition of the *ban* brand.

Chemical Products

Chemical products sales, including intersegment sales, decreased 2.6 percent to ¥167.8 billion (US$1,355.1 million). Operating income rose ¥2.9 billion, or 20.2 percent, to ¥17.7 billion (US$143.0 million). Although negative currency translations impacted both sales and operating income for overseas operations, on a local currency basis, sales grew 9.1 percent, and operating income rose 59.6 percent as well. Key growth drivers included fatty chemicals in Asia and such specialty chemicals as copier and printer toner and related products, and aroma chemicals in the United States, Europe and Japan.

Japan

The effects of sluggish economic conditions in Japan since last summer, and a drop in exports due to a slowdown of the Asian economies, led to a drop in the parent company's sales.

Operating income grew, benefiting from continuous favorable prices of raw materials for fatty chemicals and streamlined production, in spite of price increases in certain raw materials due to higher petroleum costs.

Asia

In Taiwan, sales decreased due to the transfer of part of production abroad. However, healthy growth in sales was recorded in the other Asian countries, particularly in Malaysia and the Philippines, where sales of fatty alcohols were brisk.

Led by the strong performance in fatty alcohols in Malaysia and the Philippines, and boosted by lower costs of raw materials, operating income increased significantly.

North America and Europe

Robust sales growth continued on the back of strong performances in copier and printer toner and related products in the United States, fatty amines in Germany, and aroma chemicals and copier and printer toner and related products in Spain.

Healthy growth in Germany and Spain was a primary factor in a surge in operating income.

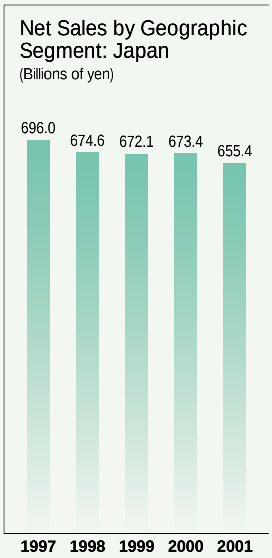
Information by Geographic Segment

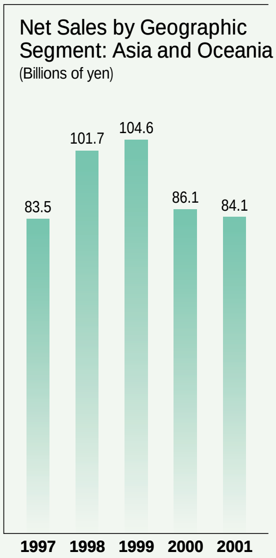
Japan

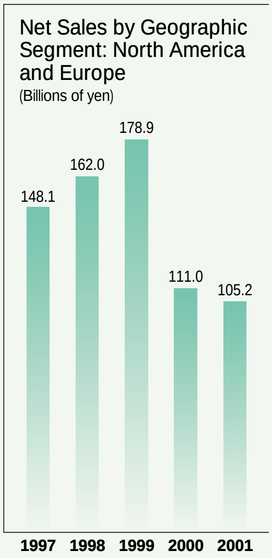
Total sales in Japan, including intersegment sales, decreased 2.7 percent to ¥655.4 billion (US$5,290.3 million). Excluding the effect of the consolidation of the sales company, total sales decreased 0.9 percent. Operating income increased ¥2.6 billion, or 2.9 percent, to ¥94.3 billion (US$761.3 million). Ongoing cost reductions, lower raw material prices and decreased depreciation expenses compensated for lower consumer products sales and increased pension-related expenses.

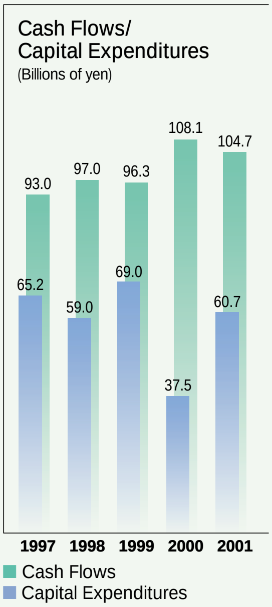
Asia and Oceania

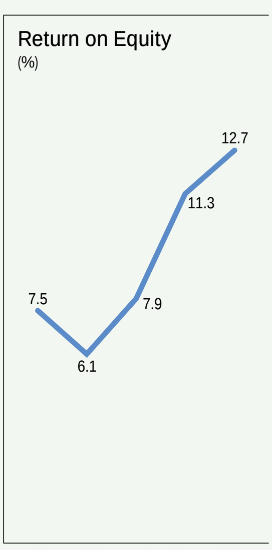
Total sales elsewhere in Asia and Oceania, including intersegment sales, decreased 2.4 percent to ¥84.1 billion (US$679.1 million). Excluding currency translation effect, sales rose 3.8 percent. Operating income increased ¥2.8 billion, or 74.0 percent, to ¥6.8 billion (US$54.9 million). Measures to concentrate resources on core brands in the consumer products business and the healthy growth in fatty chemicals sales contributed significantly to increased operating income.











North America and Europe

Total sales in North America and Europe, including intersegment sales, decreased 5.2 percent to ¥105.2 billion (US$849.8 million). Excluding currency translation effect, sales rose 7.4 percent. Operating income increased ¥2.4 billion, or 70.7 percent, to ¥5.9 billion (US$47.7 million), driven by the steady performance of premium skin care products at Andrew Jergens and the benefits of restructuring at Goldwell. Moreover, the chemical products business in Spain and Germany performed well.

Financial Position

Net cash provided by operating activities decreased to ¥122.9 billion (US$992.3 million) from ¥157.6 billion for the previous fiscal year. Negative factors included higher tax payments, decreased depreciation expenses, and an increase in working capital. These were partially offset by increased income before income taxes and minority interests.

Net cash used in investing activities increased to ¥67.3 billion (US$543.8 million) from ¥41.4 billion for the previous fiscal year, primarily because of the acquisition of the *ban* antiperspirant/deodorant brand from Chattem, Inc. and increased purchases of short-term securities as part of investment of excess cash. Principal capital spending in plant and equipment included production facilities for laundry detergent and new products such as cooking oil, and a plant relocation in Japan.

Net cash used in financing activities decreased to ¥52.1 billion (US$420.7 million) from ¥61.5 billion for the previous fiscal year. Kao redeemed corporate bonds, resulting in a reduction in short-term and long-term debt including current portion of ¥8.6 billion (US$69.9 million). In addition, aiming to enhance shareholders' returns, the Company executed a share redemption totaling 10 million shares valued at ¥28.6 billion. Payments of cash dividends increased from ¥11.4 billion in the previous fiscal year to ¥13.7 billion (US$111.3 million).

As a result, cash and cash equivalents at the end of the year increased ¥5.4 billion year-on-year to ¥153.4 billion (US$1,238.4 million).

Total assets increased 4.5 percent from a year earlier to ¥783.7 billion (US$6,325.7 million).

Shareholders' equity decreased 2.5 percent from a year earlier to ¥462.9 billion (US$3,736.8 million). While retained earnings and additional paid-in capital increased, the Company reclassified negative foreign currency translation adjustments totaling ¥35.6 billion from assets to shareholders' equity in the fiscal year under review. Return on average total shareholders' equity improved to 12.7 percent from 11.3 percent for the previous fiscal year, and the shareholders' equity ratio, defined as the ratio of shareholders' equity to total assets, stood at 59.1 percent, compared to 63.3 percent a year earlier.

EVA

Kao aims to achieve continuous improvement in EVA on a long-term basis that will lead to increasing corporate value. During the fiscal year under review, Kao focused on increasing net operating profit after taxes (NOPAT) while endeavoring to make more effective utilization of assets and hold down increases in capital charges. Measures undertaken resulted in the second consecutive improvement in EVA since its implementation.

Improve: Kao strives to improve operating profit without using additional capital. During the fiscal year under review, TCR activities continued to contribute significantly to improved profitability. Key activities included changes in product formulas and the rationalization of purchasing.

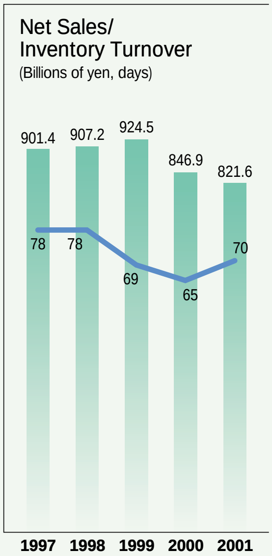
Invest: Major capital expenditures in Japan included production facilities for laundry detergents and cooking oil. In the overseas chemical products business, Kao also invested in selected sectors such as fatty alcohols, copier and printer toner and related products, and aroma chemicals. These investments are expected to contribute to future improvement of EVA.

Harvest: Kao has been working to reduce capital to improve EVA. During the fiscal year under review, Kao carried out relocation and consolidation of production facilities for laundry and cleaning products in Japan.

Financial: In this financial initiative to reduce capital charges, Kao executed a share redemption amounting to ¥28.6 billion during the fiscal year under review.

At the corporate level, Kao uses EVA as a main management measure for making strategic investment decisions and evaluating company performance. Strategic decisions during the fiscal year under review included the acquisition of antiperspirant/deodorant brand *ban*. At the tactical level, EVA is used in making daily operating decisions.

The implementation of an EVA-based management system has been successful in Japan and at a U.S. subsidiary, Andrew Jergens. The next step is a rollout to several overseas subsidiaries, which is under way.



Forward-Looking Statements

This report contains forward-looking statements that are based on management's estimates, assumptions and projections at the time of publication. Some factors, which include, but are not limited to, the risks and uncertainty associated with the worldwide economy, competitive activity and currency fluctuation, could cause actual results to differ materially from expectations.

Consolidated Balance Sheets

Kao Corporation and Consolidated Subsidiaries
March 31, 2001 and 2000

Assets	Millions of yen 2001	Millions of yen 2000	Thousands of U.S. dollars (Note 2) 2001
Current assets:			
Cash and time deposits	¥ 16,600	¥ 21,004	$ 133,979
Short-term investments (Notes 3 and 5)	156,650	139,194	1,264,326
Notes and accounts receivable:			
Trade (Note 6)	100,731	57,745	813,002
Nonconsolidated subsidiaries and affiliates	2,794	31,250	22,551
Inventories			
Finished goods	46,959	44,024	379,007
Work in process and raw materials	22,944	23,790	185,182
Deferred income taxes (Note 7)	9,796	6,980	79,064
Other current assets	11,660	9,009	94,108
Allowance for doubtful receivables	(1,923)	(1,676)	(15,521)
Total current assets	366,211	331,320	2,955,698
Property, plant and equipment, at cost (Note 6)**:**			
Land	76,509	61,096	617,506
Buildings and structures	272,193	252,167	2,196,877
Machinery, equipment and other	641,530	633,514	5,177,805
Construction in progress	12,493	7,243	100,831
	1,002,725	954,020	8,093,019
Accumulated depreciation	(704,767)	(671,067)	(5,688,192)
	297,958	282,953	2,404,827
Intangible assets:			
Goodwill	25,230	25,096	203,632
Trademarks	25,564	13,093	206,328
Excess of investment cost over net equity of consolidated subsidiaries acquired, net	—	1,054	—
Other intangible assets	6,576	7,367	53,075
	57,370	46,610	463,035
Investments and other assets:			
Investment securities (Note 5)	30,143	9,226	243,285
Investments in and advances to nonconsolidated subsidiaries and affiliates	7,069	15,341	57,054
Deferred income taxes (Note 7)	13,396	10,920	108,119
Other assets	11,613	8,917	93,729
	62,221	44,404	502,187
Foreign currency translation adjustments	—	44,729	—
	¥ 783,760	¥750,016	$6,325,747

See notes to consolidated financial statements.

Liabilities and Shareholders' Equity	Millions of yen 2001	Millions of yen 2000	Thousands of U.S. dollars (Note 2) 2001
Current liabilities:			
Short-term debt (Note 6)	**¥ 13,792**	¥ 8,914	**$ 111,316**
Current portion of long-term debt (Note 6)	**12,480**	10,196	**100,726**
Notes and accounts payable:			
Trade	**68,266**	71,886	**550,977**
Nonconsolidated subsidiaries and affiliates	**2,466**	2,446	**19,903**
Other	**27,895**	16,983	**225,141**
Accrued income taxes	**28,106**	26,146	**226,844**
Accrued expenses	**62,290**	53,742	**502,744**
Other current liabilities (Note 6)	**15,299**	16,070	**123,479**
Total current liabilities	**230,594**	206,383	**1,861,130**
Long-term liabilities:			
Long-term debt (Note 6)	**43,142**	58,960	**348,200**
Liability for employee retirement benefits (Note 9)	**14,596**	2,327	**117,805**
Liability for director and corporate auditor retirement benefits (Note 9)	**367**	973	**2,962**
Other (Note 6)	**11,351**	744	**91,614**
	69,456	63,004	**560,581**
Minority interests	**20,722**	5,650	**167,248**
Contingent liabilities (Note 10)			
Shareholders' equity (Notes 6, 11 and 16)**:**			
Common stock:			
Authorized — 980,000,000 shares in 2001 and 990,000,000 shares in 2000			
Issued — 610,826,451 shares in 2001 and 620,433,369 shares in 2000, with par value of ¥50 per share	**85,409**	85,147	**689,338**
Additional paid-in capital	**108,873**	108,612	**878,717**
Retained earnings	**298,687**	281,282	**2,410,710**
Unrealized gain on available-for-sale securities	**6,050**	—	**48,830**
Foreign currency translation adjustments	**(35,626)**	—	**(287,538)**
	463,393	475,041	**3,740,057**
Treasury stock, at cost (1,674,317 shares in 2001 and 20,947 shares in 2000)	**(405)**	(62)	**(3,269)**
	462,988	474,979	**3,736,788**
	¥783,760	¥750,016	**$6,325,747**

Consolidated Statements of Income

Kao Corporation and Consolidated Subsidiaries
Years ended March 31, 2001 and 2000

	Millions of yen		Thousands of U.S. dollars (Note 2)
	2001	2000	**2001**
Net sales (Note 12)	**¥821,629**	¥846,922	**$6,631,388**
Cost of sales	**363,122**	381,191	**2,930,767**
Gross profit	**458,507**	465,731	**3,700,621**
Selling, general and administrative expenses (Note 13)	**351,408**	366,549	**2,836,222**
Operating income (Note 12)	**107,099**	99,182	**864,399**
Other (income) expenses (Note 14):			
Interest and dividend income	**(2,098)**	(1,801)	**(16,933)**
Interest expense	**2,195**	2,852	**17,716**
Foreign currency exchange (gain) loss	**(1,331)**	3,096	**(10,742)**
Equity in earnings of nonconsolidated subsidiaries and affiliates	**(1,102)**	(1,836)	**(8,894)**
Supplemental expense for retirement benefit	**5,772**	—	**46,586**
Restructuring charges related to consumer products business in North America and Europe	**—**	2,647	**—**
Other, net	**1,792**	1,043	**14,463**
	5,228	6,001	**42,196**
Income before income taxes and minority interests	**101,871**	93,181	**822,203**
Income taxes (Note 7):			
Current	**51,193**	41,214	**413,180**
Deferred	**(10,029)**	(650)	**(80,945)**
	41,164	40,564	**332,235**
Income before minority interests	**60,707**	52,617	**489,968**
Minority interests in earnings of consolidated subsidiaries	**1,280**	470	**10,331**
Net income	**¥ 59,427**	¥ 52,147	**$ 479,637**
Per share of common stock (Note 1.o):	Yen		U.S. dollars (Note 2)
Net income	**¥96.69**	¥83.45	**$0.78**
Fully diluted net income	**93.02**	80.01	**0.75**
Cash dividends applicable to the year	**24.00**	20.00	**0.19**

See notes to consolidated financial statements.

Consolidated Statements of Shareholders' Equity

Kao Corporation and Consolidated Subsidiaries
Years ended March 31, 2001 and 2000

	Thousands	Millions of yen					
	Number of shares of common stock issued	Common stock	Additional paid-in capital	Retained earnings	Unrealized gain on available-for-sale securities	Foreign currency translation adjustments	Treasury stock, at cost
Balance at April 1, 1999	621,439	¥79,148	¥102,622	¥270,056	¥ —	¥ —	¥ (49)
Retained earnings of affiliates previously not accounted for by the equity method				(35)			
Net income				52,147			
Cash dividends, ¥18.00 per share (Note 11)				(11,260)			
Directors' and corporate auditors' bonuses				(124)			
Conversion of convertible bonds	8,994	5,999	5,990				
Purchase and redemption of treasury stock (Note 11)	(10,000)			(29,502)			
Treasury stock acquired, net (1,390 shares)							(13)
Balance at March 31, 2000	620,433	85,147	108,612	281,282	—	—	(62)
Retained earnings of consolidated subsidiaries previously not consolidated at beginning of year				**367**			
Net income				**59,427**			
Unrealized gain on available-for-sale securities, less applicable tax					**6,050**		
Changes in foreign currency translation						**(35,626)**	
Cash dividends, ¥22.00 per share (Note 11)				**(13,580)**			
Directors' and corporate auditors' bonuses				**(167)**			
Conversion of convertible bonds	**393**	**262**	**261**				
Purchase and redemption of treasury stock (Note 11)	**(10,000)**			**(28,642)**			
Treasury stock acquired, net (1,653,370 shares)							**(343)**
Balance at March 31, 2001	**610,826**	**¥85,409**	**¥108,873**	**¥298,687**	**¥6,050**	**¥(35,626)**	**¥(405)**

	Thousands	Thousands of U.S. dollars (Note 2)					
	Number of shares of common stock issued	Common stock	Additional paid-in capital	Retained earnings	Unrealized gain on available-for-sale securities	Foreign currency translation adjustments	Treasury stock, at cost
Balance at March 31, 2000	620,433	$687,224	$876,610	$2,270,234	$ —	$ —	$ (500)
Retained earnings of consolidated subsidiaries previously not consolidated at beginning of year				**2,962**			
Net income				**479,637**			
Unrealized gain on available-for-sale securities, less applicable tax					**48,830**		
Changes in foreign currency translation						**(287,538)**	
Cash dividends, US$0.178 per share (Note 11)				**(109,605)**			
Directors' and corporate auditors' bonuses				**(1,348)**			
Conversion of convertible bonds	**393**	**2,114**	**2,107**				
Purchase and redemption of treasury stock (Note 11)	**(10,000)**			**(231,170)**			
Treasury stock acquired, net (1,653,370 shares)							**(2,769)**
Balance at March 31, 2001	**610,826**	**$689,338**	**$878,717**	**$2,410,710**	**$48,830**	**$(287,538)**	**$(3,269)**

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

Kao Corporation and Consolidated Subsidiaries
Years ended March 31, 2001 and 2000

	Millions of yen		Thousands of U.S. dollars (Note 2)
	2001	2000	**2001**
Operating activities:			
Income before income taxes and minority interests	**¥101,871**	¥ 93,181	**$ 822,203**
Adjustments for:			
Income taxes paid	**(47,877)**	(27,832)	**(386,416)**
Depreciation and amortization	**58,856**	67,270	**475,028**
Loss on sales or disposals of property, plant and equipment	**2,682**	1,513	**21,647**
Equity in earnings of nonconsolidated subsidiaries and affiliates	**(1,102)**	(1,836)	**(8,894)**
Unrealized foreign currency exchange loss	**849**	3,048	**6,852**
Change in trade receivables	**(6,368)**	(169)	**(51,396)**
Change in inventories	**(940)**	10,385	**(7,587)**
Change in trade payables	**(4,274)**	2,705	**(34,495)**
Change in liability for retirement benefits	**11,775**	(312)	**95,036**
Other, net	**7,479**	9,666	**60,363**
Net cash provided by operating activities	**122,951**	157,619	**992,341**
Investing activities:			
Purchase of marketable securities	**(37,457)**	(11,087)	**(302,316)**
Proceeds from the redemption of bonds	**23,478**	—	**189,492**
Purchase of property, plant and equipment	**(41,283)**	(38,086)	**(333,196)**
Proceeds from sales of property, plant and equipment	**5,790**	2,250	**46,731**
Increase in intangible assets	**(18,529)**	(1,825)	**(149,548)**
Increase in investment in and advances to nonconsolidated subsidiaries and affiliated companies	**(673)**	(787)	**(5,432)**
Change in other investments	**1,301**	8,094	**10,500**
Net cash used in investing activities	**(67,373)**	(41,441)	**(543,769)**
Financing activities:			
Change in short-term debt	**4,169**	(3,632)	**33,648**
Repayments of long-term loans	**(1,298)**	(4,732)	**(10,476)**
Repayments of medium-term notes	**(13,448)**	(12,258)	**(108,539)**
Sales of treasury stock	**863**	—	**6,965**
Purchase of treasury stock	**(28,621)**	(29,514)	**(231,001)**
Payments of cash dividends	**(13,790)**	(11,405)	**(111,299)**
Net cash used in financing activities	**(52,125)**	(61,541)	**(420,702)**
Translation adjustments on cash and cash equivalents	**1,960**	(4,065)	**15,819**
Net increase in cash and cash equivalents	**5,413**	50,572	**43,689**
Cash and cash equivalents of newly consolidated subsidiaries, beginning of year	**35**	—	**282**
Cash and cash equivalents, beginning of year (Note 3)	**147,986**	97,414	**1,194,399**
Cash and cash equivalents, end of year (Note 3)	**¥153,434**	¥147,986	**$1,238,370**
Noncash financing activities:			
Convertible bonds converted into common stock and additional paid-in capital	**¥ 523**	¥ 11,989	**$ 4,221**

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Kao Corporation and Consolidated Subsidiaries
Years ended March 31, 2001 and 2000

1. Summary of Significant Accounting Policies

a) Basis of presenting consolidated financial statements

The accompanying consolidated financial statements have been prepared in accordance with the provisions set forth in the Japanese Securities and Exchange Law and its related accounting regulations, and in conformity with accounting principles and practices generally accepted in Japan, which are different in certain respects as to application and disclosure requirements of International Accounting Standards. The consolidated financial statements are not intended to present the financial position, results of operations and cash flows in accordance with accounting principles and practices generally accepted in countries and jurisdictions other than Japan.

In preparing the consolidated financial statements, certain reclassifications and rearrangements have been made to the consolidated financial statements issued in Japan in order to present them in a form that is more familiar to readers outside Japan. In accordance with accounting procedures generally accepted in Japan, certain comparative disclosures are not required to be and have not been presented herein. Certain 2000 financial statement items were reclassified to conform to the presentation for 2001.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from estimates.

b) Consolidation and investments in nonconsolidated subsidiaries and affiliates

The accompanying consolidated financial statements include the accounts of Kao Corporation (the "Company") and its significant subsidiaries (collectively, the "Companies"). Investments in most of the nonconsolidated subsidiaries and affiliates over which the Companies have the ability to exercise significant influence (mainly 20-50 percent owned companies) are accounted for using the equity method.

Under the control or influence concept, a company in which the parent company and/or its consolidated subsidiaries, directly or indirectly, are able to exercise control over operations is fully consolidated, and other companies over which the Company and/or its consolidated subsidiaries have the ability to exercise significant influence is accounted for by the equity method.

Investments in the remaining subsidiaries and affiliates are stated at cost except that write-downs are recorded for the value of investments that have been permanently impaired. If the equity method of accounting had been applied to these investments, the effect on the accompanying consolidated financial statements would not be material.

All significant intercompany balances and transactions have been eliminated in consolidation. All material unrealized profit included in assets resulting from transactions within the Companies is eliminated. The excess of cost of investments in the subsidiaries and affiliates over the fair value of the net assets of the acquired subsidiary at the dates of acquisition is being amortized over an estimated period not exceeding 20 years, or 5 years in situations in which the useful lives cannot be estimated.

c) Cash equivalents

For purposes of the statements of cash flows, cash equivalents are short-term investments that are readily convertible into cash and that are exposed to insignificant risk of changes in value.

Cash equivalents include time deposits and investment trusts in bonds that are represented as short-term investments, all of which mature or become due within three months of the date of acquisition.

d) Inventories

Inventories are stated at the lower of cost or market. Cost is determined principally by the average method. The cost of inventories held by certain foreign consolidated subsidiaries is determined by the first-in, first-out method.

e) Short-term investments and investment securities

Prior to April 1, 2000, short-term investments and investment securities were stated at cost, determined by the average method.

Effective April 1, 2000, the Companies adopted a new accounting standard for financial instruments, including short-term investments and investment securities.

The standard requires all applicable securities to be classified and accounted for, depending on management's intent, as follows: i) trading securities, which are held for the purpose of earning capital gains in near term, are reported at fair value, and the related unrealized gains and losses are included in earnings, ii) held-to-maturity debt securities, which are expected to be held to maturity with the positive intent and ability to hold to maturity are reported at amortized cost and iii) available-for-sale securities, which are not classified as either of the aforementioned securities, are reported at fair value, with unrealized gains and losses, net of applicable taxes, reported in a separate component of shareholders' equity. Short-term investments classified as current assets decreased by ¥1,082 million (US$8,733 thousand) and investment securities increased by the same amount as of April 1, 2000.

f) Property, plant and equipment

Property, plant and equipment are stated at cost. Depreciation of property, plant and equipment is computed under the declining-balance method for the assets located in Japan and principally under the straight-line method for the assets located outside Japan, using rates based upon the estimated useful lives, ranging from 21 to 35 years for buildings and structures and 7 or 9 years for machinery and equipment.

g) Intangible assets

Goodwill and trademarks are amortized on a straight-line basis principally over 20 years and 10 years, respectively, except that appropriate write-downs are recorded for the value of goodwill which has been permanently impaired.

h) Retirement and pension plans

The Company and domestic consolidated subsidiaries have a defined benefit pension plan covering substantially all of their employees. The pension plan also covers employees of certain nonconsolidated subsidiaries and affiliates in Japan. Directors and corporate auditors are partially covered by the pension plan.

Certain foreign subsidiaries have local pension plans covering their employees. The policies for the funded pension plans are to fund and charge to income the pension costs determined on an actuarial method.

Certain foreign subsidiaries also have local employees' retirement benefit plans and provide for the amount to state the liability for these employees' retirement benefits, primarily determined on an actuarial method.

Under the employees' retirement plans for the Company and domestic consolidated subsidiaries, prior to April 1, 2000, the annual provision for retirement benefits is calculated to state the liability at the amount that would be required if all employees voluntarily terminated their employment at each balance sheet date.

Effective April 1, 2000, the Companies adopted a new accounting standard for employees' retirement benefits and accounted for the liability for retirement benefits based on the projected benefit obligations and plan assets at the balance sheet date.

The unrecognized transitional obligation of ¥60,316 million (US$486,812 thousand), determined as of the beginning of the year, is being amortized over 15 years, and the amortization is presented as cost of sales and selling, general and administrative expenses in the consolidated statements of income. As a result, net periodic benefit costs as compared with the prior method, increased by ¥10,520 million (US$84,907 thousand) and income before income taxes and minority interests decreased by ¥10,209 million (US$82,397 thousand).

Retirement benefits to directors and corporate auditors are provided at the amount which would be required if all directors and corporate auditors retired at the balance sheet date.

i) Income taxes

The Companies provide for income taxes applicable to all items included in the consolidated statements of income regardless of when such taxes are payable. Income taxes based on temporary differences between tax and financial reporting purposes are reflected as deferred income taxes in the consolidated financial statements using the asset and liability method.

j) Leases

All leases are accounted for as operating leases. Under Japanese accounting standards for leases, finance leases that deem to transfer ownership of the leased property to the lessee are to be capitalized, while other finance leases are permitted to be accounted for as operating lease transactions if certain “as if capitalized” information is disclosed (see Note 8).

k) Appropriation of retained earnings

Appropriation of retained earnings at each year end is reflected in the financial statements for the following year upon shareholders' approval.

l) Foreign currency transactions

Prior to April 1, 2000, short-term receivables and payables denominated in foreign currencies were translated into Japanese yen at the current exchange rates at each balance sheet date, while long-term receivables and payables denominated in foreign currencies were translated at historical rates.

Effective April 1, 2000, the Companies adopted a revised accounting standard for foreign currency transactions. In accordance with the revised standard, all short-term and long-term monetary receivables and payables denominated in foreign currencies are translated into Japanese yen at the exchange rates at the balance sheet date. The foreign exchange gains and losses from translation are recognized in the consolidated statements of income to the extent that they are not hedged by foreign exchange derivatives. The adoption of revised accounting standards for foreign currency transactions did not have a material effect on the accompanying consolidated financial statements.

m) Foreign currency financial statements

The balance sheet accounts of the consolidated foreign subsidiaries are translated into Japanese yen at the current exchange rate as of the balance sheet date except for shareholders' equity, which is translated at the historical rate.

Prior to April 1, 2000, differences arising from such translations were shown as "Foreign currency translation adjustments" as either asset or liability in the consolidated balance sheet.

Effective April 1, 2000, such differences are shown as "Foreign currency translation adjustments" in a separate component of shareholders' equity in accordance with the revised accounting standard for foreign currency transactions.

Revenue and expense accounts of consolidated foreign subsidiaries are translated into Japanese yen at the annual average exchange rate.

n) Derivatives and hedging activities

The Companies use derivative financial instruments to manage their exposures to fluctuations in foreign exchange and interest rates. Foreign exchange forward contracts, foreign currency swaps, interest rate swaps and interest rate caps are utilized by the Companies to reduce foreign currency exchange and interest rate risks. The Companies do not enter into derivatives for trading purposes or speculative purposes.

Effective April 1, 2000, the Companies adopted a new accounting standard for financial instruments and a revised accounting standard for foreign currency transactions. These standards require that: a) all derivatives be recognized as either assets or liabilities and measured at fair value, and gains or losses on derivative transactions are recognized in the consolidated statements of income and b) for derivatives used for hedging purposes, if derivatives qualify for hedge accounting because of high correlation and effectiveness between the hedging instruments and the hedged items, gains or losses on derivatives are deferred until the maturity of the hedged transactions.

Short-term and long-term loans receivable denominated in foreign currencies for which foreign exchange forward contracts or foreign currency swaps are used to hedge the foreign currency fluctuations are translated at the contracted rate if the forward contracts or the swap contracts qualify for specific hedge accounting.

The interest rate swaps which qualify for hedge accounting and meet specific matching criteria are not remeasured at market value but the differential paid or received under the swap agreements are recognized and included in interest expense or income as incurred.

The adoption of the new accounting standards for financial instruments did not have a material effect on the accompanying consolidated financial statements.

o) Per share of common stock

Net income per share is computed on the basis of the weighted average number of shares of common stock outstanding during the respective years. Fully diluted net income per share of common stock assumes full conversion of the outstanding convertible bonds at the beginning of the year or at the date of issuance with an applicable adjustment for related interest expense.

Cash dividends per share presented in the accompanying consolidated statements of income are dividends applicable to the respective years including dividends to be paid after the end of the year.

2. Translation into United States Dollars

The Companies' accounts are maintained in or translated into Japanese yen. The United States dollar ($) amounts included herein represent translations using the approximate exchange rate at March 31, 2001 of ¥123.90=US$1, solely for convenience. The translations should not be construed as representations that Japanese yen have been, could have been or could in the future be converted into United States dollars at that or any other rate.

3. Cash and Cash Equivalents

Cash and cash equivalents at March 31, 2001 and 2000 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2001	2000	**2001**
Cash and time deposits	**¥ 16,600**	¥ 21,004	**$ 133,979**
Short-term investments	**156,650**	139,194	**1,264,326**
Less: cash deposits and short-term investments which mature or become due over three months after the date of acquisition	**(19,816)**	(12,212)	**(159,935)**
Cash and cash equivalents	**¥153,434**	¥147,986	**$1,238,370**

4. Supplemental Cashflow Information

The Company acquired additional stock of Kao Hanbai Company, Ltd., which is newly consolidated in 2001.

The breakdown of assets and liabilities of Kao Hanbai Company, Ltd. as of April 1, 2000 was as follows:

	Millions of yen	Thousands of U.S. dollars
Current assets	**¥ 43,682**	**$ 352,558**
Non-current assets	**30,910**	**249,475**
Current liabilities	**(41,707)**	**(336,618)**
Long-term liabilities	**(6,479)**	**(52,292)**
Negative goodwill	**(1,526)**	**(12,316)**
Minority interest	**(15,809)**	**(127,595)**
Acquisition of stock	**9,071**	**73,212**
Stock previously acquired	**(8,826)**	**(71,235)**
Stock acquired during the year	**245**	**1,977**
Cash and cash equivalent of Kao Hanbai Company, Ltd.	**(248)**	**(2,001)**
Net cash increase by acquisition of stock	**¥ (3)**	**$ (24)**

5. Short-Term Investments and Investment Securities

Short-term investments and investment securities as of March 31, 2001 and 2000 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2001	2000	**2001**
Short-term investments:			
Marketable equity securities	**¥ 68**	¥ 367	**$ 549**
Government and corporate bonds	**19,275**	11,192	**155,569**
Investment trust funds and other	**137,307**	127,635	**1,108,208**
	¥156,650	¥139,194	**$1,264,326**
Investment securities:			
Marketable equity securities	**¥20,302**	¥9,226	**$163,858**
Government and corporate bonds	**759**	—	**6,126**
Investment trust funds and other	**9,082**	—	**73,301**
	¥30,143	¥9,226	**$243,285**

The carrying amount and aggregate fair value of the securities classified as available-for-sale and held-to-maturity at March 31, 2001 were as follows:

	Millions of yen			
	2001			
	Cost	Unrealized gains	Unrealized losses	Fair value
Securities classified as:				
Available-for-sale:				
Equity securities	**¥ 9,691**	**¥11,267**	**¥613**	**¥20,345**
Debt securities	**9,253**	**104**	**—**	**9,357**
Held-to-maturity:				
Debt securities	**¥18,984**	**¥ 10**	**¥ 1**	**¥18,993**

	Thousands of U.S. dollars			
	2001			
	Cost	Unrealized gains	Unrealized losses	Fair value
Securities classified as:				
Available-for-sale:				
Equity securities	**$ 78,216**	**$90,936**	**$4,947**	**$164,205**
Debt securities	**74,681**	**839**	**—**	**75,520**
Held-to-maturity:				
Debt securities	**$153,220**	**$ 81**	**$ 8**	**$153,293**

Available-for-sale securities whose fair values are not readily determinable as of March 31, 2001 were as follows:

	Carrying amount	
	Millions of yen	Thousands of U.S. dollars
	2001	2001
Available-for-sale:		
Equity securities	**¥ 483**	**$ 3,898**
Debt securities	**130,624**	**1,054,270**
	¥131,107	**$1,058,168**

The carrying values of debt securities by contractual maturities for securities classified as available-for-sale and held-to-maturity at March 31, 2001 were as follows:

	Millions of yen		Thousands of U.S. dollars	
	2001		2001	
	Available-for-sale	Held-to-maturity	Available-for-sale	Held-to-maturity
Due within one year	**¥ 290**	**¥18,984**	**$2,341**	**$153,220**
Due after one year through five years	**759**	**—**	**6,126**	**—**
	¥1,049	**¥18,984**	**$8,467**	**$153,220**

Carrying amounts and aggregate market values of current and non-current marketable securities included in short-term investments and investment securities at March 31, 2000 were as follows:

	Millions of yen		
	2000		
	Carrying amount	Aggregate market value	Unrealized gain (loss)
Current	¥ 1,778	¥ 1,849	¥ 71
Non-current	8,741	25,439	16,698
	¥10,519	¥27,288	¥16,769

The difference between the above carrying value and the amounts shown in the accompanying consolidated balance sheets principally consisted of money management funds and non-marketable securities whose fair values are not readily determinable.

6. Short-Term and Long-Term Debt

Short-term debt at March 31, 2001 and 2000 comprised the following:

	Millions of yen		Thousands of U.S. dollars
	2001	2000	**2001**
Mortgage loans principally from banks	**¥ 148**	¥ —	**$ 1,195**
Bank borrowings	**13,644**	8,914	**110,121**
	¥13,792	¥8,914	**$111,316**

The weighted average interest rates applicable to the bank borrowings were 5.96% and 5.80% at March 31, 2001 and 2000, respectively.

Besides the above short-term debt, deposits payable to affiliated companies were included in other current liabilities, which were ¥3,366 million (US$27,167 thousand) and ¥8,145 million at March 31, 2001 and 2000, respectively, and the applicable interest rates were 0.79% and 0.41% at March 31, 2001 and 2000, respectively.

Long-term debt at March 31, 2001 and 2000 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2001	2000	**2001**
Unsecured convertible bonds due 2006, 0.95%	**¥34,833**	¥35,357	**$281,138**
Euro medium-term notes issued by the Company and certain consolidated subsidiaries, due 2001–2003, 2.09% in 2001 and 2.11% in 2000	**8,770**	20,949	**70,783**
Mortgage loans principally from banks	**440**	526	**3,551**
Unsecured loans principally from banks	**11,579**	12,324	**93,454**
	55,622	69,156	**448,926**
Less current portion	**12,480**	10,196	**100,726**
	¥43,142	¥58,960	**$348,200**

The weighted average interest rates applicable to the Euro medium-term notes shown above were interest rates at March 31, 2001 and 2000, respectively.

Besides the above long-term debt, deposits payable to customers were included in other long-term liabilities, which were ¥3,232 million (US$26,086 thousand) and the applicable interest rate was 0.49% at March 31, 2001.

The aggregate annual maturities of long-term debt as of March 31, 2001 were as follows:

Years ending March 31	Millions of yen	Thousands of U.S. dollars
2002	¥12,480	$100,726
2003	4,858	39,209
2004	3,056	24,665
2005	51	412
2006	34,833	281,138
2007 and thereafter	344	2,776

The mortgage loans are collateralized by land and buildings having a book value of ¥762 million (US$6,150 thousand) and by account receivables of ¥148 million (US$1,195 thousand) at March 31, 2001.

The conversion price of the convertible bonds is ¥1,333.00 as of March 31, 2001, subject to adjustment to reflect stock splits and certain other events.

Convertible bonds outstanding at March 31, 2001 were convertible into 26,131,283 shares of common stock of the Company on the basis of the above conversion price.

7. Income Taxes

The Company and its domestic subsidiaries are subject to Japanese national and local taxes based on income, which in the aggregate resulted in a normal statutory tax rate of approximately 42% for both 2001 and 2000. Foreign subsidiaries are subject to income taxes of the countries in which they operate.

Tax effects of significant temporary differences and tax loss carryforwards that resulted in deferred tax assets or liabilities at March 31, 2001 and 2000 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2001	2000	2001
Deferred tax assets:			
Depreciation	**¥ 18,219**	¥16,119	**$ 147,046**
Pension and severance costs	**5,750**	—	**46,408**
Accrued expenses	**6,075**	4,574	**49,032**
Enterprise taxes	**2,579**	2,429	**20,815**
Tax loss carryforwards	**7,225**	7,959	**58,313**
Other	**6,729**	5,207	**54,310**
Less valuation allowance	**(7,337)**	(9,009)	**(59,217)**
Deferred tax assets	**¥ 39,240**	¥27,279	**$ 316,707**
Deferred tax liabilities:			
Unrealized gain on available-for-sale securities	**¥ (4,516)**	¥ —	**$ (36,449)**
Undistributed foreign earnings	**(4,716)**	(3,031)	**(38,063)**
Deferred gains on sales of property	**(4,956)**	(4,869)	**(40,000)**
Other	**(3,907)**	(1,896)	**(31,533)**
Deferred tax liabilities	**¥(18,095)**	¥ (9,796)	**$(146,045)**
Net deferred tax assets	**¥ 21,145**	¥17,483	**$ 170,662**

8. Leases

a) Finance leases:

The Companies lease certain machinery, computer equipment and other assets.

Total rental expenses for the above leases for the years ended March 31, 2001 and 2000 were ¥1,290 million (US$10,412 thousand) and ¥540 million, respectively.

The pro forma information on lease property of which ownership is deemed not to be transferred to the lessee on an “as if capitalized” basis for the years ended March 31, 2001 and 2000 was as follows:

	Millions of yen		Thousands of U.S. dollars
	Machinery, equipment and other assets	Buildings, structures and other assets	Machinery, equipment and other assets
	2001	2000	2001
Acquisition cost	**¥8,057**	¥3,494	**$65,028**
Accumulated depreciation	**3,656**	1,900	**29,508**
Net leased property	**¥4,401**	¥1,594	**$35,520**

The pro forma depreciation expense computed by the straight-line method is ¥1,290 million (US$10,412 thousand) and ¥540 million for the years ended March 31, 2001 and 2000, respectively.

Obligations under finance leases as of March 31, 2001 were as follows:

	Millions of yen	Thousands of U.S. dollars
	2001	2001
Due within one year	**¥1,241**	**$10,016**
Due after one year	**3,160**	**25,504**
	¥4,401	**$35,520**

The pro forma information above does not exclude the imputed interest portion because the remaining financial lease obligations are not material compared with the book values of property, plant and equipment.

b) Operating leases:

The minimum rental commitments under noncancellable operating leases as of March 31, 2001 were as follows:

	Millions of yen	Thousands of U.S. dollars
	2001	2001
Due within one year	**¥1,805**	**$14,568**
Due after one year	**4,541**	**36,651**
	¥6,346	**$51,219**

9. Retirement Benefits

The Company and domestic consolidated subsidiaries have a defined benefit pension plan covering substantially all of their employees.

Certain foreign consolidated subsidiaries have local pension plans covering their employees.

Certain foreign consolidated subsidiaries also have local employees' retirement benefit plans and provide for the amount to state the liability for these employees' retirement benefits, primarily determined on an actuarial method.

Employees who retire from the Company and its certain consolidated subsidiaries are, under most circumstances, entitled to retirement and pension benefits determined by reference to basic rates of pay at the time of termination, length of service and conditions under which the termination occurs. If the termination is involuntary, caused by retirement at the mandatory retirement age or caused by death, the employee is entitled to greater payment than in the case of voluntary termination.

Effective April 1, 2000, the companies adopted the new accounting standard for employees' retirement benefits.

The liability for employees' retirement benefits at March 31, 2001 consisted of the following:

	Millions of yen	Thousands of U.S. dollars
	2001	**2001**
Projected benefit obligation	**¥ 225,818**	**$ 1,822,583**
Fair value of plan assets	**(147,929)**	**(1,193,939)**
Unrecognized prior service cost (credit)	**30,651**	**247,385**
Unrecognized actuarial loss	**(39,303)**	**(317,215)**
Unrecognized transitional obligation	**(56,295)**	**(454,358)**
Prepaid pension cost	**1,654**	**13,349**
Net liability for retirement benefits	**¥ 14,596**	**$ 117,805**

The components of net periodic benefit costs for the year ended March 31, 2001 were as follows:

	Millions of yen	Thousands of U.S. dollars
	2001	**2001**
Service cost	**¥ 8,725**	**$ 70,419**
Interest cost	**6,877**	**55,504**
Expected return on plan assets	**(6,749)**	**(54,471)**
Amortization of prior service cost (credit)	**(927)**	**(7,482)**
Recognized actuarial loss	**4,443**	**35,860**
Amortization of transitional obligation	**4,021**	**32,454**
Net periodic benefit costs	**¥16,390**	**$132,284**

Assumptions used for the year ended March 31, 2001 are set forth as follows:

Discount rate	Primarily 2.5%
Expected rate of return on plan assets	Primarily 4.0%
Amortization period of prior service cost	Primarily 15 years
Recognition period of actuarial gain/loss	Primarily 10 years
Amortization period of transitional obligation	15 years

Besides the above net periodic benefit costs, the costs for other retirement and pension plans such as a defined contribution plan and for supplemental retirement benefit for the year ended March 31, 2001 were ¥720 million (US$5,811 thousand) and ¥7,284 million (US$58,789 thousand), respectively. The amount charged to income for retirement benefit for directors and corporate auditors for the year ended March 31, 2001 was ¥109 million (US$880 thousand).

Total charges to income for the pension and retirement plans for the years ended March 31, 2001 and 2000 were ¥24,502 million (US$197,756 thousand) and ¥6,881 million, respectively.

10. Contingent Liabilities

The Companies' guarantees of borrowings, principally of affiliates and employees, were ¥4,476 million (US$36,126 thousand) as of March 31, 2001.

11. Shareholders' Equity

Under the Commercial Code of Japan (the "Code"), at least 50% of the issue price of new shares, with a minimum of the par value thereof, is required to be designated as stated capital. The portion which is to be designated as stated capital is determined by resolution of the Board of Directors. Proceeds in excess of the amounts designated as stated capital are credited to additional paid-in capital.

The Code provides that a portion of retained earnings equivalent to at least 10% of cash payments which are made as an appropriation of retained earnings shall be appropriated as a legal reserve until such reserve equals 25% of stated capital. The Code also provides that neither additional paid-in capital nor the legal reserve is available for cash dividends, but both may be used to reduce a deficit by resolution of shareholders or may be transferred to stated capital by resolution of the Board of Directors.

Dividends are paid semi-annually. Year-end dividends are approved by the shareholders at a meeting held subsequent to the fiscal year to which the dividends are applicable. In addition, semi-annual interim dividends may be paid upon resolution of the Board of Directors, subject to limitations imposed by the Code. Year-end dividends are reflected in the consolidated statements of shareholders' equity when authorized.

Under the Code, the amount available for dividends is based on retained earnings as recorded on the Company's books. At March 31, 2001, retained earnings recorded on the Company's books were ¥267,211 million (US$2,156,667 thousand).

On June 29, 1999, shareholders approved a stock repurchase program under which the Company may repurchase and retire up to 62 million shares of common stock subject to authorization by the Board of Directors. The Company repurchased 10 million shares of common stock during the fiscal year ended March 31, 2000. And as the Company also repurchased 10 million shares of common stock during the fiscal year ended March 31, 2001, at an aggregate cost of ¥28,642 million (US$231,170 thousand) according to the resolution of the Board of Directors on August 24, 2000, the total shares of repurchased common stock amounted to 20 million at March 31, 2001.

12. Segment Information

The Companies operate in three reportable segments: Consumer Products, Cosmetics *Sofina* and Chemical Products. Operations within the Consumer Products segment include the manufacture and sale of personal care products such as shampoos and conditioners, laundry and cleaning products, and hygiene products. The Cosmetics *Sofina* segment manufactures and sells cosmetics under the brand name, *Sofina*. The Chemical Products segment manufactures and sells fatty chemicals and specialty chemicals such as surface active agents.

Effective April 1, 2000, the Companies changed their policy of segmentation by business to include certain production operations (formerly in the Consumer Products segment or Cosmetics *Sofina* segment) in the Chemical Products segment, in order to disclose segment information more appropriately in accordance with the new segment structure focusing on capital costs and returns. The information for 2000 has been restated from the prior year's presentation in order to conform to the 2001 presentation.

Segment information by business of the Companies for the years ended March 31, 2001 and 2000 was as follows:

	Millions of yen				
	2001				
	Consumer Products	Cosmetics *Sofina*	Chemical Products	Corporate/ Eliminations	Consolidated
Sales to customers	**¥607,826**	**¥72,579**	**¥141,224**	**¥ —**	**¥821,629**
Intersegment sales	**—**	**—**	**26,669**	**(26,669)**	**—**
Total sales	**607,826**	**72,579**	**167,893**	**(26,669)**	**821,629**
Operating expenses	**521,720**	**69,748**	**150,180**	**(27,118)**	**714,530**
Operating income	**¥ 86,106**	**¥ 2,831**	**¥ 17,713**	**¥ 449**	**¥107,099**
Assets	**¥438,524**	**¥27,047**	**¥147,189**	**¥171,000**	**¥783,760**
Depreciation and amortization	**45,612**	**3,050**	**10,624**	**(430)**	**58,856**
Capital expenditures	**49,128**	**2,799**	**8,814**	**—**	**60,741**

	Millions of yen				
	2000				
	Consumer Products	Cosmetics *Sofina*	Chemical Products	Corporate/ Eliminations	Consolidated
Sales to customers	¥632,423	¥70,890	¥143,609	¥ —	¥846,922
Intersegment sales	—	—	28,792	(28,792)	—
Total sales	632,423	70,890	172,401	(28,792)	846,922
Operating expenses	550,318	68,700	157,666	(28,944)	747,740
Operating income	¥ 82,105	¥ 2,190	¥ 14,735	¥ 152	¥ 99,182
Assets	¥386,996	¥27,689	¥137,774	¥197,557	¥750,016
Depreciation and amortization	50,390	3,179	13,701	—	67,270
Capital expenditures	28,196	1,810	7,558	—	37,564

	Thousands of U.S. dollars				
	2001				
	Consumer Products	Cosmetics *Sofina*	Chemical Products	Corporate/ Eliminations	Consolidated
Sales to customers	**$4,905,779**	**$585,787**	**$1,139,822**	**$ —**	**$6,631,388**
Intersegment sales	**—**	**—**	**215,246**	**(215,246)**	**—**
Total sales	**4,905,779**	**585,787**	**1,355,068**	**(215,246)**	**6,631,388**
Operating expenses	**4,210,815**	**562,938**	**1,212,106**	**(218,870)**	**5,766,989**
Operating income	**$ 694,964**	**$ 22,849**	**$ 142,962**	**$ 3,624**	**$ 864,399**
Assets	**$3,539,339**	**$218,297**	**$1,187,966**	**$1,380,145**	**$6,325,747**
Depreciation and amortization	**368,135**	**24,617**	**85,747**	**(3,471)**	**475,028**
Capital expenditures	**396,513**	**22,591**	**71,138**	**—**	**490,242**

Geographic segment information of the Companies for the years ended March 31, 2001 and 2000 was as follows:

	Millions of yen				
	2001				
	Japan	Asia/ Oceania*	America/ Europe**	Corporate/ Eliminations	Consolidated
Sales to customers	**¥646,963**	**¥71,436**	**¥103,230**	**¥ —**	**¥821,629**
Intersegment sales	**8,507**	**12,701**	**2,057**	**(23,265)**	**—**
Total sales	**655,470**	**84,137**	**105,287**	**(23,265)**	**821,629**
Operating expenses	**561,149**	**77,333**	**99,376**	**(23,328)**	**714,530**
Operating income	**¥ 94,321**	**¥ 6,804**	**¥ 5,911**	**¥ 63**	**¥107,099**
Assets	**¥450,551**	**¥68,421**	**¥103,837**	**¥160,951**	**¥783,760**

	Millions of yen				
	2000				
	Japan	Asia/ Oceania*	America/ Europe**	Corporate/ Eliminations	Consolidated
Sales to customers	¥664,242	¥73,651	¥109,029	¥ —	¥846,922
Intersegment sales	9,214	12,525	2,014	(23,753)	—
Total sales	673,456	86,176	111,043	(23,753)	846,922
Operating expenses	581,750	82,265	107,580	(23,855)	747,740
Operating income	¥ 91,706	¥ 3,911	¥ 3,463	¥ 102	¥ 99,182
Assets	¥407,729	¥63,492	¥ 96,465	¥182,330	¥750,016

	Thousands of U.S. dollars				
	2001				
	Japan	Asia/ Oceania*	America/ Europe**	Corporate/ Eliminations	Consolidated
Sales to customers	**$5,221,654**	**$576,562**	**$833,172**	**$ —**	**$6,631,388**
Intersegment sales	**68,660**	**102,510**	**16,602**	**(187,772)**	**—**
Total sales	**5,290,314**	**679,072**	**849,774**	**(187,772)**	**6,631,388**
Operating expenses	**4,529,048**	**624,157**	**802,066**	**(188,282)**	**5,766,989**
Operating income	**$ 761,266**	**$ 54,915**	**$ 47,708**	**$ 510**	**$ 864,399**
Assets	**$3,636,408**	**$552,228**	**$838,071**	**$1,299,040**	**$6,325,747**

*Asia/Oceania: Asia and Australia
**America/Europe: North America, Europe and South Africa

Sales to foreign customers were as follows:

	Millions of yen		Thousands of U.S. dollars
	2001	2000	**2001**
Asia/Oceania	**¥ 74,474**	¥ 76,912	**$ 601,082**
America/Europe	**105,032**	118,103	**847,715**
Sales to foreign customers	**¥179,506**	¥195,015	**$1,448,797**

13. Selected Operating Expenses

Selling, general and administrative expenses principally consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2001	2000	2001
Sales commission	**¥ 8,074**	¥95,659	**$ 65,165**
Advertising	**65,758**	64,354	**530,734**
Promotion	**37,497**	27,209	**302,639**
Research and development	**37,049**	38,062	**299,023**

14. Other (Income) Expenses

Other, net consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2001	2000	2001
Loss on sales or disposals of property, plant and equipment, net	**¥2,682**	¥1,513	**$21,646**
Other, net	**(890)**	(470)	**(7,183)**
	¥1,792	¥1,043	**$14,463**

15. Derivatives

The Companies enter into foreign exchange forward contracts and foreign currency swaps to hedge foreign exchange risk associated with certain assets and liabilities denominated in foreign currencies. The Companies also enter into interest rate swap contracts to manage interest rate exposures on certain liabilities.

The Companies have purchased interest rate caps to limit the unfavorable impact from increases in interest rates on floating-rate long-term debt.

The interest rate caps effectively limit the Companies' interest exposures of floating-rate long-term borrowings to the maximum rate.

All derivative transactions are entered into to hedge interest and foreign currency exposures incorporated within the Companies' business. Accordingly, market risk in these derivatives is basically offset by opposite movements in the value of hedged assets or liabilities.

The Companies do not hold or issue derivatives for trading or speculative purposes. Because the counterparties to these derivatives are limited to major international financial institutions, the Companies do not anticipate any losses arising from credit risk.

Derivative transactions entered into by the Companies have been made in accordance with internal policies which regulate the authorization and credit limit amounts.

The Companies had the following derivatives contracts outstanding at March 31, 2001 and 2000:

	Millions of yen					
	2001			2000		
	Contract amount	Fair value	Unrealized gain/(loss)	Contract amount	Fair value	Unrealized gain/(loss)
Foreign exchange forward contracts:						
Buying U.S. Dollar	**¥ 957**	**¥ 950**	**¥ (7)**	¥ 293	¥286	¥ (7)
Buying Japanese Yen	**51**	**51**	**0**	168	166	(2)
Buying British Pound	**72**	**72**	**(0)**	—	—	—
Buying Swiss Franc	**106**	**105**	**(1)**	69	69	0
Selling U.S. Dollar	**474**	**444**	**30**	—	—	—
Selling Swiss Franc	**103**	**104**	**(1)**	262	257	5
Selling Argentine Peso	**—**	**—**	**—**	179	188	(9)
Selling other currencies	**256**	**254**	**2**	—	—	—
Foreign currency swaps:						
Receiving Japanese Yen, paying U.S. Dollar	**3,695**	**(285)**	**(285)**	—	—	—
Receiving Singapore Dollar, paying U.S. Dollar	**148**	**0**	**0**	—	—	—
Receiving Japanese Yen, paying Euro	**1,399**	**(120)**	**(120)**	—	—	—
Receiving Japanese Yen, paying British Pound	**322**	**(38)**	**(38)**	—	—	—
Receiving Japanese Yen, paying German Mark	**2,762**	**62**	**62**	—	—	—
Receiving U.S Dollar, paying German Mark	**689**	**81**	**81**	—	—	—
Receiving Japanese Yen, paying Australian Dollar	**235**	**20**	**20**	—	—	—
Interest rate swaps:						
Fixed-rate receipt, floating-rate payment	**545**	**(1)**	**(1)**	18,526	952	952
Fixed-rate payment, floating-rate receipt	**545**	**4**	**4**	526	(1)	(1)
Interest rate caps:						
Selling	**545**	**(0)**	**(0)**	526	0	0
Buying	**2,452**	**6**	**6**	2,367	29	29

	Thousands of U.S. dollars		
	2001		
	Contract amount	Fair value	Unrealized gain/(loss)
Foreign exchange forward contracts:			
Buying U.S. Dollar	**$ 7,724**	**$ 7,667**	**$ (56)**
Buying Japanese Yen	**412**	**412**	**0**
Buying British Pound	**581**	**581**	**(0)**
Buying Swiss Franc	**856**	**847**	**(8)**
Selling U.S. Dollar	**3,826**	**3,584**	**242**
Selling Swiss Franc	**831**	**839**	**(8)**
Selling other currencies	**2,066**	**2,050**	**16**
Foreign currency swaps:			
Receiving Japanese Yen, paying U.S. Dollar	**29,822**	**(2,300)**	**(2,300)**
Receiving Singapore Dollar, paying U.S. Dollar	**1,195**	**0**	**0**
Receiving Japanese Yen, paying Euro	**11,291**	**(969)**	**(969)**
Receiving Japanese Yen, paying British Pound	**2,599**	**(307)**	**(307)**
Receiving Japanese Yen, paying German Mark	**22,292**	**500**	**500**
Receiving U.S Dollar, paying German Mark	**5,561**	**654**	**654**
Receiving Japanese Yen, paying Australian Dollar	**1,897**	**161**	**161**
Interest rate swaps:			
Fixed-rate receipt, floating-rate payment	**4,399**	**(8)**	**(8)**
Fixed-rate payment, floating-rate receipt	**4,399**	**32**	**32**
Interest rate caps:			
Selling	**4,399**	**(0)**	**(0)**
Buying	**19,790**	**48**	**48**

16. Subsequent Event

At the ordinary general meeting of shareholders held on June 28, 2001, the Company's shareholders approved the appropriation of retained earnings.

Appropriation of retained earnings

	Millions of yen	Thousands of U.S. dollars
Ordinary year-end cash dividends, ¥12.00 (US$0.097) per share	**¥7,330**	**$59,161**
Directors' and corporate auditors' bonuses	**143**	**1,154**

Independent Auditors' Report

Tohmatsu & Co.
MS Shibaura Building
13-23, Shibaura 4-chome,
Minato-ku, Tokyo 108-8530, Japan

Tel: +81-3-3457-7321
Fax: +81-3-3769-8508
www.tohmatsu.co.jp

Deloitte Touche Tohmatsu

To the Board of Directors of
Kao Corporation

We have examined the consolidated balance sheets of Kao Corporation and consolidated subsidiaries as of March 31, 2001 and 2000, and the related consolidated statements of income, shareholders' equity, and cash flows for the years then ended, all expressed in Japanese yen. Our examinations were made in accordance with auditing standards, procedures and practices generally accepted and applied in Japan and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the financial position of Kao Corporation and consolidated subsidiaries as of March 31, 2001 and 2000, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles and practices generally accepted in Japan consistently applied during the period except for the change, with which we concur, in the segment information by business as discussed in Note 12.

As discussed in Note 1, effective April 1, 2000, the consolidated financial statements have been prepared in accordance with new accounting standards for employees' retirement benefits and financial instruments and the revised accounting standard for foreign currency transactions.

Our examinations also comprehended the translation of Japanese yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made in conformity with the basis stated in Note 2. Such U.S. dollar amounts are presented solely for the convenience of readers outside Japan.

Deloitte Touche Tohmatsu

June 28, 2001

Principal Subsidiaries and Affiliates

Consumer Products, Cosmetics *Sofina* and Chemical Products Businesses

Area	Country	Company	Consumer Products/Cosmetics *Sofina*	Chemical Products
Asia	Japan	Kao Cosmetics Sales Co., Ltd.	●	
	Japan	Kao Hanbai Company, Ltd.	●	
	Japan	Nivea-Kao Company Limited	●	
	Japan	Kao-Quaker Company, Limited		●
	Japan	Novartis Kao Co., Ltd.	●	
	China	Kao Corporation Shanghai	●	
	China	Kao Chemical Corporation Shanghai		●
	China	Zhongshan Kao Chemicals Limited		●
	Hong Kong	Kao (Hong Kong) Limited	●	
	Hong Kong	Kao Chemicals (Hong Kong) Limited		●
	Indonesia	P.T. Kao Indonesia	●	
	Indonesia	P.T. Kao Indonesia Chemicals		●
	Malaysia	Kao (Malaysia) Sdn. Bhd.	●	
	Malaysia	Kao Trading (M) Sdn. Bhd.	●	
	Malaysia	Fatty Chemical (Malaysia) Sdn. Bhd.		●
	Malaysia	Kao Soap (Malaysia) Sdn. Bhd.	●	
	Malaysia	Kao Oleochemical (Malaysia) Sdn. Bhd.		●
	Malaysia	Kao Plasticizer (Malaysia) Sdn. Bhd.		●
	Philippines	Pilipinas Kao, Incorporated		●
	Singapore	Kao (Southeast Asia) Pte. Ltd.		●
	Singapore	Kao (Singapore) Private Limited	●	
	Taiwan	Kao (Taiwan) Corporation	●	●
	Thailand	Kao Industrial (Thailand) Company Limited	●	●
	Thailand	Kao Commercial (Thailand) Company Limited	●	
	Thailand	Kao Consumer Products (Southeast Asia) Co., Ltd.	●	
	Vietnam	Kao Vietnam Co., Ltd.	●	
Oceania	Australia	Kao (Australia) Marketing Pty. Ltd.	●	
America	Canada	Jergens Canada Inc.	●	
	Mexico	Quimi-Kao, S.A. de C.V.		●
	United States	The Andrew Jergens Company	●	
	United States	Kao Chemicals Americas Corporation		●
	United States	High Point Textile Auxiliaries LLC		●
	United States	Kao Specialties Americas LLC		●
Europe	Austria	Guhl Ikebana Kosmetika GmbH	●	
	France	Kao Corporation (France) SARL		●
	Germany	Kao Corporation GmbH	●	
	Germany	Kao Chemicals GmbH		●
	Germany	Guhl Ikebana GmbH	●	
	Netherlands	Guhl Ikebana Cosmetics B.V.	●	
	Spain	Kao Corporation S.A.		●
	Spain	Kao Chemicals Europe, S.L.		●
	Switzerland	Guhl Ikebana AG	●	

● Consumer Products/Cosmetics *Sofina*
● Chemical Products

Goldwell Products for Professional Hair Salons

Country	Company
Austria	Goldwell Handelsgesellschaft mbH
Belgium	N.V. Goldwell Belgium S.A.
Czech Republic	Goldwell Cosmetics (CZ) s.r.o.
Denmark	Goldwell A/S
Finland	Goldwell Oy
Germany	Goldwell GmbH
Germany	Goldwell Vertriebs GmbH
Italy	Goldwell Italia S.p.A.
Netherlands	Goldwell Nederland B.V.
Switzerland	Goldwell AG
United Kingdom	Goldwell (Hair Cosmetics) Ltd.
Canada	Goldwell Cosmetics (Canada) Ltd.
United States	Goldwell Cosmetics (USA) Inc.
South Africa	Goldwell South Africa (Pty.) Ltd.
Hong Kong	Goldwell Cosmetics (Hong Kong) Ltd.
Singapore	Goldwell Cosmetics Singapore PTE. Ltd.
Taiwan	Goldwell Taiwan Cosmetics Ltd.
Australia	Goldwell Cosmetics (Australia) Pty. Ltd.

Investor Information

Kao Corporation

Head Office
14-10, Nihonbashi Kayabacho 1-chome
Chuo-ku, Tokyo 103-8210, Japan
Telephone: 81-3-3660-7111
Facsimile: 81-3-3660-7103

Date of Establishment
June 19, 1887

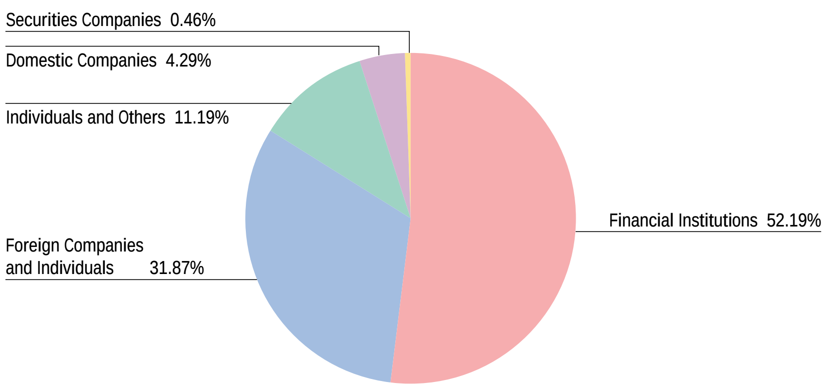
Common Stock (As of March 31, 2001)
Authorized: 980,000,000 shares
Outstanding: 610,826,451 shares
Number of Shareholders: 39,300

Stock Listings
Tokyo Stock Exchange, Osaka Securities Exchange

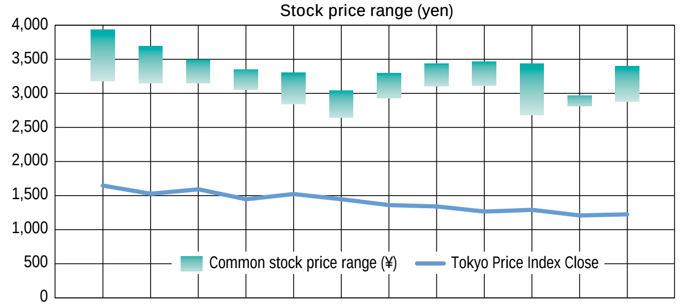
Ticker Symbol Number
4452

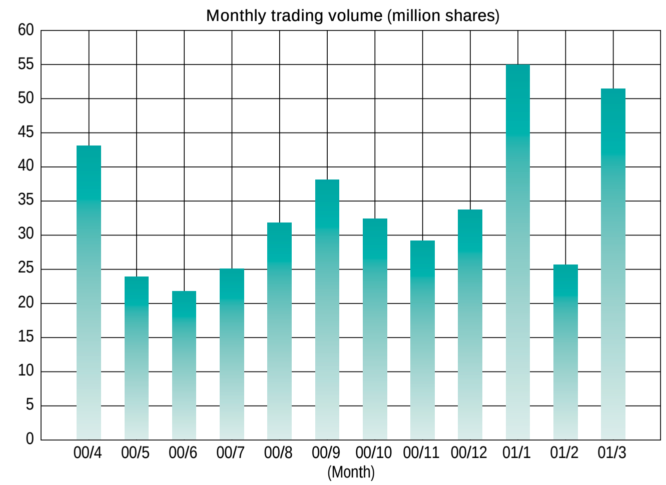
Transfer Agent
The Chuo Mitsui Trust and Banking Company, Limited
8-4, Izumi 2-chome,
Suginami-ku, Tokyo 168-0063, Japan

Composition of Shareholders (As of March 31, 2001)



Stock Price Range & Trading Volume
(Tokyo Stock Exchange)





Further Information
Investor Relations Department
Telephone: 81-3-3660-7101
Facsimile: 81-3-3660-7103
http://www.kao.co.jp/e/



Kao Corporation

14-10, Nihonbashi Kayabacho 1-chome
Chuo-ku, Tokyo 103-8210, Japan
Telephone: 81-3-3660-7111
Facsimile: 81-3-3660-7103
http://www.kao.co.jp/

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