

NOTES TO NON-CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED MARCH 31, 2001 AND 2000

1 Basis of Presenting Non-Consolidated Financial Statements

Kawasaki Steel Corporation (the "Company") maintains its accounts and records in accordance with the provisions set forth in the Commercial Code of Japan (the "Code") and the Securities and Exchange Law and in conformity with accounting principles and practices generally accepted in Japan, which may differ in some material respects from accounting principles and practices generally accepted in countries and jurisdictions other than Japan.

The notes to the non-consolidated financial statements include information which is not required under accounting principles generally accepted in Japan but is presented herein as additional information.

The translation of the Japanese yen amounts into U.S. dollars are included solely for the convenience of the reader, using the approximate exchange rate at March 31, 2001, which was ¥123.90 to US\$1.00. These convenience translations should not be construed as representations that the Japanese yen amounts have been, could have been, or could in the future be, converted into U.S. dollars at this or any other rate of exchange.

2 Summary of Significant Accounting Policies

(a) Translation of Foreign Currencies

Revenues and expenses are translated at the rates of exchange prevailing when transactions are made. In 2001, the Company adopted the revised Accounting Standards for Foreign Currency Transactions which was issued by the Business Accounting Deliberation Council. Under the new method, all monetary assets and liabilities denominated in foreign currencies are translated into yen at the rate of exchange in effect at the balance sheet date. As a result of this change, ordinary profit increased by ¥363 million (\$2,936 thousand) and loss before income tax decreased by the same amount.

(b) Short-term Investments and Investments in Securities

Through March 31, 2000, marketable securities included in short-term investments and investments in securities were stated at cost. Other investments were carried at cost. The cost was determined by the moving average method.

Effective April 1, 2000, the Company adopted the Accounting Standards for Financial Instruments which was issued by the Business Accounting Deliberation Council. In accordance with the new standards, securities are classified into four categories: trading securities, held-to-maturity debt securities, equity investments in associates, and other securities.

Other investments are carried at cost. The cost is determined by the moving average method.

(Trading Securities)

The Company has no trading securities.

(Held-to-maturity debt securities and other securities)

Management determines the appropriate classification of debt securities at the time of purchase and reevaluates the classification as of each balance sheet date. Debt securities are classified as held-to-maturity when the Company has the positive intent and ability to hold the securities to maturity. Held-to-maturity debt securities are stated at amortized cost adjusted for the amortization of premiums and the accretion of discounts to maturity.

Marketable equity securities and debt securities not classified as held-to-maturity are classified as other securities. Other securities are carried at fair value with the unrealized gains and losses, net of tax, reported in a separate component of shareholders' equity. Under the Code, unrealized holding gains on securities, net of related taxes is not available for distribution as dividends and bonuses to directors and corporate auditors. The amortized cost of debt securities in this category is adjusted for the amortization of premiums and the accretion of discounts to maturity. Realized gains and losses and declines in value judged to be other than temporary on other securities are charged to income.

(c) Inventories

Inventories are mainly carried at cost as determined by the last-in, first-out method, except for inventories of the engineering business, which are valued by the individual identification method.

(d) Property, Plant and Equipment

Property, plant and equipment are stated at cost. Depreciation is mainly computed at rates based on the estimated useful lives of assets on the declining-balance method.

The principal estimated useful lives are as follows:

Buildings and structures 14 to 50 years

Machinery and equipment 5 to 15 years

The cost of maintenance, repairs and minor renewals is charged to expenses in the year incurred; major renewals and betterments are capitalized.

When assets are sold or otherwise disposed of, the profits or losses thereon, computed on the basis of the difference between depreciated cost and proceeds, are credited or charged to income in the year of disposal, and cost and accumulated depreciation are removed from the respective accounts.

(e) Accrued Severance Indemnities

Through March 31, 2000, accrued severance indemnities were provided for the present value of the amount that would be required if all eligible employees voluntarily retired on the balance sheet date.

Effective April 1, 2000, the Company adopted the Accounting Standards for Retirement Benefits which was issued by the Business Accounting Deliberation Council. In accordance with the new standards, accrued severance indemnities are provided based on the amount of projected benefit obligation reduced by pension plan assets at fair value at the end of the annual period. The translation obligation at the date of adoption, ¥36,165 million (\$291,892 thousand), is amortized in 5 years. As a result of this change, ordinary profit increased by ¥3,365 million (\$27,161 thousand) and loss before income tax decreased by ¥2,077 million (\$16,770 thousand).

(f) Leases

In Japan, finance leases other than those that are deemed to transfer the ownership of the leased assets to lessees are accounted for by a method similar to that applicable to ordinary operating leases.

(g) Research and Development and Computer Software

Research and development expenditure is charged to income when incurred.

Expenditure related to computer software developing for internal use is charged to income when incurred, except if it contributes to generation of income or to future cost saving. Such expenditure is capitalized as an asset, is amortized by the straight-line method over its estimated useful life, which is in the range of 5 years.

(h) Income Taxes

The Company recognizes deferred income taxes arising from temporary differences between the tax basis of assets and liabilities and their reported amounts in the financial statements.

(i) Per Share Information

The computation of basic net income per share is based on the weighted average number of shares of common stock outstanding during each period. The average number of shares used in the computation was 3,191,956 thousand and 3,251,556 thousand for the years ended March 31 2001 and 2000, respectively.

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

3 Contingencies

At March 31, 2001 and 2000, the Company was contingently liable as follows:

	Millions of yen		Thousands of U.S. dollars
	2001	2000	2001
Guarantees of loans	¥ 5,580	¥ 5,985	\$ 45,041
Similar-to-guarantee acts	¥ 290,220	¥ 333,783	\$ 2,342,377

4 Leases

The Company leases certain building and structures, machinery and equipment, office space and other assets. Total lease payments under these leases were ¥6,195 million (\$50,002 thousand) and ¥6,880 million for the years ended March 31, 2001 and 2000, respectively.

Pro forma information on leased property such as acquisition costs, accumulated depreciation and future minimum lease payments under finance lease that do not transfer ownership of the leased property to the lessee on an “as if capitalized” basis for the years ended March 31, 2001 and 2000 was as follows:

	Millions of yen		
	2001		
	Machinery and equipment	Other	Total
Acquisition costs	¥ 41,728	¥ 4,105	¥ 45,833
Accumulated depreciation	26,732	2,679	29,411
Net leased property	<u>¥ 14,996</u>	<u>¥ 1,425</u>	<u>¥ 16,422</u>
	2000		
	Machinery and equipment	Other	Total
Acquisition costs	¥ 47,737	¥ 4,328	¥ 52,065
Accumulated depreciation	29,124	2,612	31,737
Net leased property	<u>¥ 18,612</u>	<u>¥ 1,715</u>	<u>¥ 20,327</u>
	Thousands of U.S. dollars		
	2001		
	Machinery and equipment	Other	Total
Acquisition costs	\$ 336,790	\$ 33,136	\$ 369,926
Accumulated depreciation	215,755	21,629	237,384
Net leased property	<u>\$ 121,035</u>	<u>\$ 11,507</u>	<u>\$ 132,542</u>

Future minimum lease payments under finance leases as of March 31, 2001 and 2000 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2001	2000	2001
Due within one year	¥ 5,261	¥ 5,998	\$ 42,465
Due after one year	11,160	14,329	90,077
Total	<u>¥ 16,422</u>	<u>¥ 20,327</u>	<u>\$ 132,542</u>

The acquisition costs and future minimum lease payments under finance leases include the imputed interest expense portion.

Depreciation expenses, which are not reflected in the accompanying non-consolidated statements of income, computed by the straight-line method, were ¥6,195 million (\$50,002 thousand) and ¥6,880 million for the years ended March 31, 2001 and 2000, respectively.

5 Income taxes

The Company is subject to several taxes based on income, which in the aggregate resulted in statutory tax rates of approximately 41.0% for the years ended March 31, 2001 and 2000.

The effective rate for the two years ended March 31, 2001 and 2000 differs from the statutory tax rate for the following reasons:

	<u>2001</u>		<u>2000</u>	
Statutory tax rate	41.0	%	41.0	%
Adjustments of deferred tax assets by verifying realizability	-		(15.1)	
Expenses not deductible for income tax purposes	(2.3)		(2.9)	
Other	<u>0.2</u>		<u>0.1</u>	
Effective tax rate	<u>38.9</u>	%	<u>23.1</u>	%

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets at March 31, 2001 and 2000 are presented below:

	<u>Millions of yen</u>		<u>Thousands of U.S. dollars</u>
	<u>2001</u>	<u>2000</u>	<u>2001</u>
Deferred tax assets:			
Operating loss carry-forwards	¥ 25,896	¥ 33,955	\$ 209,014
Write-down of investments in securities	19,105	-	154,202
Accrued severance indemnities	15,506	16,339	125,151
Write-down of investments in and advances to associates	13,012	9,486	105,028
Loss on disposal of tangible fixed assets •••	4,031	2,100	32,539
Accrued expenses	2,636	1,909	21,281
Others	<u>7,976</u>	<u>9,024</u>	<u>64,376</u>
Total gross deferred tax assets	88,165	72,816	711,590
Deferred tax liabilities:			
Unrealized holding gains on securities	(23,338)	-	(188,368)
Reserve for advanced depreciation of property	(14,706)	(17,978)	(118,696)
Others	<u>(2,319)</u>	<u>(1,335)</u>	<u>(18,718)</u>
Total gross deferred tax liabilities •	(40,364)	(19,314)	(325,782)
Net deferred tax assets	<u>¥ 47,800</u>	<u>¥ 53,502</u>	<u>\$ 385,800</u>

In assessing the realizability of deferred tax assets, the management of the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is entirely dependent upon the generation of future taxable income in specific tax jurisdictions during the periods in which those temporary differences become deductible. Although realization is not assured, management considered the projected future taxable income in making this assessment. Based on these factors, management believes it is more likely than not the Company will realize the benefits of these deductible differences.

6 Special Profit (Loss)

In March 31, 2001 and 2000, special profit (loss) consisted of the following:

	Millions of yen		Thousand of U.S. dollars
	2001	2000	2001
Profit on sales of property, plant and equipment	¥ -	¥ 1,944	\$ -
Profit on sales of marketable securities	-	21,639	-
Profit on sales of investments in and advances to associates	1,644	-	13,273
Profit on sales of investments in securities	6,069	-	48,985
Loss on disposal of tangible fixed assets	(7,707)	-	(62,207)
Write-down of marketable securities	-	(1,432)	-
Write-down of investments in securities	(51,105)	(1,206)	(412,475)
Write-down of inventories /real estate for sale	-	(2,290)	-
Write-down of investments in and advances to associates	(9,079)	-	(73,279)
Allowance for doubtful receivables in and advances to associates	(6,616)	-	(53,399)
Loss on disposal of affiliates' businesses	-	(5,865)	-
Loss on restructuring businesses	(8,274)	-	(66,782)
Expenses on special retirement payments	(5,877)	(16,098)	(47,435)
Cost of past service portion	-	(5,129)	-
Amortization of transition obligation on accrued severance indemnities	(7,233)	-	(58,379)
	<u>¥ (88,179)</u>	<u>¥ (8,438)</u>	<u>\$ (711,698)</u>

7 Subsequent Event

In April 2001, the Company and NKK Corporation (“ NKK ”) reached a basic agreement to consolidate their entire operations.

(1) Basic structure and schedule

In the first stage, the Company and NKK plan to jointly establish a Holding Company (“Holding”) and become 100%-owned subsidiaries of Holding by the “stock-for-stock exchange” method by October 2002.

In the second stage, full integration will be completed under the Holding to form new entities based on each segment ,by April 2003.

(2)The company name, location of the head office, representative board members of Holding and other basic issues will be decided through discussion.

(3) Share exchange ratio

The “stock-for-stock” exchange ratio to form Holding will be determined by the Company and NKK, taking into consideration “fairness opinions” from independent professional institutions.