# ANNUAL REPORT 2010

For the Year Ended December 31, 2010

TOKAI CARBON CO., LTD.

ANNUAL REPORT 2010

## Contents







# Profile

The Tokai Carbon Group commenced operations as a pioneer in the carbon industry in Japan in 1918, and since then has actively contributed to the development of society through carbon-related products and services based on diverse manufacturing fields and technology.

The Company engages in the production and sale of Carbon black for use in automotive tires and other rubber products, Graphite electrodes for use in electric arc furnaces for steel production, Fine carbon for use in a wide range of new energy related fields, such as solar batteries and semi-conductors, Friction materials for use in brakes and clutches on engineering vehicles, motorcycles and automobiles, etc., and Industrial furnaces & related products, for use in heat-treating ceramics, electrical parts, metal, and glass, etc.

Growing together with these five core divisions, Tokai Carbon continues to spread its wings from Japan to the rest of the world.

# Corporate Philosophy

Our corporate philosophy is "Ties of reliability". We believe in the importance of trust between Tokai Carbon and our stakeholders (as represented by customers, shareholders, employees, and society). This idea of mutual reliability, which is based on common values shared with our stakeholders, is the foundation of our continued business and existence.

This concept allows us to provide added value to our stakeholders, thus enabling them to achieve their individual goals. Through this cycle of trust, we will strive to further enhance our ties of reliability.

# History

| | |
|---|---|
| **1918** | Established as Tokai Electrode Mfg. Co. Ltd. (TDK) with a plant in Nagoya and the head office in Tokyo. |
| **1935** | Tanoura Plant opened to meet increasing demand for Graphite Electrodes. |
| **1936** | Kyushu Wakamatsu Plant opened for Pitch Coke production. |
| **1938** | Chigasaki Plant opened primarily for Carbon Brush production. |
| **1941** | Carbon Black production started on a commercial basis at the Kyushu Wakamatsu Plant. |
| **1960** | A 10-year technical agreement was made with Cabot Corporation for Carbon Black production. |
| **1962** | Chita Plant, the largest Carbon Black plant in Japan, opened. |
| **1971** | Hohfu Plant opened for Graphite Electrode production. |
| **1973** | Hohfu Laboratory opened. |
| **1975** | Changed the Company name to Tokai Carbon Co., Ltd. Chita Laboratory opened for Carbon Black production. |
| **1978** | Ishinomaki Plant opened for Carbon Black production. |
| **1982** | Production of SiC whisker, TOKAWHISKER, implemented on a commercial base. |
| **1987** | Tanoura Laboratory and the Fuji Research Laboratory opened. |
| **1987** | Tokai Carbon America Inc. established. Shonan Techno-Center opened for the development of new product lines. |
| **1990** | Tokai Carbon made a capital investment and entered into a technical agreement with Thai Carbon Product Company in Thailand for Carbon Black production.<br>European Representative Office established in Dusseldorf. |
| **1990** | A technical agreement was made with Jung Woo Coal Chemical Company in South Korea for Carbon Black production. |
| **1992** | Tokai Carbon merged with Toyo Carbon Co., Ltd., another leading company founded in 1918 that manufactures Graphite Electrodes, Friction Materials and Specialty Carbon products, etc. |
| **1994** | Tokai Carbon Europe S.R.L. established as a sales company of Specialty Graphite products. |
| **1996** | Tokai Carbon U.S.A., Inc. is established as its wholly owned subsidiary manufacturing company of SiC Coated Materials.<br>Tokai Carbon Korea Co., Ltd., established as a joint venture company for Specialty Graphite products. |
| **1997** | Tokai Carbon America Inc. and the European Representative Office closed. |
| **1999** | Tokai Carbon Europe Ltd. established as a holding company of Graphite Technologies PLC(defunct)., Svensk Specialgrafit AB and Tokai Carbon Italy S.R.L. (Graphite Technologies PLC. and Svensk Specialgrafit AB were acquired during the year). |
| **2000** | Tokai Carbon acquired the majority of the shares of Thai Carbon Product Co., Ltd. Subsequently, the name was changed to Thai Tokai Carbon Product Co., Ltd. |
| **2001** | Shonan Industrial Complex opened, whereas Shonan Techno-Center closed. |
| **2002** | SGL Tokai Carbon Ltd. Shanghai established in China as a joint venture company with SGL Carbon AG for production and sales of Graphite Electrodes. |
| **2003** | Tokai Material Co., Ltd., established by transfer of the brake business from Mitsubishi Materials Kenzai Corporation. |
| **2004** | Tokai Carbon (Tianjin) Co., Ltd., established in China for production and sales of Carbon Black. |
| **2005** | Tokai Carbon acquired ERFTCARBON GmbH (current TOKAI ERFTCARBON GmbH) in Germany for production and sales of Graphite Electrodes. |
| **2006** | Dalian Tokai-Jinqi-Fuji Carbon Co., Ltd. established for machining and sales of graphite products.<br>Tokai Carbon made Tokai Konetsu Co., Ltd., a wholly owned subsidiary through a share exchange.<br>Tokai Carbon acquired Carbon Industrie-Produkte GmbH group (current Tokai Carbon Deutschland GmbH) in Germany. |
| **2007** | Tokai Carbon opened and separated the Noshiro Plant from Tokai Fine Carbon Machining Co., Ltd. and established the 100% consolidated subsidiary of Tokai Noshiro Seiko Co., Ltd.<br>Tokai Carbon Europe GmbH established in Germany as the chief operating company for fine carbon businesses in Europe. |
| **2008** | Tokai Carbon (Shanghai) Co., Ltd. established in China (Shanghai) for sales of fine carbon products. |
| **2010** | Singapore Representative Office reopened. |

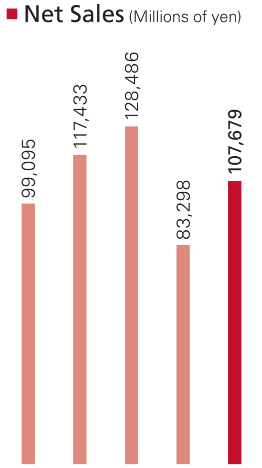
# Consolidated Financial Highlights

TOKAI CARBON Co., Ltd. and Consolidated Subsidiaries
Years ended December 31, 2010, 2009, 2008, 2007 and 2006

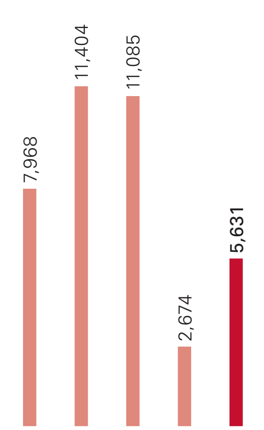
| | Millions of Yen | | | | | Thousands of U.S. Dollars |
|---|---|---|---|---|---|---|
| | 2006 | 2007 | 2008 | 2009 | **2010** | **2010** |
| **For the Year:** | | | | | | |
| Net sales | ¥ 99,095 | ¥117,433 | ¥128,486 | ¥ 83,298 | **¥107,679** | **$1,321,377** |
| *Carbon and Graphite Products* | 90,812 | 108,236 | 119,269 | 78,425 | **101,631** | **1,247,147** |
| *Industrial Furnaces and Related Products* | 7,570 | 8,543 | 8,709 | 4,406 | **5,628** | **69,064** |
| *Others* | 713 | 654 | 508 | 467 | **420** | **5,154** |
| Gross profit | 29,327 | 37,340 | 38,580 | 18,323 | **24,348** | **298,785** |
| Operating income | 14,800 | 20,746 | 21,619 | 5,299 | **10,575** | **129,770** |
| Income before income taxes and minority interests | 13,716 | 21,044 | 18,789 | 4,938 | **9,212** | **113,044** |
| Net income | 7,968 | 11,404 | 11,085 | 2,674 | **5,631** | **69,101** |
| Depreciation and amortization | 5,112 | 6,283 | 8,046 | 9,525 | **8,854** | **108,651** |
| Research and development costs | 1,491 | 1,655 | 2,026 | 2,073 | **2,012** | **24,690** |
| Capital expenditures | 6,276 | 13,034 | 17,544 | 8,066 | **6,710** | **82,342** |
| **At Year-End:** | | | | | | |
| Total assets | ¥164,062 | ¥174,279 | ¥172,172 | ¥154,922 | **¥155,304** | **$1,905,804** |
| Total net assets | 99,398 | 111,152 | 104,434 | 106,042 | **105,606** | **1,295,938** |
| | | | | | | U.S. Dollars |
| **Per Share Data: (Yen)** | | | | | | |
| Net income | ¥ 39.92 | ¥ 53.42 | ¥ 50.43 | ¥ 12.28 | **¥ 26.05** | **$ 0.32** |
| Total net assets | 475.25 | 499.42 | 471.61 | 478.26 | **484.53** | **5.95** |
| Cash dividends applicable to the year | 7.00 | 9.00 | 10.00 | 8.00 | **8.00** | **0.09** |
| **Financial Ratios: (%)** | | | | | | |
| Return on assets | 9.2% | 12.4% | 10.8% | 3.1% | **6.4%** | **6.4%** |
| Return on equity | 8.7 | 11.0 | 10.4 | 2.6 | **5.4** | **5.4** |
| Equity ratio | 59.7 | 62.8 | 59.7 | 67.2 | **66.6** | **66.6** |

Note: U.S. dollar amounts in this annual report are translated from Japanese yen, for convenience only, at the rate of ¥81.49 to US$1, the approximate rate of exchange at December 31, 2010.

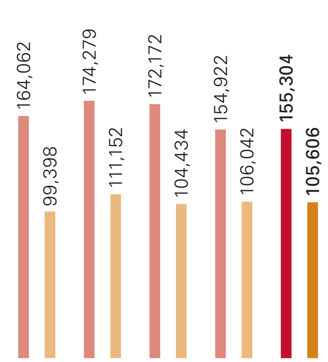
■ Net Sales (Millions of yen)



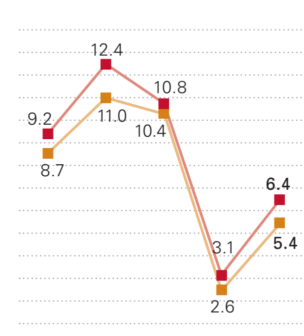

■ Net Income (Millions of yen)




■ Total Assets
■ Total Net Assets
(Millions of yen)




■ Return on Assets
■ Return on Equity
(%)






# President's Message

## Business Results for Year Ended December 31, 2010

The global economy during 2010 was on the road to recovery, led by steady economic growth in emerging countries. Since midyear, however, the recovery has slowed, owing primarily to expanding fiscal and financial crises in European countries, a downturn in the U.S. economy, and growing concerns over inflation in emerging countries. The Japanese economy also picked up in the first half of the year, reflecting the recovery in the global economy and the effects of the government's stimulus measures. However, the business atmosphere has turned for the worse since the summer. The diminishing effects of the stimulus measures after implementation, a slowdown in exports due to the deceleration in the global economy, and the ongoing appreciation of the yen adversely impacted the Japanese economy during the second half of the year.

Under these conditions, although demand has recovered in the industries in which the Tokai Carbon Group's customers operate (e.g., rubber products, steel, IT hardware, and industrial machinery), some businesses have been slow to recover. Yen appreciation also led to a decrease in net sales and income.

As a result, consolidated net sales for the fiscal year under review increased by 29.3% year on year, to ¥107,679 million. Operating income increased by 99.6% year on year, to ¥10,575 million, as a result of continued efforts to cut expenses across the board since the previous year. Ordinary income rose 97.4% year on year, to ¥9,854 million. Net income increased to ¥5,630 million, up 110.5% year on year.

In the aim of increasing shareholder returns, enhancing corporate value, and strengthening theGroup's operational foundation, the Company has adopted a policy of setting dividends based on its earnings status viewed from a medium-term perspective, while also maintaining sufficient retained earnings. The Company retains earnings to fund strategic investments in new businesses, including M&A, invest in improving existing operations' efficiency, solidify its financial condition, and maintain stable dividends. For the fiscal year ended December 31, 2010, the Company plans to pay year-end dividend of ¥4 per share, the same as that of the previous period. The year-end dividend will bring total 2010 dividends to ¥8 per share.

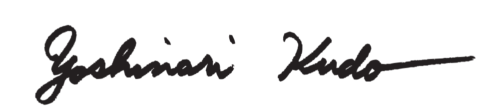
## Issues to Be Addressed

The Japanese economy is expected to head toward a moderate recovery against the backdrop of steady growth in emerging economies and a recovery in the U.S. economy. However, prospects for the future remain uncertain as the pace of Japan's recovery largely depends on the global economy, coupled with the trend in foreign currency exchange markets.

Amid such an environment, the Group will step forward to remain as the "Global Leader of Carbon Materials." To this end, the Group is determined to make all-out efforts in achieving the "T-2012" three-year management plan to enhance its corporate value and take up the challenge once again of achieving sustainable growth, based on its four guiding principles (enhancement of value-creation capabilities, fair management, ecological harmony, and internationalism) and its corporate philosophy,"Ties of Reliability."

In addition, the Group will make every effort to pay greater attention to the basics of a manufacturing company, namely security, quality control, and environmental protection, and will continue to reinforce corporate governance and corporate social responsibility (CSR). Furthermore, the Group will continue strengthening its operational foundation through implementing, assessing, and improving its internal controls over financial reporting in compliance with the Financial Instruments and Exchange Act (J-SOX).

We hope for your continued support and encouragement.



**Yoshinari Kudo**, President and CEO

# Review of Operations

## Carbon Products

### Carbon Black

*Carbon black is mainly used as a reinforcing agent of industrial rubber products, typically auto tires. Among other important uses are electro conductive filler and coloring agent for printing inks, paints and plastics.*

In Japan, the tire and automotive parts industries, in which our customers operate, enjoyed a recovery until the third quarter. In particular, demand in the tire industry remained favorable, due chiefly to unabated exports until the fourth quarter, even after the government's eco-car subsidy program was terminated. In addition, as there were strong demand for tires in Thailand and China and firm demand from automotive manufacturing in these countries, sales volumes of carbon black continued to recover.

As a result, net sales of carbon black increased by 35.6% year on year, to ¥39,975 million.

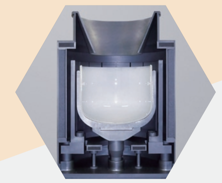
### Graphite Electrodes

*Graphite electrodes function as conductors of electricity that are consumed in an electric furnace in the steelmaking process.*

Global blast furnace production of raw steel was on a gradual recovery path to the 2008 level that preceded the financial crisis, after bottoming out in the first quarter of the previous year. Operations in the electric arc furnace industry, in which our customers operate, were also on the road to recovery worldwide, and demand for electrodes picked up. However, the recovery slowed down somewhat in the second half of the year.

As a result, although export sales declined due to the impact of yen appreciation, net sales of graphite electrodes increased by 19.3% year on year, to ¥38,425 million.

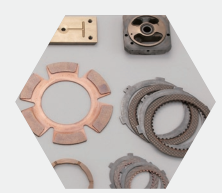
### Fine Carbon



*Fine carbon products are a wide variety of specialty graphites that are characterized by excellent electric conductance, high heat resistance, mechanical strength and lubricant ability, and are applied as key parts in the manufacturing processes of electric appliances, semiconductors, solar cells and LED, among other products.*

Demand for fine carbon did not see a major recovery during the first quarter in the industries in which our customers operate. Since the second quarter, however, demand in the solar cell and semiconductor industries, which are growing markets, has surged, especially in China, Korea, and other Asian countries. The Company has also implemented sales price revisions since the third quarter. As a result, despite the negative impact on export sales from yen appreciation, net sales of fine carbon increased by 35.1% year on year, to ¥15,537 million.

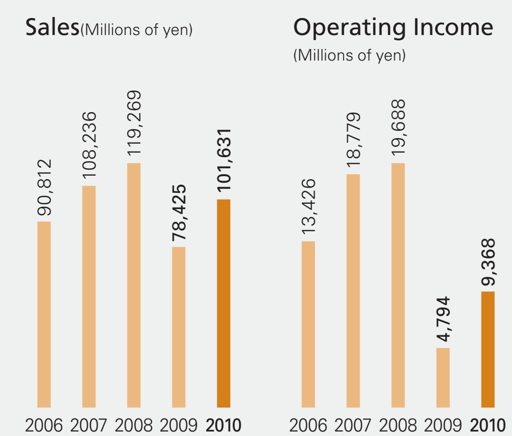
### Friction Materials



*Friction materials are widely used for clutches and brakes of automobiles, motorcycles, construction, agricultural, transportation and other industrial machinery.*

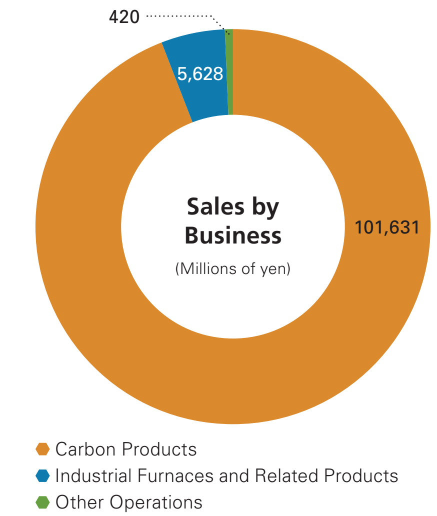
Sales were on a rapid recovery path due to unabated firm demand in construction machinery markets, our major client segment, supported by substantial demand growth in China and other emerging countries. Although demand for friction materials for two-wheeled vehicles showed signs of moderate recovery, demand for four-wheeled vehicles picked up steadily. In general, demand showed encouraging signs of recovery.

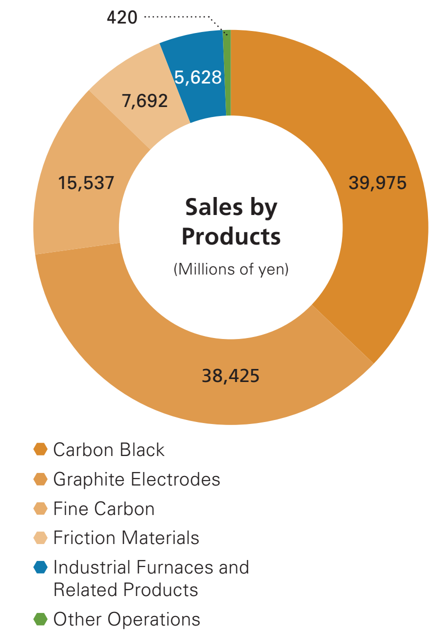
As a result, net sales of friction materials rose 46.7% year on year, to ¥7,692 million.

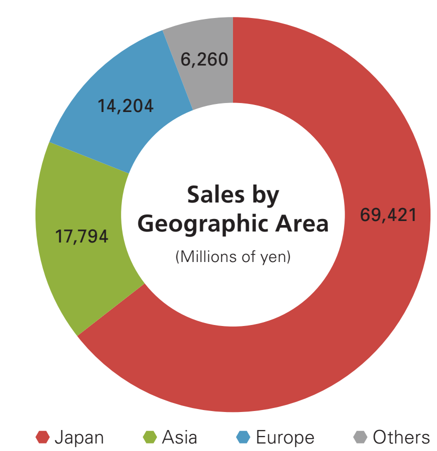



Overall, net sales in the Carbon Products segment increased by 29.6% year on year, to ¥101,631 million. Operating income increased by 95.4% year on year, to ¥9,368 million.

## Fiscal 2010 Sales by Segments



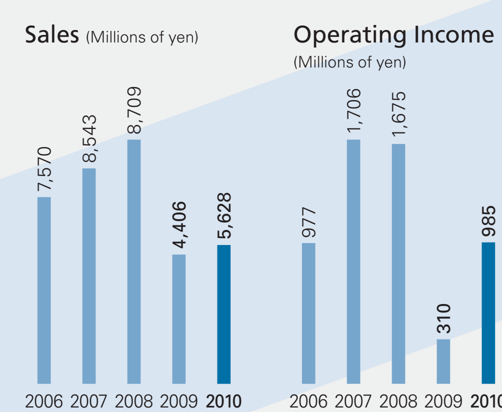




## Industrial Furnaces and Related Products

*Industrial furnaces and heating elements are manufactured by Tokai Konetsu Kogyo Co., Ltd., which is a wholly subsidiary, for the purposes of heating, sintering, dissolving and heat-treating such objects as ceramics, electronic parts, metals, glass and powdered materials.*

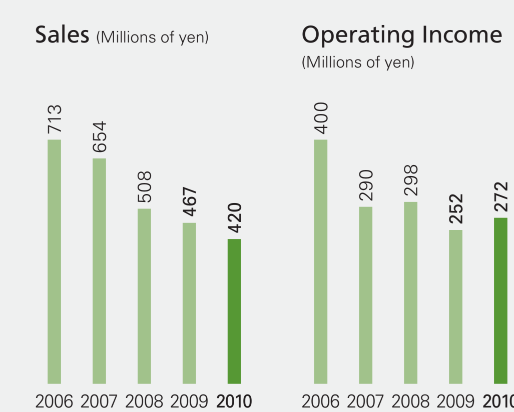
For the most part, substantial capital investment was not seen in our major clients in IT-related industries, although capital investment showed signs of a moderate recovery. Accordingly, sales of industrial furnaces, our major products, remained at a low level, similar to that of the previous year. However, sales of heating elements and related products rose over the previous year, owing to a recovery in demand in the glass and electronic component industries.

As a result, net sales in the Industrial Furnaces and Related Products segment increased by 27.7% year on year, to ¥5,628 million. Also, operating income soared by 217.0% year on year, to ¥985 million, as a result of our efforts in improving profitability centering on productivity.




## Other Operations

Net revenues from Other Operations, including real estate rental revenues, declined 10.0% year on year, to ¥420 million. However, operating income increased by 8.0%, to ¥272 million.



# Research and Development

The Group's R&D activities are mainly carried out at the Fuji Research Laboratory, Chita Laboratory, and Carbon and Ceramics Laboratories (Hofu Laboratory and Tanoura Laboratory), all working in coordination with Tokai Carbon's Development and Technology divisions. We promote vigorous R&D activities including research into new products based on fundamental research, development of technology for industrial use, enhancement of existing products, and quality improvements. The cost of research and development for the consolidated fiscal year ended December 31, 2010, amounted to ¥2,012 million.

Fuji Research Laboratory (Shizuoka, Japan)

## Carbon Products Segment

Tokai Carbon considers fine carbon and fine ceramics to be growth fields. Our products offer outstanding material characteristics that make them suitable for a wide range of applications. Recent years have seen remarkable growth in high-tech needs relating to energy, semi-conductors, electronics, high-temperature thermal insulation and environmental fields. We are responding to these changes by developing carbon products to satisfy this demand.

We are investing in R&D of products that leverage our accumulated technologies, including water-soluble carbon black for use as pigment in ink-jet printing ink, fuel cell separators, and negative-electrode carbon materials for use in lithium-ion batteries. Research and development costs for this segment came to ¥1,901 million.

## Industrial Furnaces and Related Products Segment

Tokai Carbon conducts R&D in this segment through its subsidiary Tokai Konetsu Kogyo Co., Ltd. Development projects here include a rotary gas furnace for processing powders, and a new generation low-energy industrial furnace that aims to reduce $CO_2$ emissions. We are building our strength in other fields too. These efforts include film formers for use in manufacturing thin-film photovoltaic cells, a prototype apparatus for heat treating lithium-ion battery electrode materials, and manufacture of heat-treatment furnaces for ceramic electrode components.

Moreover, Tokai Carbon is leveraging Tokai Konetsu Kogyo's proprietary technologies as a base for developing new products and applications. The focus technologies include silicon carbide heating elements, silicon carbide structural materials, ceramic resistors, and silicon nitride materials.

Research and development costs for this segment came to ¥111 million.



# Forecast of Consolidated Earnings for Fiscal 2011 (Jan.1, 2011 – Dec.31, 2011)

| | Net sales | | Operating income | | Ordinary income | | Net income | | Net income per share |
|---|---|---|---|---|---|---|---|---|---|
| | Million yen | % | Million yen | % | Million yen | % | Million yen | % | yen |
| First six months | 53,500 | (1.6) | 4,600 | (12.7) | 4,500 | (8.2) | 2,400 | (14.8) | 11.24 |
| Full year | 109,000 | 1.2 | 10,000 | (5.4) | 10,100 | 2.5 | 5,700 | 1.2 | 26.69 |

Notes: 1. Percentages represent Y-on-Y changes for the full year and increase / decrease from the same period of the previous year for the first six months.
2. "FY2011 (expected)" represents estimates announced in February 2011.
3. The impact from the Great East Japan Earthquake occurred on March 11, 2011 on business performance is currently unclear, information will be disclosed promptly once details emerge.

# Corporate Governance

## Approach to Corporate Governance

Tokai Carbon recognizes that the aim of managing a corporation should be to enhance the soundness and transparency of business management and ensure continual advancement of corporate value. With a top priority on strengthening corporate governance, we therefore strive to improve our management organization and the function of supervisory management.

The Company currently employs the corporate auditor system to ensure effective corporate governance. The Corporate Auditors include external auditors who maintain a certain level of independence from management. The Corporate Auditors attend all important meetings including Board of Directors' Meetings and Managing Executives Meetings. By voicing objective opinions at these meetings, the Corporate Auditors help management to ensure effective direction and oversight of the Company. Management considers that this system is amply sufficient to ensure the independence of auditors and effective corporate governance given the scale and organizational structure of the Company.

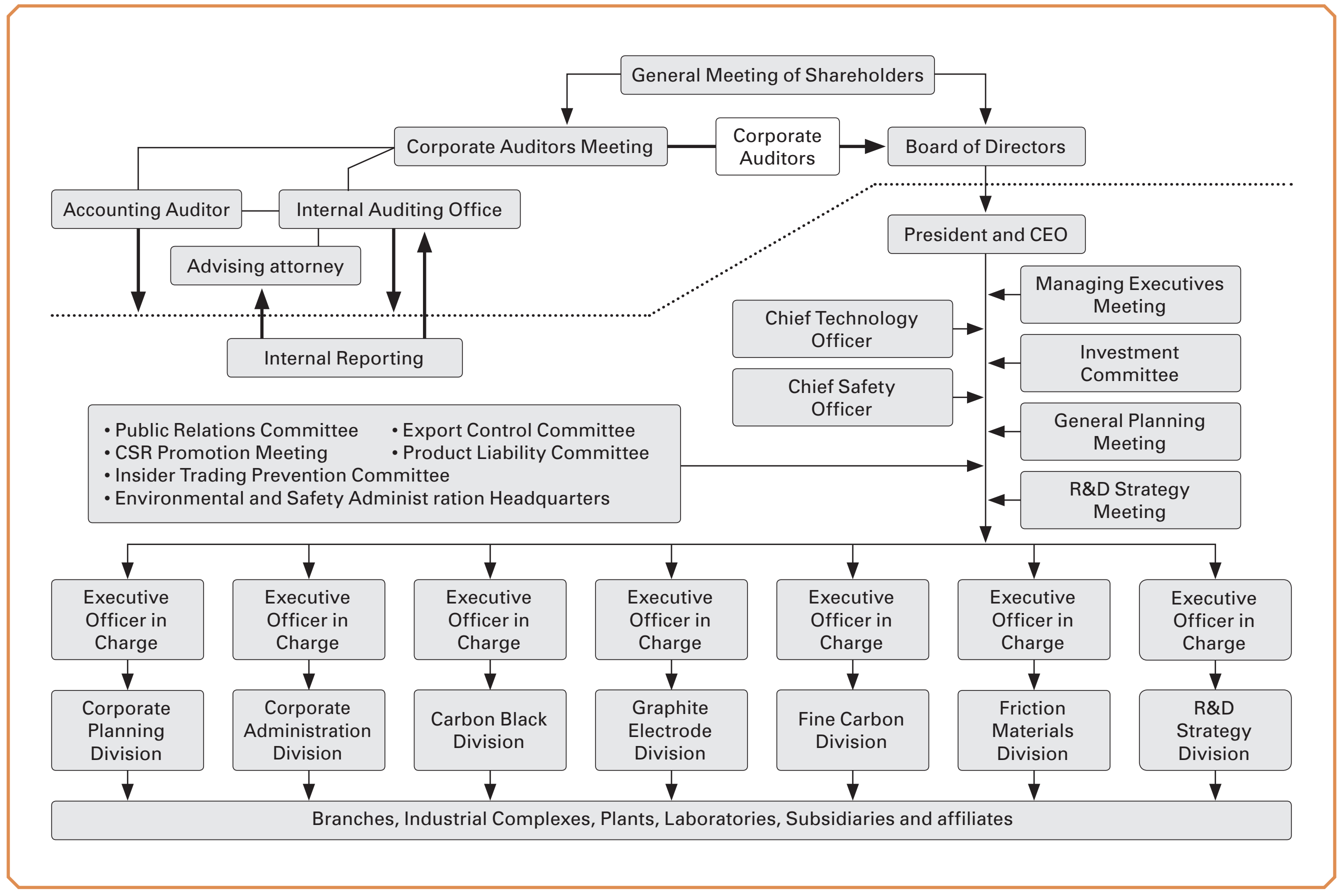
## Corporate Governance Structure

Tokai Carbon's basic management policies and strategies are determined by its Board of Directors, which consists nine directors, including one external director. Their meetings are usually held once a month and otherwise as necessary to make decisions on matters required by corporate laws and important business issues or to share reports on the status of business operations.

Since the Company introduced the Executive Officer System in March 1999, the Board of Directors selects and appoints Executive Officers who take charge of businessoperations in different departments of the Company to accelerate operational decision making and clarify responsibilities. The President and Executive Officers in charge of different business operations have a Managing Executives Meeting once a month to deliberate on managerial matters.

The Company also has a board of Corporate Auditors, which consists of four auditors, two of which are external auditors. Corporate Auditors are required to conduct a fair and independent audit of the Company's business operations. They attend the Board Meeting, the Managing Executives Meeting, and any other important meetings to oversee directors' decision making and the execution of business, and then present their opinions. The Corporate Auditors Meeting is usually held once a month and otherwise as required.

Tokai Carbon Corporate Governance Structure (Outline as of March 25, 2011)




## Takeover Defense Measures

Tokai Carbon adopted "Countermeasures (Anti-takeover Measures) for Large-scale Purchases of Company Stock and Other Securities" upon receiving approval from the shareholders at the general meeting of shareholders held in March 28, 2008. Due to the fact that the effective term of the Original Plan was until the closing of the general meeting of shareholders in March 25, 2011, our Board of Directors has come to a decision to continue the Countermeasures after making partial amendment to the Original Plan with the aim of ensuring and enhancing the corporate value of Tokai Carbon and the common interests of its shareholders. The plan was approved and passed at the 149th general meeting of shareholders held in March 25,2011 and shall remain in effect for a period of 3 years until the date of conclusion of the general meeting of shareholders to be held in 2014.







## Consolidated Balance Sheets

TOKAI CARBON Co., Ltd. and Consolidated Subsidiaries
December 31, 2010 and 2009

| | Millions of Yen | | Thousands of U.S. Dollars (Note 1) |
|---|---|---|---|
| | **2010** | 2009 | **2010** |
| **ASSETS** | | | |
| **CURRENT ASSETS:** | | | |
| Cash and cash equivalents | **¥ 14,005** | ¥ 8,978 | **$ 171,862** |
| Receivables: | | | |
| Trade notes and accounts | **30,390** | 27,569 | **372,929** |
| Unconsolidated subsidiaries and associated companies | **1,104** | 839 | **13,547** |
| Allowance for doubtful receivables | **(65)** | (110) | **(798)** |
| Inventories (Note 4) | **33,869** | 36,821 | **415,622** |
| Deferred tax assets (Note 10) | **688** | 897 | **8,443** |
| Prepaid expenses and other current assets | **1,694** | 1,884 | **20,788** |
| Total current assets | **81,685** | 76,878 | **1,002,393** |
| **PROPERTY, PLANT AND EQUIPMENT :** | | | |
| Land | **7,088** | 7,264 | **86,980** |
| Buildings and structures | **46,316** | 46,032 | **568,364** |
| Machinery and equipment | **115,968** | 114,618 | **1,423,095** |
| Furniture and fixtures | **6,555** | 6,627 | **80,439** |
| Lease assets | **16** | 12 | **196** |
| Construction in progress | **5,054** | 4,081 | **62,020** |
| Total | **180,997** | 178,634 | **2,221,094** |
| Accumulated depreciation | **(130,081)** | (123,866) | **(1,596,282)** |
| Net property, plant and equipment | **50,916** | 54,768 | **624,812** |
| **INVESTMENTS AND OTHER ASSETS:** | | | |
| Investment securities (Note 3) | **18,286** | 18,566 | **224,396** |
| Investments in and advances to unconsolidated subsidiaries and associated companies | **2,563** | 2,777 | **31,452** |
| Deferred tax assets (Note 10) | **244** | 342 | **2,994** |
| Other assets | **1,610** | 1,591 | **19,757** |
| Total investments and other assets | **22,703** | 23,276 | **278,599** |
| **TOTAL** | **¥155,304** | ¥154,922 | **$1,905,804** |

See notes to consolidated financial statements.

| | Millions of Yen | | Thousands of U.S. Dollars (Note 1) |
|---|---|---|---|
| | **2010** | 2009 | **2010** |
| **LIABILITIES AND EQUITY** | | | |
| **CURRENT LIABILITIES:** | | | |
| Short-term bank loans (Note 5) | **¥ 5,992** | ¥ 10,678 | **$ 73,530** |
| Current portion of long-term debt (Note 5) | **283** | 12 | **3,473** |
| Payables: | | | |
| Trade notes and accounts | **14,959** | 10,416 | **183,569** |
| Unconsolidated subsidiaries and associated companies | **92** | 72 | **1,129** |
| Income taxes payable | **1,351** | 1,844 | **16,579** |
| Accrued expenses | **1,398** | 1,522 | **17,155** |
| Other current liabilities | **4,551** | 4,038 | **55,847** |
| Total current liabilities | **28,626** | 28,582 | **351,282** |
| **LONG-TERM LIABILITIES:** | | | |
| Long-term debt (Note 5) | **12,171** | 11,342 | **149,356** |
| Liability for retirement benefits (Note 7) | **2,411** | 2,569 | **29,586** |
| Retirement allowances for directors, corporate auditors and operating officers (Note 8) | **285** | 332 | **3,497** |
| Allowance for environmental safety measures (Note 2.i) | **924** | 728 | **11,339** |
| Deferred tax liabilities (Note 10) | **4,209** | 4,180 | **51,651** |
| Other | **1,072** | 1,147 | **13,155** |
| Total long-term liabilities | **21,072** | 20,298 | **258,584** |
| **COMMITMENTS AND CONTINGENT LIABILITIES** (Notes 12 and 15) | | | |
| **EQUITY** (Note 9): | | | |
| Common stock — authorized, 598,764,000 shares; issued, 224,943,104 shares in 2010 and 2009 | **20,436** | 20,436 | **250,779** |
| Capital surplus | **17,503** | 17,503 | **214,787** |
| Retained earnings | **71,388** | 67,500 | **876,034** |
| Net unrealized gain on available-for-sale securities | **5,824** | 5,988 | **71,469** |
| Deferred gain on derivatives under hedge accounting | | | |
| Foreign currency translation adjustments | **(4,542)** | (2,167) | **(55,737)** |
| Treasury stock — at cost, 11,368,713 shares in 2010 and 7,176,461 shares in 2009 | **(7,126)** | (5,112) | **(87,446)** |
| Total | **103,483** | 104,148 | **1,269,886** |
| Minority interests | **2,123** | 1,894 | **26,052** |
| Total equity | **105,606** | 106,042 | **1,295,938** |
| | | | |
| **TOTAL** | **¥155,304** | ¥154,922 | **$1,905,804** |

See notes to consolidated financial statements.

## Consolidated Statements of Income

TOKAI CARBON Co., Ltd. and Consolidated Subsidiaries
Years Ended December 31, 2010 and 2009

| | Millions of Yen | | Thousands of U.S. Dollars (Note 1) |
|---|---|---|---|
| | **2010** | 2009 | **2010** |
| **NET SALES** | **¥107,679** | ¥83,298 | **$1,321,377** |
| | | | |
| **COST OF SALES** | **83,331** | 64,975 | **1,022,592** |
| Gross profit | **24,348** | 18,323 | **298,785** |
| | | | |
| **SELLING, GENERAL AND ADMINISTRATIVE EXPENSES** | **13,773** | 13,024 | **169,015** |
| Operating income | **10,575** | 5,299 | **129,770** |
| | | | |
| **OTHER INCOME (EXPENSES):** | | | |
| Interest and dividends | **377** | 437 | **4,626** |
| Interest expense | **(649)** | (606) | **(7,964)** |
| Exchange gain (losses) | **(935)** | 175 | **(11,474)** |
| Equity in gains (losses) of associated companies | **362** | (111) | **4,442** |
| Gain on sales of property, plant and equipment | | 192 | |
| Gain on sales of investment securities | | 940 | |
| Impairment losses (Note 6) | **(441)** | (880) | **(5,412)** |
| Provision for environment and safety measures | **(289)** | | **(3,546)** |
| Special retirement payments | | (258) | |
| Other — net | **212** | (250) | **2,602** |
| Other expenses — net | **(1,363)** | (361) | **(16,726)** |
| **INCOME BEFORE INCOME TAXES AND MINORITY INTERESTS** | **9,212** | 4,938 | **113,044** |
| **INCOME TAXES** (Note 10): | | | |
| Current | **2,790** | 2,620 | **34,237** |
| Deferred | **443** | (349) | **5,436** |
| Total | **3,233** | 2,271 | **39,673** |
| **MINORITY INTERESTS IN NET INCOME (LOSS)** | **348** | (7) | **4,270** |
| **NET INCOME** | **¥ 5,631** | ¥ 2,674 | **$ 69,101** |
| | Yen | | U.S. Dollars |
| | **2010** | 2009 | **2010** |
| **PER SHARE OF COMMON STOCK** (Notes 2.q and 16): | | | |
| Net income | **¥26.05** | ¥12.28 | **$0.32** |
| Cash dividends applicable to the year | **8.00** | 8.00 | **0.09** |

See notes to consolidated financial statements.

## Consolidated Statements of Changes in Equity

TOKAI CARBON Co., Ltd. and Consolidated Subsidiaries
Years Ended December 31, 2010 and 2009

| | Thousands of Shares / Millions of Yen | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Common Stock | | | | | Deferred | | Treasury Stock | | | | |
| | Shares | Amount | Capital Surplus | Retained Earnings | Unrealized Gain (Losses) on Available-for-Sale Securities | Gain (Losses) on Derivatives under Hedge Accounting | Foreign Currency Translation Adjustments | Shares | Amount | Total | Minority Interests | Total Equity |
| **BALANCE, JANUARY 1, 2009** | **224,943** | **¥20,436** | **¥17,503** | **¥66,778** | **¥5,913** | **¥6** | **¥(2,817)** | **(7,148)** | **¥(5,105)** | **¥102,714** | **¥1,720** | **¥104,434** |
| Net income | | | | 2,674 | | | | | | 2,674 | | 2,674 |
| Cash dividends, ¥8.00 per share | | | | (1,960) | | | | | | (1,960) | | (1,960) |
| Purchase of treasury stock | | | | | | | | (40) | (16) | (16) | | (16) |
| Disposal of treasury stock | | | | (4) | | | | 12 | 9 | 5 | | 5 |
| Increase due to application of PITF No. 18 | | | | 12 | | | | | | 12 | | 12 |
| Net change in the year | | | | | 75 | (6) | 650 | | | 719 | 174 | 893 |
| **BALANCE, DECEMBER 31, 2009** | **224,943** | **20,436** | **17,503** | **67,500** | **5,988** | | **(2,167)** | **(7,176)** | **(5,112)** | **104,148** | **1,894** | **106,042** |
| Net income | | | | 5,631 | | | | | | 5,631 | | 5,631 |
| Cash dividends, ¥8.00 per share | | | | (1,742) | | | | | | (1,742) | | (1,742) |
| Purchase of treasury stock | | | | | | | | (4,196) | (2,017) | (2,017) | | (2,017) |
| Disposal of treasury stock | | | | (1) | | | | 4 | 3 | 2 | | 2 |
| Net change in the year | | | | | (164) | | (2,375) | | | (2,539) | 229 | (2,310) |
| **BALANCE, DECEMBER 31, 2010** | **224,943** | **¥20,436** | **¥17,503** | **¥71,388** | **¥ 5,824** | | **¥(4,542)** | **(11,368)** | **¥(7,126)** | **¥103,483** | **¥2,123** | **¥105,606** |

| | Thousands of U.S. Dollars (Note 1) | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Common Stock | Capital Surplus | Retained Earnings | Unrealized Gain (Losses) on Available-for-Sale Securities | Deferred Gain (Losses) on Derivatives under Hedge Accounting | Foreign Currency Translation Adjustments | Treasury Stock | Total | Minority Interests | Total Equity |
| **BALANCE, DECEMBER 31, 2009** | **$250,779** | **$214,787** | **$828,322** | **$73,481** | | **$(26,592)** | **$(62,732)** | **$1,278,045** | **$23,242** | **$1,301,287** |
| Net income | | | 69,101 | | | | | 69,101 | | 69,101 |
| Cash dividends, $0.09 per share | | | (21,377) | | | | | (21,377) | | (21,377) |
| Purchase of treasury stock | | | | | | | (24,751) | (24,751) | | (24,751) |
| Disposal of treasury stock | | | (12) | | | | 37 | 25 | | 25 |
| Net change in the year | | | | (2,012) | | (29,145) | | (31,157) | 2,810 | (28,347) |
| **BALANCE, DECEMBER 31, 2010** | **$250,779** | **$214,787** | **$876,034** | **$71,469** | | **$(55,737)** | **$(87,446)** | **$1,269,886** | **$26,052** | **$1,295,938** |

See notes to consolidated financial statements.

## Consolidated Statements of Cash Flows

TOKAI CARBON Co., Ltd. and Consolidated Subsidiaries
Years Ended December 31, 2010 and 2009

| | Millions of Yen | | Thousands of U.S. Dollars (Note 1) |
|---|---|---|---|
| | **2010** | 2009 | **2010** |
| **OPERATING ACTIVITIES:** | | | |
| Income before income taxes and minority interests | **¥9,212** | ¥4,938 | **$113,044** |
| Adjustments for: | | | |
| Income taxes — paid | **(3,046)** | (3,716) | **(37,379)** |
| Depreciation and amortization | **8,854** | 9,525 | **108,651** |
| Amortization of consolidation differences | | 80 | |
| Increase in liability for retirement benefits | **170** | 442 | **2,086** |
| (Increase) decrease in prepaid expense for pension cost | **(228)** | 153 | **(2,798)** |
| Exchange losses | **295** | | **3,620** |
| Equity in gains (losses) of associated companies | **(362)** | 111 | **(4,442)** |
| Increase in allowance for environment and safety measures | **196** | | **2,405** |
| Gains on sales of investment securities | | (940) | |
| Gains on sales of property, plant and equipment | | (192) | |
| Impairment losses | **441** | 880 | **5,412** |
| (Increase) decrease in trade notes and accounts receivable | **(4,045)** | 8,447 | **(49,638)** |
| Decrease in inventories | **1,816** | 435 | **22,285** |
| Increase (decrease) in notes and accounts payable | **5,038** | (8,198) | **61,824** |
| Increase in consumption taxes payable | **223** | 155 | **2.736** |
| Decrease in interest and dividend receivables | **58** | 58 | **712** |
| Increase in interest payable | **3** | 50 | **37** |
| Increase in special retirement payments | | (16) | |
| Other — net | **(38)** | (131) | **(466)** |
| Total adjustments | **9,375** | 7,143 | **115,045** |
| Net cash provided by operating activities | **18,587** | 12,081 | **228,089** |
| **INVESTING ACTIVITIES:** | | | |
| Proceeds from repayment of time deposits | **239** | | **2,933** |
| Payment for purchases of property, plant and equipment | **(6,375)** | (10,812) | **(78,230)** |
| Proceeds from sales of property, plant and equipment | **160** | 629 | **1,964** |
| Proceeds from sales of investment securities | | 1,578 | |
| Payments for long-term loans | | (286) | |
| Other | **(113)** | (341) | **(1,387)** |
| Net cash used in investing activities | **(6,089)** | (9,232) | **(74,720)** |
| **FINANCING ACTIVITIES:** | | | |
| Decrease in short-term bank loans — net | **(4,387)** | (16,181) | **(53,835)** |
| Proceeds from long-term debt | **1,385** | 11,332 | **16,996** |
| Repayments of long-term debt | | (580) | |
| Payments for purchases of treasury stock | **(2,017)** | (16) | **(24,752)** |
| Dividends paid | **(1,769)** | (1,980) | **(21,708)** |
| Proceeds from issuances of common stock by consolidated subsidiaries to minority shareholders | | 133 | |
| Other | **(8)** | 5 | **(98)** |
| Net cash used in financing activities | **(6,796)** | (7,287) | **(83,397)** |
| FOREIGN CURRENCY TRANSLATION ADJUSTMENTS ON CASH AND CASH EQUIVALENTS | **(675)** | 142 | **(8,283)** |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | **5,027** | (4,296) | **61,689** |
| CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR | **8,978** | 13,274 | **110,173** |
| CASH AND CASH EQUIVALENTS, END OF YEAR | **¥14,005** | ¥8,978 | **$171,862** |

See notes to consolidated financial statements.

## Notes to Consolidated Financial Statements

TOKAI CARBON Co., Ltd. and Consolidated Subsidiaries
Years Ended December 31, 2010 and 2009

### 1. BASIS OF PRESENTING CONSOLIDATED FINANCIAL STATEMENTS

The accompanying consolidated financial statements have been prepared in accordance with the provisions set forth in the Japanese Financial Instruments and Exchange Act and its related accounting regulations, and in conformity with accounting principles generally accepted in Japan ("Japanese GAAP"), which are different in certain respects as to the application and disclosure requirements of International Financial Reporting Standards.

In preparing these consolidated financial statements, certain reclassifications and rearrangements have been made to the consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan. In addition, certain reclassifications have been made in the 2009 consolidated financial statements to conform to the classifications used in 2010.

The consolidated financial statements are stated in Japanese yen, the currency of the country in which TOKAI CARBON Co., Ltd. (the "Company") is incorporated and operates. The translation of Japanese yen amounts into U.S. dollar amounts is included solely for the convenience of readers outside Japan and has been made at the rate of ¥81.49 to $1, the approximate rate of exchange at December 31, 2010. Such translation should not be construed as a representation that the Japanese yen amounts could be converted into U.S. dollars at that or any other rate.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**a. Consolidation —** The consolidated financial statements as of December 31, 2010 include the accounts of the Company and its significant 24 (24 in 2009) subsidiaries (together, the "Group").

Under the control or influence concept, those companies in which the Company, directly or indirectly, is able to exercise control over operations are fully consolidated, and those companies over which the Group has the ability to exercise significant influence are accounted for by the equity method.

Investments in 6 (6 in 2009) associated companies are accounted for by the equity method. Investments in the remaining 2 (2 in 2009) unconsolidated subsidiaries are stated at cost. If the equity method of accounting had been applied to the investments in these companies, the effect on the accompanying consolidated financial statements would not be material.

The difference between the cost and underlying net equity of investments in consolidated subsidiaries and associated companies is deferred and amortized using the straight-line method over a certain period which is derived on an individual case basis, with the exception of minor differences which are charged or credited to income in the period of acquisition.

All significant intercompany balances and transactions have been eliminated in consolidation. All material unrealized profit included in assets resulting from transactions within the Group is eliminated.

**b. Unification of Accounting Policies Applied to Foreign Subsidiaries for the Consolidated Financial Statements —** In May 2006, the Accounting Standards Board of Japan (the "ASBJ") issued ASBJ Practical Issues Task Force ("PITF") No. 18, "Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries for the Consolidated Financial Statements." PITF No. 18 prescribes that (1) the accounting policies and procedures applied to a parent company and its subsidiaries for similar transactions and events under similar circumstances should in principle be unified for the preparation of the consolidated financial statements, (2) financial statements prepared by foreign subsidiaries in accordance with either International Financial Reporting Standards or the generally accepted accounting principles in the United States of America tentatively may be used for the consolidation process, (3) however, the following items should be adjusted in the consolidation process so that net income is accounted for in accordance with Japanese GAAP unless they are not material: (a) amortization of goodwill; (b) scheduled amortization of actuarial gains or losses of pensions that has been directly recorded in equity; (c) expensing capitalized development costs of R&D; (d) cancellation of fair value model accounting for property, plant and equipment and investment properties and incorporation of cost model accounting; (e) recording the prior years' effects of changes in accounting policies in the income statement where retrospective adjustments to financial statements have been incorporated; and (f) exclusion of minority interests from net income, if contained. PITF No. 18 was effective for fiscal years beginning on or after April 1, 2008 with early adoption permitted.

**c. Cash Equivalents —** 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, mutual funds invested in bonds that represent short-term investments, and securities purchased under resale arrangements, all of which mature or become due within three months of the date of acquisition.

**d. Inventories —** Inventories of the Company and consolidated domestic subsidiaries were stated at cost, being determined by the average method.

Inventories of foreign consolidated subsidiaries are stated principally at the lower of cost or market, with cost being determined using the first-in, first-out method.

**e. Marketable and Investment Securities —** Marketable and investment securities are classified and accounted for, depending on management's intent, as follows: (1) 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 (2) available-for-sale securities, which are not classified as the aforementioned securities, are classified as available-for-sale securities and reported at fair value, with unrealized gains and losses, net of applicable taxes, reported in a separate component of equity.

Non-marketable available-for-sale securities are stated at cost determined by the moving-average method. For other than temporary declines in fair value, available-for-sale securities are reduced to net realizable value by a charge to income.

**f. Property, Plant and Equipment —** Property, plant and equipment are stated at cost. Depreciation of property, plant and equipment of the Company and its consolidated domestic subsidiaries is computed principally by the declining-balance method at rates based on the estimated useful lives of the assets, while the straight-line method is applied to the buildings of the Company and its domestic subsidiaries, and to all property, plant and equipment of consolidated foreign subsidiaries. Equipment held for lease is depreciated by the straight-line method over the respective lease periods.

The range of useful lives is principally from 2 to 60 years for buildings and structures and from 2 to 22 years for machinery and equipment.

**g. Employees' Retirement Benefits —** The Company and certain domestic consolidated subsidiaries have contributory funded pension plans. Other domestic consolidated subsidiaries have funded and unfunded retirement benefit plans.

Employees' retirement benefits are accounted for as a liability for retirement benefits based on projected benefit obligations and plan assets at the balance sheet date.

Change in accounting policy

Effective from the year ended December 31, 2010, the Company adopted the "Partial Amendments to Accounting Standard for Retirement Benefits (Part 3)" (Statement No. 19 issued by the ASBJ on July 31, 2008).

The adoption of this standard had no effect on the consolidated financial statements.

Additional information

The Company shifted from a tax-qualified pension plan to a defined benefit pension plan in January of 2010.

The shift had no effect on the consolidated financial statements.

**h. Retirement Allowances for Directors, Corporate Auditors and Operating Officers —** Retirement allowances for directors, corporate auditors and operating officers are recorded to state the liability at the amount that would be required if all directors, corporate auditors and operating officers retired at each balance sheet date.

The liability for retirement benefits for directors and corporate auditors is stated at the fixed amount required to be paid in accordance with the Company's internal regulations if they had retired on March 30, 2006 because such plan for directors and corporate auditors was repealed effective March 30, 2006.

**i. Allowance for Environmental Safety Measures —** In accordance with the Special Measures Law for the Promotion of Proper Disposal of Polychlorinated Biphenyl ("PCB") Waste, the Company sets aside a reserve in an amount equal to the estimated disposal expenses for stored PCB's as of the balance sheet date.

**j. Research and Development Costs —** Expenditures for research and development activities are charged to income as incurred.

**k. Leases —** In March 2007, the ASBJ issued ASBJ Statement No. 13, "Accounting Standard for Lease Transactions," which revised the previous accounting standard for lease transactions issued in June 1993. The revised accounting standard for lease transactions is effective for fiscal years beginning on or after April 1, 2008 with early adoption permitted for fiscal years beginning on or after April 1, 2007.

Under the previous accounting standard, finance leases that were deemed to transfer ownership of the leased property to the lessee were to be capitalized. However, other finance leases were permitted to be accounted for as operating lease transactions if certain "as if capitalized" information is disclosed in the notes to the lessee's financial statements. The revised accounting standard requires that all finance lease transactions should be capitalized to recognize lease assets and lease obligations in the balance sheet. In addition, the accounting standard permits leases which existed at the transition date and do not transfer ownership of the leased property to the lessee to be accounted for as operating lease transactions.

The Company accounted for leases which existed at the transition date and do not transfer ownership of the leased property to the lessee as operating lease transactions.

**l. Income Taxes —** The provision for income taxes is computed based on the pretax income included in the consolidated statements of income. The asset and liability approach is used to recognize deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. Deferred taxes are measured by applying currently enacted tax laws to the temporary differences.

**m. Appropriations of Retained Earnings —** Appropriations of retained earnings at each year-end are reflected in the consolidated financial statements for the following year upon shareholders' approval.

**n. Foreign Currency Transactions —** 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 forward exchange contracts.

**o. 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 equity, which is translated at the historical rate. Differences arising from such translation were shown as "Foreign currency translation adjustments" in a separate component of equity.

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

**p. Derivatives and Hedging Activities —** The Group uses derivative financial instruments to manage its exposures to fluctuations in foreign exchange and interest rates. Foreign exchange forward contracts and interest rate swaps are utilized by the Group to reduce foreign currency exchange and interest rate risks. The Group does not enter into derivatives for trading or speculative purposes.

Gains and losses on derivatives used for hedging purposes, if the derivatives qualify for hedge accounting because of high correlation and effectiveness between the hedging instruments and the hedged items, are deferred until the maturity of the hedged transactions.

Foreign exchange forward contracts employed to hedge foreign exchange exposures to export sales are measured at fair value.

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 is recognized and included in interest expense or income.

**q. Per Share Information —** Basic net income per share is computed by dividing net income available to common shareholders by the weighted-average number of common shares outstanding for the period.

Diluted net income per share reflects the potential dilution that could occur if securities were exercised or converted into common stock. 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 time of issuance) with an applicable adjustment for related interest expense, net of tax.

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.

**r. New Accounting Pronouncements Asset Retirement Obligations —** In March 2008, the ASBJ published a new accounting standard for asset retirement obligations, ASBJ Statement No. 18, "Accounting Standard for Asset Retirement Obligations," and ASBJ Guidance No. 21, "Guidance on Accounting Standard for Asset Retirement Obligations." Under this accounting standard, an asset retirement obligation is defined as a legal obligation imposed either by law or contract that results from the acquisition, construction, development and the normal operation of a tangible fixed asset and is associated with the retirement of such tangible fixed asset.

The asset retirement obligation is recognized as the sum of the discounted cash flows required for the future asset retirement and is recorded in the period in which the obligation is incurred if a reasonable estimate can be made. If a reasonable estimate of the asset retirement obligation cannot be made in the period the asset retirement obligation is incurred, the liability should be recognized when a reasonable estimate of asset retirement obligation can be made. Upon initial recognition of a liability for an asset retirement obligation, an asset retirement cost is capitalized by increasing the carrying amount of the related fixed asset by the amount of the liability. The asset retirement cost is subsequently allocated to expense through depreciation over the remaining useful life of the asset. Over time, the liability is accreted to its present value each period. Any subsequent revisions to the timing or the amount of the original estimate of undiscounted cash flows are reflected as an increase or a decrease in the carrying amount of the liability and the capitalized amount of the related asset retirement cost. This standard is effective for fiscal years beginning on or after April 1, 2010 with early adoption permitted for fiscal years beginning on or before March 31, 2010.

Accounting Changes and Error Corrections — In December 2009, the ASBJ issued ASBJ Statement No. 24, "Accounting Standard for Accounting Changes and Error Corrections," and ASBJ Guidance No. 24, "Guidance on Accounting Standard for Accounting Changes and Error Corrections." Accounting treatments under this standard and guidance are as follows:

(1) Changes in accounting policy

When a new accounting policy is applied with a revision of accounting standards, the new policy is applied retrospectively unless the revised accounting standards include specific transitional provisions. When the revised accounting standards include specific transitional provisions, an entity shall comply with the specific transitional provisions.

(2) Changes in presentations

When the presentation of financial statements is changed, prior period financial statements are reclassified in accordance with the new presentation.

(3) Changes in accounting estimates

A change in an accounting estimate is accounted for in the period of the change if the change affects that period only, and is accounted for prospectively if the change affects both the period of the change and future periods.

(4) Corrections of prior period errors

When an error in prior period financial statements is discovered, those statements are restated.

This accounting standard and the guidance are applicable to accounting changes and corrections of prior period errors which are made from the beginning of the fiscal year that begins on or after April 1, 2011.

Segment Information Disclosures — In March 2008, the ASBJ revised ASBJ Statement No. 17, "Accounting Standard for Segment Information Disclosures," and issued ASBJ Guidance No. 20, "Guidance on Accounting Standard for Segment Information Disclosures." Under the standard and guidance, an entity is required to report financial and descriptive information about its reportable segments. Reportable segments are operating segments or aggregations of operating segments that meet specified criteria. Operating segments are components of an entity about which separate financial information is available and such information is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. Generally, segment information is required to be reported on the same basis as is used internally for evaluating operating segment performance and deciding how to allocate resources to operating segments. This accounting standard and the guidance are applicable to segment information disclosures for the fiscal years beginning on or after April 1, 2010.

## 3. MARKETABLE AND INVESTMENT SECURITIES

Marketable and investment securities as of December 31, 2010 and 2009 consisted of the following:

| | Millions of Yen | | Thousands of U.S. Dollars |
|---|---|---|---|
| | 2010 | 2009 | 2010 |
| **Non-current:** | | | |
| Marketable equity securities | ¥18,257 | ¥18,527 | $224,040 |
| Non-marketable equity securities | 28 | 38 | 344 |
| Trust fund investments and other | 1 | 1 | 12 |
| **Total** | ¥18,286 | ¥18,566 | $224,396 |

The carrying amounts and aggregate fair values of marketable and investment securities at December 31, 2010 and 2009 were as follows:

| | Millions of Yen | | | |
|---|---|---|---|---|
| December 31, 2010 | Cost | Unrealized Gains | Unrealized Losses | Fair Value |
| Securities classified as available-for-sale — Equity securities | ¥9,046 | ¥9,606 | ¥(395) | ¥18,257 |
| December 31, 2009 | | | | |
| Securities classified as available-for-sale — Equity securities | ¥9,022 | ¥9,930 | ¥(425) | ¥18,527 |
| | Thousands of U.S. Dollars | | | |
| December 31, 2010 | Cost | Unrealized Gains | Unrealized Losses | Fair Value |
| Securities classified as available-for-sale — Equity securities | $111,007 | $117,880 | $(4,847) | $224,040 |

## 4. INVENTORIES

Inventories at December 31, 2010 and 2009 consisted of the following:

| | Millions of Yen | | Thousands of U.S. Dollars |
|---|---|---|---|
| | 2010 | 2009 | 2010 |
| Merchandise | ¥ 102 | ¥ 99 | $ 1,252 |
| Finished products | 6,619 | 6,861 | 81,225 |
| Work in process | 17,865 | 20,123 | 219,229 |
| Raw materials and supplies | 9,283 | 9,738 | 113,916 |
| **Total** | ¥33,869 | ¥36,821 | $415,622 |

## 5. SHORT-TERM BANK LOANS AND LONG-TERM DEBT

Short-term bank loans at December 31, 2010 and 2009 consisted of notes to banks and bank overdrafts. The annual interest rates applicable to the short-term bank loans ranged from 0.180% to 5.100% and from 0.305% to 4.860% at December 31, 2010 and 2009, respectively.

Long-term debt at December 31, 2010 and 2009 consisted of the following:

| | Millions of Yen | | Thousands of U.S. Dollars |
|---|---|---|---|
| | 2010 | 2009 | 2010 |
| Long-term loans from banks and insurance companies<br>2010: 1.40% – 4.39% due 2011 – 2014<br>2009: 1.40% – 4.39% due 2010 | ¥12,442 | ¥11,343 | $152,682 |
| Obligations under finance leases | 12 | 11 | 147 |
| Total | 12,454 | 11,354 | 152,829 |
| Less current portion | (283) | (12) | (3,473) |
| **Long-term debt, less current portion** | ¥12,171 | ¥11,342 | $149,356 |

Annual maturities of long-term debt, excluding finance leases (see Note 12), at December 31, 2010 were as follows:

| Year Ending December 31 | Millions of Yen | Thousands of U.S. Dollars |
|---|---|---|
| 2011 | ¥ 283 | $ 3,473 |
| 2012 | 10,277 | 126,114 |
| 2013 | 813 | 9,977 |
| 2014 | 1,081 | 13,265 |
| **Total** | ¥12,454 | $152,829 |

## 6. LONG-LIVED ASSETS

The Group groups long-lived asset, principally based on the division of management accounting, but leasehold improvements and idle assets are grouped by respective asset category. The Group reviewed its long-lived assets for impairment as of December 31, 2010 and, as a result, recognized an impairment loss of ¥441 million ($5,412 thousand) as an other expense for certain idle assets of the plant assets group of the Chigasaki plant and Shizuoka land on the Company. The recoverable amount of Chigasaki plant was measured based on its discounted cash flow. The recoverable amount of Shizuoka land was measured at its net selling price.

## 7. RETIREMENT AND PENSION PLANS

Employees whose service with the Company and certain consolidated domestic subsidiaries is terminated 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.

The liability (asset) for employees' retirement benefits at December 31, 2010 and 2009 consisted of the following:

| | Millions of Yen | | Thousands of U.S. Dollars |
|---|---|---|---|
| | 2010 | 2009 | 2010 |
| Projected benefit obligation | ¥6,169 | ¥6,366 | $75,703 |
| Fair value of plan assets | (3,962) | (3,700) | (48,620) |
| Unrecognized actuarial loss | (127) | (201) | (1,559) |
| Prepaid expense for pension cost | 331 | 104 | 4,062 |
| **Net liability** | ¥2,411 | ¥2,569 | $29,586 |

The components of net periodic benefit costs for the years ended December 31, 2010 and 2009 are as follows:

| | Millions of Yen | | Thousands of U.S. Dollars |
|---|---|---|---|
| | 2010 | 2009 | 2010 |
| Service cost | ¥340 | ¥475 | $4,172 |
| Interest cost | 76 | 80 | 933 |
| Amortization of actuarial gain | 59 | 85 | 724 |
| Other | 59 | 66 | 724 |
| **Net periodic benefit costs** | ¥534 | ¥706 | $6,553 |

Assumptions used for the years ended December 31, 2010 and 2009 are set forth as follows:

| | 2010 | 2009 |
|---|---|---|
| Discount rate | 2.0% | 2.0% |
| Expected rate of return on plan assets | 0.0% | 0.0% |
| Recognition period of actuarial gain / loss | 10 years | 10 years |

## 8. RETIREMENT ALLOWANCES FOR DIRECTORS, CORPORATE AUDITORS AND OPERATING OFFICERS

Retirement allowances for directors, corporate auditors and operating officers are paid subject to approval of the shareholders in accordance with the Companies Act of Japan (the "Companies Act").

The Company recorded a liability for its unfunded retirement allowance plan covering all of its directors, corporate auditors and operating officers. The annual provisions for retirement allowances for directors, corporate auditors and operating officers for the years ended December 31, 2010 and 2009 were ¥39 million ($480 thousand) and ¥50 million, respectively.

In addition, the director retirement bonus plan was abolished.

## 9. EQUITY

Japanese companies are subject to the Companies Act. The significant provisions in the Companies Act that affect financial and accounting matters are summarized below:

**a. Dividends**

Under the Companies Act, companies can pay dividend at any time during the fiscal year in addition to the year-end dividend upon resolution at the shareholders meeting. For companies that meet certain criteria such as: (1) having a Board of Directors, (2) having independent auditors, (3) having a Board of Corporate Auditors, and (4) the term of service of the directors is prescribed as one year rather than two years of normal term by its articles of incorporation, the Board of Directors may declare dividends (except for dividends-in-kind) at any time during the fiscal year if the company has prescribed so in its articles of incorporation.

The Companies Act permits companies to distribute dividends-in-kind (non-cash assets) to shareholders subject to certain limitations and additional requirements.

Semiannual interim dividends may be paid once a year upon resolution by the Board of Directors if the articles of incorporation of the company so stipulate. The Companies Act provides certain limitations on the amounts available for dividends or the purchase of treasury stock. The limitation is defined as the amount available for distribution to the shareholders, but the amount of net assets after dividends must be maintained at no less than ¥3 million.

**b. Increases / Decreases and Transfer of Common Stock, Reserve and Surplus**

The Companies Act requires that an amount equal to 10% of dividends must be appropriated as a legal reserve (a component of retained earnings) or as additional paid in capital (a component of capital surplus) depending on the equity account charged upon the payment of such dividends until the total of the aggregate amount of the legal reserve and additional paid-in capital equals 25% of common stock. Under the Companies Act, the total amount of additional paid-in capital and legal reserve may be reversed without limitation. The Companies Act also provides that common stock, legal reserve, additional paid-in capital, other capital surplus and retained earnings can be transferred among the accounts under certain conditions upon resolution of the shareholders.

**c. Treasury Stock and Treasury Stock Acquisition Rights**

The Companies Act provides for companies to purchase treasury stock and dispose of such treasury stock by resolution of the Board of Directors. The amount of treasury stock purchased cannot exceed the amount available for distribution to the shareholders which is determined by specific formula.

Under the Companies Act, stock acquisition rights are presented as a separate component of equity.

The Companies Act provides that companies can purchase both treasury stock acquisition rights and treasury stock. Such treasury stock acquisition rights are presented as a separate component of equity or deducted directly from stock acquisition rights.

## 10. INCOME TAXES

The Company and its domestic subsidiaries are subject to Japanese national and local income taxes which, in the aggregate, resulted in a normal effective statutory tax rate of approximately 40% for the years ended December 31, 2010 and 2009.

The tax effects of significant temporary differences which resulted in deferred tax assets and liabilities at December 31, 2010 and 2009 are as follows:

| | Millions of Yen | | Thousands of U.S. Dollars |
|---|---|---|---|
| | 2010 | 2009 | 2010 |
| **Deferred tax assets:** | | | |
| Depreciation and amortization | ¥ 116 | ¥ 135 | $ 1,424 |
| Impairment loss on long-lived assets | 671 | 495 | 8,234 |
| Retirement and severance benefits | 505 | 488 | 6,197 |
| Allowance for officers' retirement benefits | 90 | 102 | 1,104 |
| Allowance for environmental safety measures | 370 | 291 | 4,540 |
| Accrued enterprise tax | 109 | 144 | 1,338 |
| Unrealized gains on sale of assets eliminated in consolidation | 383 | 448 | 4,700 |
| Loss carryforward of subsidiaries | 604 | 693 | 7,412 |
| Valuation loss on investment securities | 387 | 387 | 4,749 |
| Other | 573 | 708 | 7,032 |
| Less valuation allowance | (1,800) | (1,805) | (22,089) |
| Deferred tax assets | 2,008 | 2,086 | 24,641 |
| **Deferred tax liabilities:** | | | |
| Net unrealized gains on available-for-sale securities | 3,427 | 3,557 | 42,054 |
| Deferred profits on property for income tax purposes | 1,082 | 1,046 | 13,278 |
| Retained earnings of overseas consolidated subsidiaries | 281 | 231 | 3,448 |
| Prepaid expense for pension cost | 132 | | 1,620 |
| Other | 363 | 200 | 4,455 |
| Deferred tax liabilities | 5,285 | 5,034 | 64,855 |
| Net deferred tax liabilities | ¥3,277 | ¥2,948 | $40,214 |

Net deferred tax liabilities presented in the consolidated balance sheets at December 31, 2010 and 2009 are as follows:

| | Millions of Yen | | Thousands of U.S. Dollars |
|---|---|---|---|
| | 2010 | 2009 | 2010 |
| Current assets — deferred tax assets | ¥ (688) | ¥ (897) | $ (8,443) |
| Investments and other assets — deferred tax assets | (244) | (342) | (2,994) |
| Current liabilities — deferred tax liabilities | | 7 | |
| Long-term liabilities — deferred tax liabilities | 4,209 | 4,180 | 51,651 |
| Deferred tax liabilities | ¥3,277 | ¥ 2,948 | $40,214 |

A reconciliation between the normal effective statutory tax rate and the actual effective tax rate reflected in the accompanying consolidated statements of income for the years ended December 31, 2010 and 2009 is as follows:

| | 2010 | 2009 |
|---|---|---|
| Normal effective statutory tax rate | **40.00%** | 40.00% |
| Expenses not deductible for income tax purposes | **1.8** | 2.5 |
| Income not taxable for income tax purpose | **(0.4)** | (0.9) |
| Minimum inhabitant taxes | | 0.9 |
| Amortization of consolidation differences | | 7.8 |
| Undistributed earnings of overseas subsidiaries | **0.6** | (17.9) |
| Valuation allowance | | 18.5 |
| Tax credit for experimental and research expense | **(1.8)** | (3.1) |
| Differences of effective tax rate for overseas subsidiaries | **(2.5)** | (3.1) |
| Equity in (gains) losses of associated companies | **(0.9)** | 0.9 |
| Other — net | **(1.7)** | 0.4 |
| Actual effective tax rate | **35.10%** | 46.00% |

## 11. RESEARCH AND DEVELOPMENT COSTS

Research and development costs charged to income were ¥2,012 million ($24,690 thousand) and ¥2,073 million for the years ended December 31, 2010 and 2009, respectively.

## 12. LEASES

As discussed in Note 2, the Company accounts for leases which existed at the transition date and do not transfer ownership of the leased property to the lessee as operating lease transactions. Pro forma information of such leases existing at the transition date, such as acquisition cost, accumulated depreciation, obligations under finance leases, depreciation expense, and interest expense on an "as if capitalized" basis for the years ended December 31, 2010 and 2009 was as follows:

**As a Lessee**

| | Millions of Yen | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | **2010** | | | | 2009 | | | |
| | Machinery and Equipment | Furniture and Fixtures | Software | Total | Machinery and Equipment | Furniture and Fixtures | Software | Total |
| Acquisition cost | **¥3** | **¥8** | **¥4** | **¥15** | ¥7 | ¥20 | ¥4 | ¥31 |
| Accumulated depreciation | **2** | **6** | **3** | **11** | 4 | 17 | 2 | 23 |
| **Net leased property** | **¥1** | **¥2** | **¥1** | **¥ 4** | ¥3 | ¥ 3 | ¥2 | ¥ 8 |

| | Thousands of U.S. Dollars | | | |
|---|---|---|---|---|
| | **2010** | | | |
| | Machinery and Equipment | Furniture and Fixtures | Software | Total |
| Acquisition cost | **$37** | **$98** | **$49** | **$184** |
| Accumulated depreciation | **24** | **74** | **37** | **135** |
| **Net leased property** | **$13** | **$24** | **$12** | **$ 49** |

Future minimum lease payments:

| | Millions of Yen | | Thousands of U.S. Dollars |
|---|---|---|---|
| | **2010** | 2009 | **2010** |
| Due within one year | **¥3** | ¥4 | **$37** |
| Due after one year | **1** | 4 | **12** |
| **Total** | **¥4** | ¥8 | **$49** |

Paid lease fees and depreciation expense:

| | Millions of Yen | | Thousands of U.S. Dollars |
|---|---|---|---|
| | **2010** | 2009 | **2010** |
| Paid lease fees | **¥4** | ¥8 | **$49** |
| Depreciation expense | **4** | 8 | **49** |

The acquisition cost and future minimum lease payments include the imputed interest expense portion.

Depreciation is based on the straight line method over the lease term of the lease assets.

## 13. FINANCIAL INSTRUMENTS AND RELATED DISCLOSURES

In March 2008, the ASBJ revised ASBJ Statement No. 10, "Accounting Standard for Financial Instruments," and issued ASBJ Guidance No. 19, "Guidance on Accounting Standard for Financial Instruments and Related Disclosures." This accounting standard and the guidance are applicable to financial instruments and related disclosures at the end of the fiscal years ending on or after March 31, 2010 with early adoption permitted from the beginning of the fiscal years ending before March 31, 2010. The Group applied the revised accounting standard and the new guidance effective December 31, 2010.

**(1) Policy for Financial Instruments**

The Group policy is to manage highly stable financial assets, centered on investments in short term deposits, and raise funds largely by obtaining bank loans. The Group deployed a cash management system to facilitate intragroup lending and borrowing and use funds more efficiently and reduce financial costs, engaging in intragroup lending and borrowing. Other policies are to employ derivative transactions for hedging risk to mention later and to refrain from speculative trading.

**(2) Nature and Extent of Risks Arising from Financial Instruments**

Trade receivables are exposed to customer credit risk. As the Group operates globally, foreign currency denominated trade receivables are subject to foreign exchange fluctuations. Marketable and investment securities are subject to market risk. Those securities mainly comprise shares in other companies with which the Group does business or has capital affiliations.

Most trade payables are due within one year.

Borrowings are to secure funding needed for operations and capital investments. Some of these instruments are subject to interest rate fluctuation risks, which the Group hedges using interest rate swaps.

The Group engages in two types of derivative transactions. They include forward foreign exchange fluctuation risks associated with foreign currency denominated trade receivables and payables. The Group also uses interest rate swaps to hedge fluctuations in interest rates on borrowings.

**(3) Risk Management for Financial Instruments**

a. Credit risk management (including risk of customers breaching contracts)

In keeping with its credit management rules, the Group regularly monitors the status of key customers with outstanding operating receivables and oversees due dates and balances while endeavoring to swiftly identify and ameliorate collection concerns that could stem from deteriorating financial positions or other factors.

The Group minimizes credit risks relating to counterparty breaches of derivative contracts by transacting solely with highly creditworthy financial institutions.

The maximum credit risk amount at December 31, 2010 is the balance sheet value of financial assets exposed to such risks.

b. Market risk management (foreign exchange and interest rate risks)

Where necessary, the Group hedges the resulting risks, net of foreign currency denominated trade receivables and payables, with forward foreign exchange contracts. It uses interest rate swaps to minimize the risks of interest payment fluctuations.

The Group regularly assesses the prices of marketable and investment securities and the financial positions of issuers (business partners). It factors in relationships with business partners in constantly reviewing the necessity of instruments.

The execution and control of derivative transactions is maintained based on internal rules on transaction rights.

c. Funding-related liquidity risk management (risk of inability to settle by payment dates)

The Group is exposed to liquidity risk customer credit and debt, managing them by producing and managing funding plans.

**(4) Fair Values of Financial Instruments**

Fair values of financial instruments are based on quoted prices in active markets. If quoted prices are not available, other rational valuation techniques are used instead. Please see Note 14 for the detail of the fair value of derivatives.

a. Fair value of financial instruments

| | Millions of Yen | | |
|---|---|---|---|
| December 31, 2010 | Carrying Amount | Fair Value | Unrealized Gain / Loss |
| Cash and cash equivalents | ¥12,076 | ¥12,076 | |
| Receivables | 31,494 | 31,494 | |
| Investment securities | 19,571 | 22,000 | ¥2,429 |
| Total | ¥63,141 | ¥65,570 | ¥2,429 |
| Payables | ¥15,052 | ¥15,052 | |
| Long-term debt | 12,162 | 12,210 | ¥ 48 |
| Total | ¥27,214 | ¥27,262 | ¥ 48 |

| | Thousands of U.S. Dollars | | |
|---|---|---|---|
| December 31, 2010 | Carrying Amount | Fair Value | Unrealized Gain / Loss |
| Cash and cash equivalents | $148,190 | $148,190 | |
| Receivables | 386,477 | 386,477 | |
| Investment securities | 240,164 | 269,972 | $29,808 |
| Total | $774,831 | $804,639 | $29,808 |
| Payables | $184,710 | $184,710 | |
| Long-term debt | 149,245 | 149,834 | $ 589 |
| Total | $333,955 | $334,544 | $ 589 |

**Cash and Cash Equivalents**
The carrying values of cash and cash equivalents approximate fair value because of their short maturities.

**Investment Securities**
The fair values of investment securities are measured at the quoted market price of the stock exchange for equity instruments. The information of the fair value for the investment securities by classification is included in Note 3.

**Receivables and Payables**
The carrying values of receivables and payables approximate fair value because of their short maturities.

**Long-Term Debt**
The fair values of long-term debt are determined by discounting the cash flows related to the debt at the Group's assumed corporate borrowing rate.

**Derivatives**
Information on the fair value for derivatives is included in Note 14.

b. Financial instruments whose fair value cannot be reliably determined

| | Carrying Amount | |
|---|---|---|
| December 31, 2010 | Millions of Yen | Thousands of U.S. Dollars |
| Investments in equity instruments that do not have a quoted market price in an active market | ¥881 | $10,811 |

**(5) Maturity Analysis for Financial Assets and Securities with Contractual Maturities**

| | Millions of Yen | | | |
|---|---|---|---|---|
| December 31, 2010 | Due in 1 Year or Less | Due after 1 Year through 5 Years | Due after 5 Years through 10 Years | Due after 10 Years |
| Cash and cash equivalents | ¥12,076 | | | |
| Receivables | 31,494 | | | |
| Total | ¥43,570 | | | |

| | Thousands of U.S. Dollars | | | |
|---|---|---|---|---|
| December 31, 2010 | Due in 1 Year or Less | Due after 1 Year through 5 Years | Due after 5 Years through 10 Years | Due after 10 Years |
| Cash and cash equivalents | $148,190 | | | |
| Receivables | 386,477 | | | |
| Total | $534,667 | | | |

Please see Note 5 for annual maturities of long-term debt and Note 12 for obligations under finance leases, respectively.

## *14. DERIVATIVES*

The Group enters into foreign exchange forward contracts to hedge foreign exchange risk associated with certain assets and liabilities denominated in foreign currencies. The Group enters into interest rate swap contracts as derivative financial instruments. Interest rate swap transactions are made in order to minimize the risk of interest rate increases on floating rate borrowing. The Group does not hold or issue derivatives for trading purposes.

Because the counterparties to these derivatives are limited to major international financial institutions, the Group does not anticipate any losses arising from credit risk.

All derivative transactions the Group enters into are approved by directors in charge. The conditions of such transactions are reported periodically to the Board of Directors.

Derivative Transactions to Which Hedge Accounting Is Applied at December 31, 2010

| | | Millions of Yen | | |
|---|---|---|---|---|
| December 31, 2010 | Hedged Item | Contract Amount | Contract Amount Due after One Year | Fair Value |
| Foreign currency forward contracts — Selling: | | | | |
| U.S.$ | Receivables | ¥354 | | |
| EUR | Receivables | 176 | | |

| | | Thousands of U.S. Dollars | | |
|---|---|---|---|---|
| December 31, 2010 | Hedged Item | Contract Amount | Contract Amount Due after One Year | Fair Value |
| Foreign currency forward contracts — Selling: | | | | |
| U.S.$ | Receivables | $4,344 | | |
| EUR | Receivables | 2,160 | | |

The above forward exchange contracted amounts which qualify for hedge accounting and are assigned to associated receivables are not remeasured at market value. In addition, the fair value of such forward exchange contracted amounts in Note 13 is included in that of hedged items (i.e. receivables).

| December 31, 2010 | Hedged Item | Millions of Yen Contract Amount | Contract Amount Due after One Year | Fair Value |
|---|---|---|---|---|
| Interest rate swaps (fixed rate payment, floating rate receipt) | Long-term debt | **¥9,500** | **¥9,500** | |

| December 31, 2010 | Hedged Item | Thousands of U.S. Dollars Contract Amount | Contract Amount Due after One Year | Fair Value |
|---|---|---|---|---|
| Interest rate swaps (fixed rate payment, floating rate receipt) | Long-term debt | **$116,579** | **$116,579** | |

The above 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 is recognized and included in interest expense or income. In addition, the fair value of such interest rate swaps in Note 13 is included in that of the hedged items (i.e. long-term debt).

## 15. CONTINGENT LIABILITIES

At December 31, 2010, the Group guaranteed borrowings of affiliated companies in the amount of ¥329 million ($4,037 thousand).

## 16. NET INCOME PER SHARE

Reconciliation of the differences between basic and diluted net income per share ("EPS") for the years ended December 31, 2010 and 2009 is as follows:

| | Millions of Yen | Thousands of Shares | Yen | U.S. Dollars |
|---|---|---|---|---|
| Year Ended December 31, 2010 | Net Income | Weighted-Average Shares | EPS | |
| Basic EPS — Net income available to common shareholders | **¥5,631** | **216,164** | **¥26.05** | **$0.32** |
| Year Ended December 31, 2009 | | | | |
| Basic EPS — Net income available to common shareholders | ¥2,674 | 217,780 | ¥12.28 | |

Diluted EPS is not disclosed because it is anti-dilutive.

## 17. SUBSEQUENT EVENTS

**a. Earnings Distribution**

The following appropriations of retained earnings at December 31, 2010 were approved at the Company's shareholders meeting held on March 25, 2011:

| | Millions of Yen | Thousands of U.S. Dollars |
|---|---|---|
| Year-end cash dividends, ¥4.00 ($0.04) per share | ¥854 | $10,480 |

**b. Loss of the Earthquake**

On March 11, 2011, there was an earthquake in the northeastern area of Japan. One of our plants in Ishinomaki city, Miyagi prefecture and a plant of our subsidiaries, Tokai Konetsu Kogyo Co., Ltd., in Shibata-cho, Miyagi prefecture were hit by it. The book value of the main assets at the plant in Ishinomaki is below:

| | Millions of Yen | Thousands of U.S. Dollars |
|---|---|---|
| | **2010** | **2010** |
| Buildings and structures | **¥1,008** | **$12,370** |
| Machinery and equipment | **859** | **10,541** |
| Inventories | **1,276** | **15,658** |
| **Total** | **¥3,143** | **$38,569** |

The above "book value" of main assets does not mean loss. It means the book value at the end of February 2011.

Both of the companies made headquarters aware of measures to get information and carry out plans to recover. However we cannot estimate losses caused by the earthquake at this point in time.

## 18. SEGMENT INFORMATION

Information about industry segments, geographical segments and sales to foreign customers of the Company and consolidated subsidiaries for the years ended December 31, 2010 and 2009 is as follows:

**(1) Industry Segments**

a. Sales and Operating Income

| | Millions of Yen | | | | |
|---|---|---|---|---|---|
| | **2010** | | | | |
| | Carbon and Graphite Products | Industrial Furnaces and Related Products | Others | Eliminations / Corporate | Consolidated |
| Sales to customers | **¥101,631** | **¥5,628** | **¥420** | | **¥107,679** |
| Intersegment sales | **284** | **96** | **579** | **¥(959)** | |
| Total sales | **101,915** | **5,724** | **999** | **(959)** | **107,679** |
| Operating expenses | **92,546** | **4,739** | **727** | **(908)** | **97,104** |
| Operating income | **¥ 9,369** | **¥ 985** | **¥272** | **¥ (51)** | **¥ 10,575** |

b. Assets, Depreciation, Impairment Losses and Capital Expenditures

| | Millions of Yen | | | | |
|---|---|---|---|---|---|
| | **2010** | | | | |
| | Carbon and Graphite Products | Industrial Furnaces and Related Products | Others | Eliminations / Corporate | Consolidated |
| Assets | **¥129,760** | **¥12,454** | **¥1,541** | **¥11,549** | **¥155,304** |
| Depreciation | **8,466** | **336** | **66** | **(15)** | **8,853** |
| Impairment losses | **441** | | | | **441** |
| Capital expenditures | **6,620** | **84** | **14** | **(8)** | **6,710** |

a. Sales and Operating Income

| | Thousands of U.S. Dollars | | | | |
|---|---|---|---|---|---|
| | 2010 | | | | |
| | Carbon and Graphite Products | Industrial Furnaces and Related Products | Others | Eliminations / Corporate | Consolidated |
| Sales to customers | **$1,247,159** | **$69,064** | **$ 5,154** | | **$1,321,377** |
| Intersegment sales | **3,485** | **1,178** | **7,105** | **$(11,768)** | |
| Total sales | **1,250,644** | **70,242** | **12,259** | **(11,768)** | **1,321,377** |
| Operating expenses | **1,135,673** | **58,155** | **8,921** | **(11,142)** | **1,191,607** |
| Operating income | **$ 114,971** | **$12,087** | **$ 3,338** | **$ (626)** | **$ 129,770** |

b. Assets, Depreciation, Impairment Losses and Capital Expenditures

| | Thousands of U.S. Dollars | | | | |
|---|---|---|---|---|---|
| | 2010 | | | | |
| | Carbon and Graphite Products | Industrial Furnaces and Related Products | Others | Eliminations / Corporate | Consolidated |
| Assets | **$1,592,343** | **$152,828** | **$18,910** | **$141,723** | **$1,905,804** |
| Depreciation | **103,890** | **4,123** | **810** | **(184)** | **108,639** |
| Impairment losses | **5,412** | | | | **5,412** |
| Capital expenditures | **81,237** | **1,031** | **172** | **(98)** | **82,342** |

a. Sales and Operating Income

| | Millions of Yen | | | | |
|---|---|---|---|---|---|
| | 2009 | | | | |
| | Carbon and Graphite Products | Industrial Furnaces and Related Products | Others | Eliminations / Corporate | Consolidated |
| Sales to customers | ¥78,425 | ¥4,406 | ¥467 | | ¥83,298 |
| Intersegment sales | 174 | 338 | 416 | ¥(928) | |
| Total sales | 78,599 | 4,744 | 883 | (928) | 83,298 |
| Operating expenses | 73,805 | 4,433 | 631 | (870) | 77,999 |
| Operating income | ¥ 4,794 | ¥ 311 | ¥252 | ¥ (58) | ¥ 5,299 |

b. Assets, Depreciation, Impairment Losses and Capital Expenditures

| | Millions of Yen | | | | |
|---|---|---|---|---|---|
| | 2009 | | | | |
| | Carbon and Graphite Products | Industrial Furnaces and Related Products | Others | Eliminations / Corporate | Consolidated |
| Assets | ¥129,817 | ¥11,088 | ¥1,925 | ¥12,092 | ¥154,922 |
| Depreciation | 9,057 | 405 | 69 | (6) | 9,525 |
| Impairment losses | 880 | | | | 880 |
| Capital expenditures | 7,901 | 212 | 19 | (66) | 8,066 |

**(2) Geographical Segments**

The geographical segments of the Company and its consolidated subsidiaries for the years ended December 31, 2010 and 2009 are summarized as follows:

| | Millions of Yen | | | | | |
|---|---|---|---|---|---|---|
| | 2010 | | | | | |
| | Japan | Europe | Asia | Others | Eliminations / Corporate | Consolidated |
| Sales to customers | **¥ 69,421** | **¥ 14,204** | **¥ 17,794** | **¥6,260** | | **¥107,679** |
| Interarea transfer | **8,417** | **492** | **1,658** | **75** | **¥(10,642)** | |
| Total sales | **77,838** | **14,696** | **19,452** | **6,335** | **(10,642)** | **107,679** |
| Operating expenses | **71,699** | **12,977** | **17,146** | **6,005** | **(10,723)** | **97,104** |
| Operating income | **¥ 6,139** | **¥ 1,719** | **¥ 2,306** | **¥ 330** | **¥ 81** | **¥ 10,575** |
| Assets | **¥112,563** | **¥12,024** | **¥18,040** | **¥4,127** | **¥ 8,550** | **¥155,304** |

| | Thousands of U.S. Dollars | | | | | |
|---|---|---|---|---|---|---|
| | 2010 | | | | | |
| | Japan | Europe | Asia | Others | Eliminations / Corporate | Consolidated |
| Sales to customers | **$ 851,896** | **$174,304** | **$218,358** | **$76,819** | | **$1,321,377** |
| Interarea transfer | **103,288** | **6,038** | **20,346** | **921** | **$(130,593)** | |
| Total sales | **955,184** | **180,342** | **238,704** | **77,740** | **(130,593)** | **1,321,377** |
| Operating expenses | **879,850** | **159,247** | **210,406** | **73,690** | **(131,586)** | **1,191,607** |
| Operating income | **$ 75,334** | **$ 21,095** | **$ 28,298** | **$ 4,050** | **$ 993** | **$ 129,770** |
| Assets | **$1,381,310** | **$147,552** | **$221,377** | **$50,644** | **$ 104,921** | **$1,905,804** |

| | Millions of Yen | | | | | |
|---|---|---|---|---|---|---|
| | 2009 | | | | | |
| | Japan | Europe | Asia | Others | Eliminations / Corporate | Consolidated |
| Sales to customers | ¥54,293 | ¥13,689 | ¥11,592 | ¥3,724 | | ¥ 83,298 |
| Interarea transfer | 5,122 | 392 | 772 | 30 | ¥(6,316) | |
| Total sales | 59,415 | 14,081 | 12,364 | 3,754 | (6,316) | 83,298 |
| Operating expenses | 57,089 | 11,797 | 11,935 | 3,542 | (6,364) | 77,999 |
| Operating income | ¥ 2,326 | ¥ 2,284 | ¥ 429 | ¥ 212 | ¥ 48 | ¥ 5,299 |
| Assets | ¥112,751 | ¥14,149 | ¥16,784 | ¥3,408 | ¥ 7,830 | ¥154,922 |

### (3) Sales to Foreign Customers

| | Millions of Yen | | | |
|---|---|---|---|---|
| | 2010 | | | |
| | Asia | Europe | Others | Total |
| Overseas sales | **¥31,498** | **¥13,561** | **¥9,234** | **¥ 54,293** |
| Net sales | | | | **107,679** |
| Ratio of overseas sales to net sales | **29.2%** | **12.6%** | **8.6%** | **50.4%** |

| | Thousands of U.S. Dollars | | | |
|---|---|---|---|---|
| | 2010 | | | |
| | Asia | Europe | Others | Total |
| Overseas sales | **$386,526** | **$166,413** | **$113,315** | **$ 666,254** |
| Net sales | | | | **1,321,377** |

| | Millions of Yen | | | |
|---|---|---|---|---|
| | 2009 | | | |
| | Asia | Europe | Others | Total |
| Overseas sales | ¥21,053 | ¥12,459 | ¥6,862 | ¥40,374 |
| Net sales | | | | 83,298 |
| Ratio of overseas sales to net sales | 25.3% | 15.0% | 8.2% | 48.5% |

Note: The countries included in each segment are as follows:
(1)Asia: Korea, China, Thailand, Indonesia, etc.
(2)Europe: Germany, United Kingdom, Italy, Sweden, etc.
(3)Others: North and South America, Middle East and Central and Western Asia, Oceania, etc.

Deloitte.

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## INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
TOKAI CARBON Co., Ltd.:

We have audited the accompanying consolidated balance sheets of TOKAI CARBON Co., Ltd. (the "Company") and consolidated subsidiaries as of December 31, 2010 and 2009, and the related consolidated statements of income, changes in equity, and cash flows for the years then ended, all expressed in Japanese yen. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Japan. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of TOKAI CARBON Co., Ltd. and consolidated subsidiaries as of December 31, 2010 and 2009, and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in Japan.

Our audits 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 1. Such U.S. dollar amounts are presented solely for the convenience of readers outside Japan.

Deloitte Touche Tohmatsu LLC

March 25, 2011

Member of
**Deloitte Touche Tohmatsu Limited**

# Board of Directors, Executive Officers and Corporate Auditors (as of March 25, 2011)

## Board of Directors

| | |
|---|---|
| President and CEO | Yoshinari Kudo |
| Senior Managing Executive Officer | Kiyonari Nakai<br>Nobuyuki Murofushi<br>Hajime Nagasaka |
| Managing Executive Officer | Hiroshi Hirama<br>Naoshi Takahashi |
| Executive Officer | Masanao Hosoya<br>Hideo Toko |
| External Director | Yoshio Kumakura |

## Executive Officers

Yuji Serizawa
Itsuro Imazu
Takekuni Kawaguchi
Eiichi Nishii
Jinichi Suzuki
Yoshikazu Matsuyama
Makoto Itoi

## Corporate Auditors

Tsunehisa Samukawa
Masahiro Kusaba*
Ryuichi Sato*
Katsuhiko Namba

*External Auditor

# Corporate Data (as of December 31, 2010)

| | |
|---|---|
| **Company Name** | TOKAI CARBON CO., LTD. |
| **Established** | April 8, 1918 |
| **Paid-in Capital** | ¥20,436 million ($221,889,000) |
| **Head Office** | Aoyama Bldg.2-3, Kita-Aoyama 1-Chome, Minato-ku, Tokyo 107-8636, Japan<br>TEL: +81-3-3746-5100<br>FAX: +81-3-3405-7205<br>Web site: http://www.tokaicarbon.co.jp/ |
| **Number of Employees** | 1,796 (as a consolidated basis) |
| **Branch Offices** | Osaka Branch (Osaka)<br>Nagoya Branch (Aichi)<br>Fukuoka Branch (Fukuoka) |
| **Laboratories** | Fuji Research Laboratory (Shizuoka)<br>Chita Laboratory (Aichi)<br>Hofu Laboratory (Yamaguchi)<br>Tanoura Laboratory (Kumamoto) |
| **Industrial Complexes** | Shonan Industrial Complex (Kanagawa)<br>Chigasaki Plant (Kanagawa)<br>Chigasaki Second Plant (Kanagawa) |
| **Plants** | Ishinomaki Plant (Miyagi)<br>Chita Plant (Aichi)<br>Shiga Plant (Shiga)<br>Hofu Plant (Yamaguchi)<br>Kyusyu Wakamatsu Plant (Fukuoka)<br>Tanoura Plant (Kumamoto) |
| **Representative Office** | Singapore Representative Office |

### Group Companies and Affiliates

#### EUROPE

**United Kingdom**
Consolidated Subsidiaries
- Tokai Carbon Europe Ltd.
- Tokai Carbon UK Ltd.

**Germany**
Consolidated Subsidiaries
- Tokai Erftcarbon GmbH
- Tokai Carbon Europe GmbH
- Tokai Carbon Deutschland GmbH
- Carbon-Mechanik GmbH

**Italy**
Consolidated Subsidiary
- Tokai Carbon Italia S.R.L.

**Sweden**
Consolidated Subsidiary
- Svensk Special grafit AB

#### NORTH AMERICA

**U.S.A.**
Consolidated Subsidiaries
- Tokai Carbon U.S.A., Inc.
- Tokai Carbon Electrode Sales Inc.
- Tokai Carbon Electrode Sales LLC.

Affiliate Accounted for by Equity Method
- MWI, Inc.

#### ASIA

**Japan**
Consolidated Subsidiaries
- Tokai Konetsu Kogyo Co., Ltd.
- Tokai Material Co., Ltd.
- Tokai Fine Carbon Machining Co., Ltd.
- Oriental Sangyo Co., Ltd.
- Tokai Unyu Co., Ltd.
- Tokai Noshiro Seiko Co., Ltd.
- Erema Sangyo Co., Ltd.*
- Mitomo Brake Co., Ltd.
- Daiya Tsusho Co., Ltd.

Affiliate Accounted for by Equity Method
- Heisei Ceramics Co., Ltd.

**China**
Consolidated Subsidiaries
- Tokai Carbon (Tianjin) Co., Ltd.
- Tokai Carbon (Shanghai) Co., Ltd.
- Shanghai Tokai Konetsu Co., Ltd.

Affiliates Accounted for by Equity Method
- SGL Tokai Carbon Ltd.Shanghai
- Dalian Tokai-Jinqi-Fuji Carbon Co.,Ltd.

**Korea**
Affiliate Accounted for by Equity Method
- Tokai Carbon Korea Co., Ltd.

**Thailand**
Consolidated Subsidiary
- Thai Tokai Carbon Product Co., Ltd.

**Singapore**
Affiliates Accounted for by Equity Method
- SGL Tokai Process Technology Pte. Ltd.

*Erema Sangyo Co., Ltd. changed its corporate name to Tokai Konetsu Engineering Co., Ltd. effective January 1, 2011

● Carbon and Graphite Products ● Industrial Furnaces and Related Products ● Other

# Investor Information (as of December 31, 2010)

| | |
|---|---|
| **Fiscal year end** | December 31 |
| **General Meeting of Shareholders** | March |
| **Common Stock** | Authorized Shares: 598,764,000 shares<br>Outstanding Shares: 224,943,104 shares |
| **Number of shareholders** | 21,072 |

**Major shareholders**

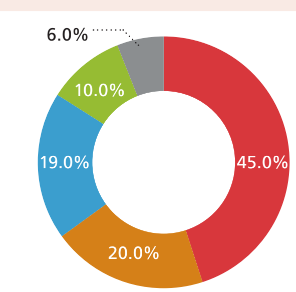
| Shareholders | Number of shares held |
|---|---|
| The Master Trust Bank of Japan, Ltd. (Trust Account) | 18,223,000 |
| Japan Trustee Services Bank, Ltd. (Trust Account) | 17,060,000 |
| Bank of Tokyo-Mitsubishi UFJ | 7,958,000 |
| Mitsubishi UFJ Trust and Banking Corp. | 6,988,000 |
| The Nomura Trust and Banking Co., Ltd. (Trust Account) | 6,149,000 |
| The Master Trust Bank of Japan, Ltd. (Mitsubishi Chemical Corp. Retirement Benefit Trust Account) | 5,900,000 |
| Mitsubishi Corp. | 5,844,000 |
| Tokyo Marine & Nichido Fire Insurance Co., Ltd. | 4,880,000 |
| JP Morgan Securities Japan Co., Ltd. | 4,103,000 |
| The Chase Manhattan Bank 385036 | 3,473,000 |

| | |
|---|---|
| **Stock Exchange Listing** | First Section of the Tokyo Stock Exchange |
| **Securities code number** | 5301 |
| **Transfer agent** | Mitsubishi UFJ Trust and Banking Corp.<br>Head Office: 4-5 Marunouchi 1- Chome, Chiyoda-ku, Tokyo, Japan |

**Ownership and Distribution of Shares**

| | |
|---|---|
| Japanese Financial Institutions | 95,561,000 |
| Japanese Individuals and Others | 42,409,000 |
| Foreign Investors | 40,517,000 |
| Other Japanese companies | 20,861,000 |
| Japanese Securities Companies | 11,842,000 |
| Total | 211,190,000 |

Notes: 1. Stocks less than 1,000 are rounded down.
2. "Others" contains 11,369,000 treasury stocks.



*Leading the Way into the Future >>*

**TOKAI CARBON CO., LTD.**

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