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Delivering Value

GRACE

1995 Annual Report

FINANCIAL SUMMARY

Dollars in millions, except per share amounts	1995	1994[1]	1993[1]
Operating Results			
Sales and revenues	**$3,665.5**	$3,218.2	$2,895.5
Income from continuing operations before special items[2]	**194.7**	157.6	119.1
(Loss)/income from continuing operations	**(196.6)**	(41.4)	19.1
(Loss)/income from discontinued operations[3]	**(129.3)**	124.7	6.9
Net (loss)/income	**(325.9)**	83.3	26.0
Capital expenditures	**537.6**	444.6	309.6
Depreciation and amortization	**186.3**	165.0	153.5
Research and development expenses	**120.6**	106.8	111.5
Financial Position			
Total assets	**$6,297.6**	$6,230.6	$6,108.6
Total debt	**1,933.8**	1,529.7	1,706.1
Common shareholders' equity	**1,224.4**	1,497.1	1,510.2
Data Per Common Share			
Earnings from continuing operations before special items[2]	**$ 2.03**	$ 1.68	$ 1.30
(Loss)/earnings from continuing operations	**(2.05)**	(.45)	.20
Net (loss)/earnings	**(3.40)**	.88	.28
Dividends	**1.175**	1.40	1.40
Book value	**12.57**	15.91	16.16
Other Information			
Common shares outstanding – end of year *(thousands)*	**97,375**	94,083	93,465
Common shares outstanding – average *(thousands)*	**95,822**	93,936	91,461
Dividends paid on common stock	**$ 112.1**	$ 131.5	$ 127.9
Number of employees – continuing operations *(thousands)*	**21.2**	20.6	20.4

[1] Certain amounts have been reclassified to conform to the 1995 presentation.

[2] See footnote (2) to table on page 53 for reconciliation of income from continuing operations before special items to (loss)/income from continuing operations. The special items in the table have also been excluded in determining earnings per common share from continuing operations before special items.

[3] Includes income of $22.0, $124.7 and $115.1 in 1995, 1994 and 1993, respectively, from discontinued health care operations. 1995 health care results reflect special charges totaling $102.4 relating to asset impairments of $81.6, the phaseout of certain of Grace's health care research programs of $5.0, additional costs associated with Grace's long-term incentive programs applicable to NMC of $4.3, changes in accounting estimates of $1.8 and other items totaling $6.6.

About the Company

W. R. Grace & Co. is a global leader in packaging and specialty chemicals markets. With 21,000 employees in 50 countries, Grace generated sales of $3.7 billion in 1995. Core businesses include packaging, catalysts and silica-based products, construction materials and container sealants. Grace's strategy for delivering value to shareholders, customers and employees is to profitably grow its core businesses on a global basis; capitalize on technical strengths and market leadership positions; build through research, capital investments and complementary strategic alliances; and continually improve operating performance.

To Our

1995 was a year of extraordinary change and accomplishment for W. R. Grace as we implemented a series of initiatives to maximize shareholder value. Specifically, we:

- Pursued the spin-off of our *National Medical Care (NMC)* unit, culminating in an agreement with Fresenius AG in February 1996.
- Pursued strategic alternatives for our *Grace Dearborn* water treatment and process chemicals business. In March 1996, we reached an agreement with Betz Laboratories, Inc. to sell *Grace Dearborn* for $632 million.
- Took aggressive steps that will lead to an enhanced capital structure.
- Implemented significant changes in corporate governance and the composition of the Board of Directors.
- Adopted an operating company management philosophy and sharpened our focus on performance improvements.

Continued Growth in Earnings Per Share
(continuing operations before special items)

Strong Operating Performance

We achieved strong operating performance in 1995. We increased sales of our continuing operations in packaging and specialty chemicals nearly 14%, to $3.7 billion, and pretax operating earnings more than 20%. Grace's operating earnings per share from continuing operations, before special charges, increased 21% to $2.03. That gives us great confidence as Grace moves forward, solely focused on these core businesses.

Sales from *NMC*, which was classified as a discontinued operation in the second quarter in anticipation of a spin-off, increased 11% to $2.1 billion.

Grace recorded a loss of $326 million for the year due to special after-tax charges of $645 million, primarily related to discontinued operations, restructuring activities, asset impairments, corporate governance and projected spending for asbestos litigation and environmental remediation. These charges reflect recent trends, as well as reassessments of future plans and forecasts. We expect the resulting reduction in shareholder equity to be more than restored this year, when we finalize the disposition of *NMC* and *Dearborn*. Once those steps are taken, Grace will be positioned for consistent, solid performance in the future.

Moving Forward to Build & Deliver Value

The Grace team is moving forward aggressively to build and deliver value through sustained earnings growth and an increased focus on improving cash flow management. Value-enhancing measures initiated in 1995 include cost management efforts, organizational restructuring and a revised senior management compensation program requiring targeted levels of stock ownership.

Consistent with Grace's goal of maximizing shareholder value, in February 1996, the Company announced an agreement with Fresenius AG to merge its worldwide dialysis products business with *NMC*, the world's largest provider of dialysis services. The new company, to be named Fresenius Medical Care, will be the largest fully integrated renal care company in the world. We are moving toward the finalization of this transaction, with completion expected by the third quarter of 1996. We are enthusiastic about the value this arrangement will bring to Grace and our shareholders. Grace will receive $2.3 billion in a tax-free cash distribution, and Grace shareholders will own 44.8% of the new company, which should be the bellwether company in the renal care industry. Grace common shareholders also will receive a distribution of one share of common stock of a restructured Grace—consisting of our packaging and specialty chemicals businesses—for each share currently held.

Proceeds from the *NMC* and *Grace Dearborn* transactions will be applied to significantly reduce our debt and to repurchase up to 20% of Grace's common stock. In anticipation of the separation of *NMC* from Grace, the Board of Directors lowered the Company's quarterly cash dividend and adopted a dividend policy of distributing approximately 20–30% of the prior year's net earnings, a level more in line with peer companies. We believe these initiatives will give us a capital structure consistent with the growth strategies of our core businesses and will provide our shareholders even greater long-term value through stock appreciation.

High Expectations for Future Performance

I have high expectations for Grace's future performance as the premier packaging and specialty chemicals company. That means we shall strive to be in the top quartile of our peers in important measures of performance—as well as remaining the supplier-of-choice to our customers. Our strategy is clear: profitably grow our core businesses on a global basis; capitalize on our underlying technical strengths and market leadership positions; build through research, capital investments and selected strategic acquisitions or alliances that complement existing businesses; and continually improve our operating performance. Successful implementation of this strategy will result in internal sales growth in the mid-teens, increasingly positive cash flows and operating margins increasing three points in 1996 and one point per year thereafter.

Our businesses are leaders in their global markets and continue to grow steadily, expanding into new markets and geographic regions. Today half of our sales are outside North America, with each of the other regions realizing above mid-teens sales growth in 1995.

To meet growing demand for our products on a global basis, we invested more than $500 million last year in capital expenditures to expand or upgrade manufacturing operations. We are targeting our research and development investments to achieve a better balance of new product development, application-driven technology and breakthrough research—all aimed at supporting our core businesses. We expect more focused investments to bring products to market faster and to develop manufacturing process technologies that will further enhance productivity and quality.

There is much opportunity to continue our growth trend, internally generated as well as through possible strategic acquisitions. As we grow, we will focus on ensuring that our growth is profitable. In 1995 we initiated programs to reduce annual costs by more than $100 million. We continue to focus on asset management—reducing working capital, improving capital productivity and enhancing cash flows. We are on the right track, and I am confident that we will be successful.

Changing the Way We Manage the Company

We have changed, and are continuing to change, the way we manage the Company. During the year, the composition of the Board changed significantly, and new corporate governance policies and practices were adopted. I want to thank those directors who are retiring, effective May 10, for their dedication and service to Grace: Dr. George C. Dacey, Edward W. Duffy, Peter S. Lynch, Robert C. Macauley and Eugene J. Sullivan, and also Gordon J. Humphrey, who retired in late 1995. I also welcome two newly appointed directors—Dr. Marye Ann Fox and Dr. Thomas A. Vanderslice.

We are now a well-focused, operating company—sharing resources, skills, people and management know-how. Creating this new environment for success is one of my primary responsibilities, as it is for our newly formed Executive and Operating Committees.

Together we are making sure we have the right business strategies, the right systems and tools, the right people in the right jobs, the right rewards and recognition, and the right organizational structure to successfully serve our customers, provide excellent results for our shareholders and afford new and challenging opportunities for our employees.

1995 was an extraordinary and successful year for Grace, due largely to the dedication of Grace employees around the world. Together, as promised, we are delivering value. Together, we are building upon the strengths of our businesses to ensure continued and consistently improving performance.

Albert J. Costello
Chairman, President and Chief Executive Officer
March 11, 1996

During 1995, CEO Al Costello visited major Grace sites and met a number of key customers. Top: Bill Ritzel, manufacturing manager, with Costello (right) at *Grace Davison's* Curtis Bay, Maryland plant. Bottom: Costello (center) with J. Gary Koenzig, president of *Grace Packaging* (left), visiting Sainsbury's, the U.K.'s largest food retailer.

Grace at a Glance

Highlights

- Grew sales 19% to $1.7 billion. Pretax operating earnings rose 20%.
- Launched $350 million global capital expansion program, including $50 million to build a plant in Seneca, South Carolina to serve fresh-cut produce market.
- Formed joint venture in China, with market potential for sausage packaging estimated at $100 million by the year 2000.
- Increased acceptance of case-ready packaging systems by retailers and consumers.
- Increased sales of *Cryovac® TBG™* (total bone guard) meat packaging in North America by 35%.
- Accelerated timetable for completion of new packaging plant in Kuantan, Malaysia—expected to open by mid-1996.
- Integrated German packaging firm acquired in 1994, solidifying position in European laminates market.
- Increased sales of *Formpac™* foam trays for retail display of fresh meat, poultry and produce by 19%.

Grace Packaging

Grace is the world's leading innovator in flexible packaging technology and products. Working in close partnership with customers, it facilitates the distribution, protection, preservation and presentation of food products in markets throughout the world. *Cryovac* bags, films and laminates have revolutionized marketing and merchandising techniques for the food industry and other markets. Grace's high-performance materials, such as *Cryovac* and *Darfresh™* packaging, incorporate sophisticatec multilayer coextrusion technology. They preserve flavor and aroma and enhance the shelf life and appearance of packaged foods, such as fresh and processed meats, poultry and cheese. They also improve the marketability of consumer packaged goods, such as housewares, hardware, toys, tapes and compact discs.

Grace Davison

Grace is the world's leading supplier of fluid cracking catalysts used to "crack" crude oil into motor fuels and other petroleum-based products. Its polyolefin catalysts are critical in the manufacture of polyethylene resins for plastic film,

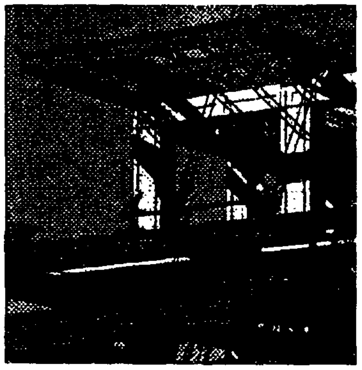
gas distribution pipe and household containers. Grace also is a leading global supplier of silica products and zeolite adsorbents. These value-added functional additives and processing aids are used in the coatings, plastics, personal care, food, pharmaceutical, building and chemical industries

Highlights

- Achieved record sales for the third straight year—increased sales 13% to $687 million. Pretax operating earnings rose 18%.
- Constructed and started up new fluid cracking catalyst facilities in Curtis Bay, Maryland and Lake Charles, Louisiana.
- Achieved sales growth of 35% in the Asia Pacific region, which represents 10% of total *Grace Davison* sales.
- Commenced construction of grassroots plant in Kuantan, Malaysia to manufacture silica products—scheduled for mid-1996 opening.

Highlights

- Increased sales to $397 million.
- Field-tested innovative shrinkage-reducing admixture to minimize concrete cracking.
- Introduced *Monokote®* *6HY* (high-yield) fireproofing, offering significant cost advantages to customers.
- Expanded market presence in Asia Pacific region, achieving sales growth of 24%.
- Named "supplier of the year" by J. L. Manta, a major fireproofing customer, for outstanding product quality and customer support during the expansion of McCormick Place convention center in Chicago, Illinois.

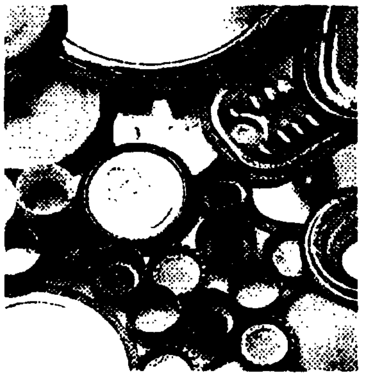


Grace Construction Products

Grace cement additives, concrete admixtures, waterproofing systems, fireproofing and masonry products are sold globally to protect some of the world's most important structures from the punishing effects of nature. Meeting the most stringent building codes and performance requirements, Grace's specialty construction materials and systems strengthen concrete, fight corrosion, prevent water damage and protect structural steel against collapse in the event of fire.

Grace Container Products

Grace container sealants and coatings ensure the integrity of more than 450 billion cans and bottles annually, making Grace the world leader in container sealing technology. Grace container sealant and coating systems protect foods and beverages from bacteria and other contaminants, extend shelf life and preserve flavor. They are used in beer, beverage, food, aerosol and composite containers. Grace specialty polymers are used in printed circuit board manufacture and component assembly in the electronics, electrical, automotive and defense industries.

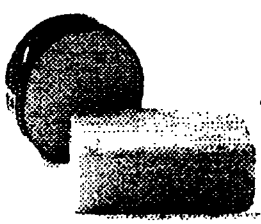


Highlights

- Increased sales 10% to $357 million. Pretax operating earnings rose 17%.
- Formed joint venture in Russia to support globalizing customers with local sourcing for high-performance can and closure sealants.
- Extended global availability of advanced, environmentally friendly sealants for ultra-high-speed application in the manufacture of beer and beverage cans.
- Gained significant brewery and consumer acceptance of *Darafresh™* oxygen-scavenging technology to preserve the flavor and freshness of beer. In 1995, an estimated 2.5 billion bottles of beer were sealed with *Darafresh* technology—more than double the number in 1994.
- Dedicated new Philippines container technical center, providing enhanced regional technical support to global customers.

Grace Packaging

GROWING AT NEARLY DOUBLE THE INDUSTRY AVERAGE



A leading global producer of flexible plastic packaging systems, Grace has helped shape, and in some cases, revolutionize the packaging industry. *Grace Packaging* continues its role as an innovator, with 60% of its current product offering introduced in just the last five years. Its *Cryovac*® bags, films and laminates extend the freshness, flavor and shelf life of fresh and processed meats, poultry, cheese, fish and produce. *Cryovac* shrink packaging also adds value and merchandising appeal to consumer and industrial goods.

Grace's leadership in the packaging industry is built on a strong combination of core competencies:

- Film processing and resin technology
- Food and packaging sciences expertise
- Relationships with supermarket chains and retail sellers throughout the world
- Total systems: technical and sales service; equipment design and installation; label design; and an extensive distribution network.

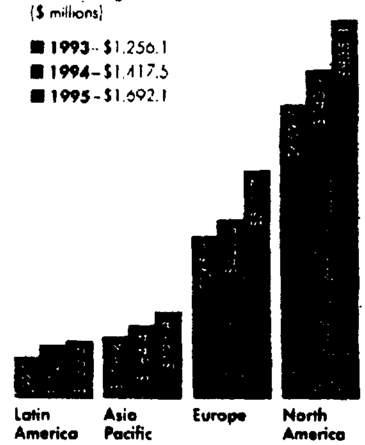
Providing unique competitive advantages, these core competencies helped *Grace Packaging* achieve sales and revenues of $1.7 billion in 1995, a 19% increase over 1994, representing the 33rd consecutive year of improved sales performance. In the last five years, Grace's plastic packaging business has grown at nearly double the industry average.

Future growth opportunities have been clearly identified to capitalize on technical innovations, new packaging applications and geographic expansion. Addressing these opportunities, the Company is making significant investments to upgrade and expand production capabilities; develop the right worldwide infrastructure; build its employee base; and provide advanced customer service and technical training to drive market innovation in all the growing regions of the world.

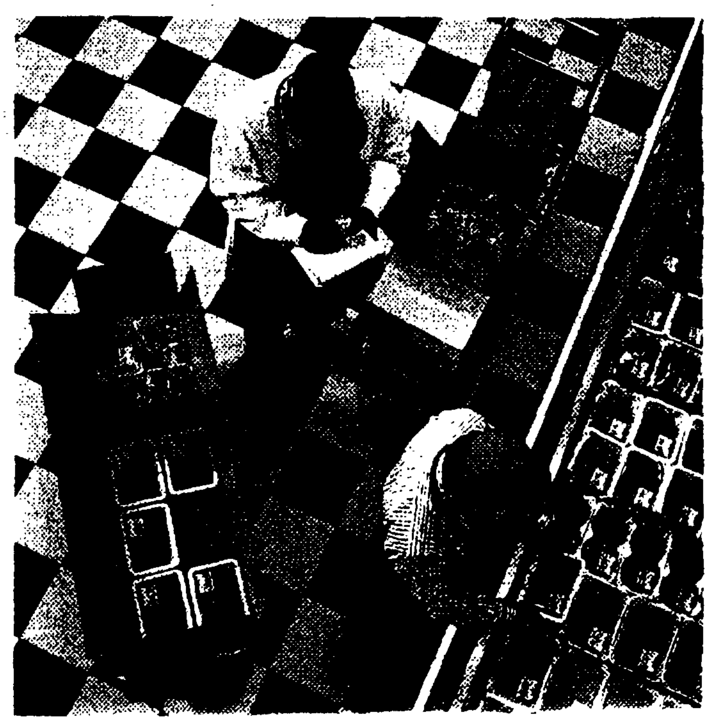
New Opportunities for Meat Producers

Grace's advanced packaging technology is improving both the quality and variety of meats available at the supermarket. *Cryovac* abuse-resistant vacuum packaging materials and productivity-enhancing equipment facilitate faster product handling for meat processors. With *Cryovac TBG*™ bags offering retailers product protection and operational efficiency for previously hard-to-handle bone-in pork, beef and veal, supermarkets can stock product without fear of spoilage and can maintain the right amount of inventory to meet demand. Retailers in North America are demanding *Cryovac* vacuum packaging for their bone-in pork at record levels, with sales of packaging for pork increasing 69% in 1995.

Outstanding Sales Growth in All Regions
($ millions)



Grace packaging systems have revolutionized the distribution of food products. The boxed beef concept, pioneered with *Cryovac* barrier bags, is still the workhorse system in leading-edge markets for large cuts of meat. Today it is gaining increased acceptance in emerging Latin American and Asia Pacific markets. An extension of this technology, *TBG* bags protect bone-in meats. *Cryovac* packaging systems now make it possible to deliver case-ready products to supermarkets. The benefits for consumers: enhanced quality and product availability.



Capitalizing on Case-Ready Advantages

On the leading edge of the next revolution in food distribution, *Grace Packaging* offers a full range of sophisticated packaging options to facilitate case-ready distribution. Case-ready products are prepared in centralized processing plants and delivered fresh to retailers, prepackaged in convenient sizes for sale to consumers. They offer retailers a major cost-savings opportunity over the traditional system of cutting and packaging in supermarket back rooms.

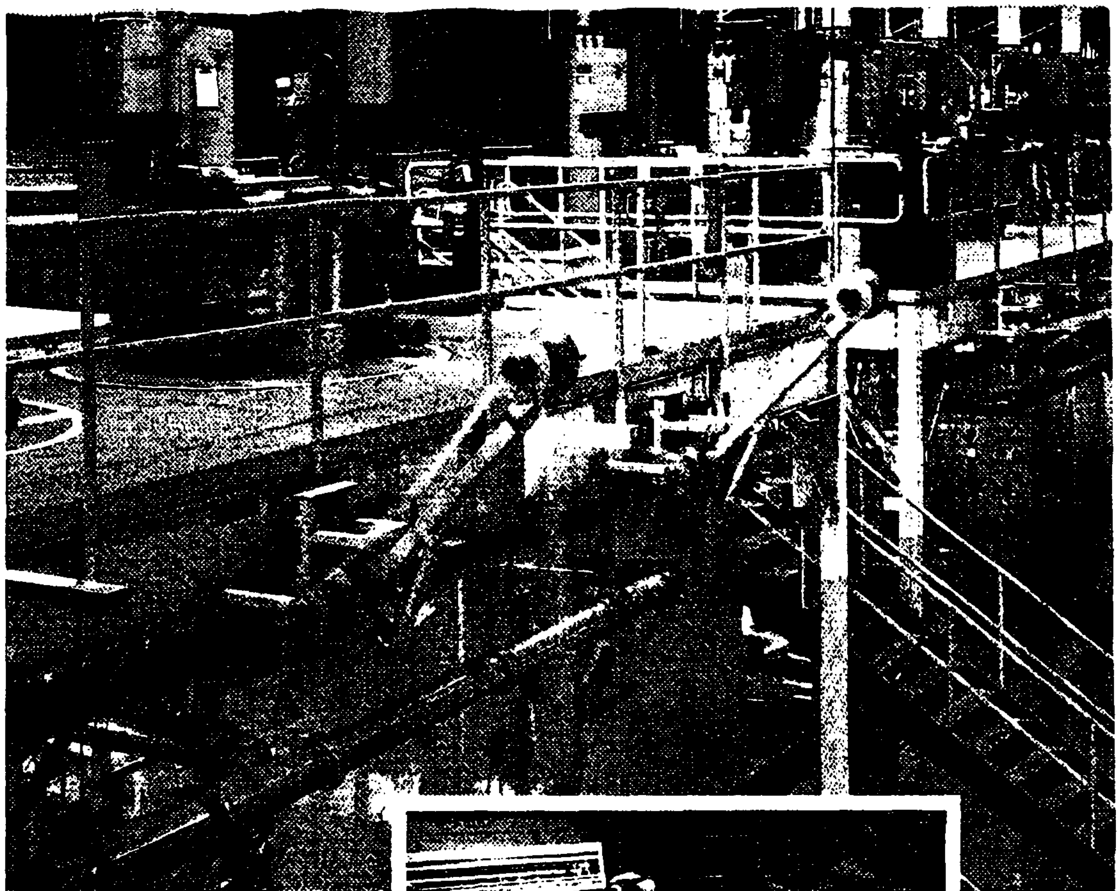
Specialty cheeses have long been packaged for consumer sale in traditional *Cryovac* bags and laminates. Today, consumer unit cheese packaging using *Cryovac BDF* film is gaining in popularity, particularly in Europe. Many poultry producers ship their products in *Cryovac* case-ready packages that allow supermarkets to display a much greater variety and spend more time on creative merchandising. Pork producers have started to market case-ready products, and the number of market tests featuring beef continues to grow. Although in its infancy, the market for case-ready meats represents a $1 billion global opportunity for Grace over the next five to ten years.

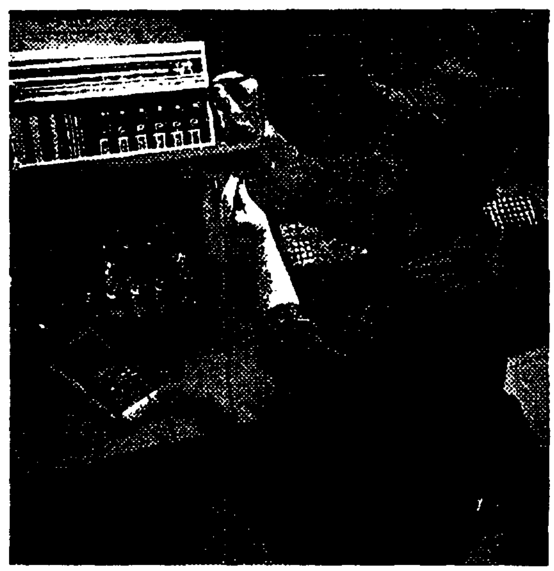
Accelerated Demand for Fresh-Cut Produce

Consumer demand for convenience and for healthier foods has produced a rapidly accelerating trend toward packaged, fresh-cut produce. Over the next five years, the North American fresh-cut produce market is expected to triple in size, with industry estimates suggesting that as much as 25% of produce will be sold fresh-cut and consumer-ready by the year 2000.

Fresh-cut vegetables are aerobic, meaning they must "breathe" oxygen to stay fresh; the amount of oxygen varies from vegetable to vegetable. Broccoli and cauliflower, for example, have higher respiration rates than carrots and potatoes. *Cryovac* packaging film can be varied to match each vegetable's natural breathing rate, significantly increasing distribution and shelf life. Longer shelf life results in less spoilage and waste for consumers, store owners and food industry managers.

Fresh-cut packaging relieves busy consumers of the time and labor involved in food preparation by providing ready-to-eat products, including salads, coleslaw, carrot sticks, broccoli florets and stir-fry vegetables. It also provides a solution to increased labor costs and limited preparation space in the hotel, restaurant and institutional food service industries.





$350 Million Earmarked for Manufacturing Expansion

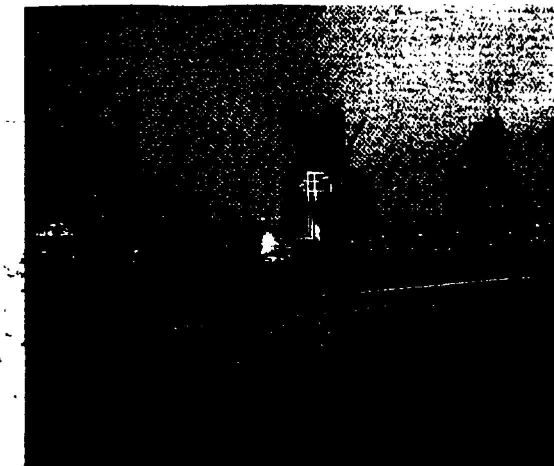
In 1995, Grace launched a worldwide, $350 million capital expansion program to increase manufacturing capacity. Making a major commitment to the produce industry, Grace is building a $50 million, 124,000 sq. ft. plant in Seneca, South Carolina. Other expansions are slated for plants in the U.S., Europe, South America, Australia, Canada and Malaysia. The expansion program includes installation of advanced production equipment—including extrusion lines, converters and state-of-the-art printing presses—to provide increased operating flexibility and efficiencies in the manufacture of bags, films and laminates.

In Simpsonville, South Carolina, new computer-controlled production lines will result in greater precision, enhanced product quality and a 30% increase in production capability. A key manufacturing site for bags, films and laminates, Simpsonville also provides graphic arts services to customers throughout North America.

New Ventures in Emerging Markets

In November 1995, Grace formed a strategic packaging joint venture in Gaoming, China. It will manufacture shrink films for packaging chub sausage, which is a cooked, nonrefrigerated, pork sausage staple popular throughout China. With market potential for this product estimated at $100 million by the year 2000, the joint venture provides an excellent springboard for the successful introduction of advanced packaging products and technologies into China.

In the past two years, *Grace Packaging* has established joint ventures in Malaysia and Russia. Each of these initiatives should help ensure that the latest *Cryovac* packaging products and advanced manufacturing processes are readily available as customers grow their businesses in emerging markets.



With technologies based on alumina and silica, *Grace Davison* formulates an array of petroleum refinery catalysts, polyolefin catalysts and silica products. Using sophisticated technologies, *Grace Davison* provides a constant flow of advanced catalysts, contributing to the global growth of state-of-the-art petroleum refining. A new silicas plant in Kuantan, Malaysia—to open in mid-1996—will supply growing Asia Pacific demand, particularly in the plastics and coatings markets.

Grace Davison

THIRD STRAIGHT YEAR OF RECORD SALES

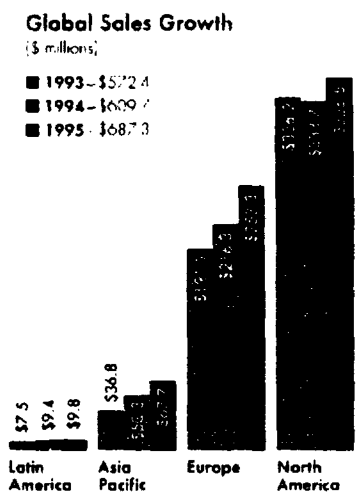
Committed to customer service, product innovation and low-cost, high-quality manufacturing, *Grace Davison* is the leading global supplier of fluid cracking catalysts (FCCs) to produce gasoline and other fuels from crude oil. It is the leading supplier of silica-supported polyolefin catalysts and catalytic supports used in the manufacture of polyethylene resins for plastic film, gas distribution pipe and household containers. *Grace Davison* also is a world leader in silica technology and materials used to enhance a variety of products, including coatings, pharmaceuticals, foods, plastics and personal care products.

Leadership through Customer Responsiveness

Serving the increasingly complex petroleum refining industry, *Grace Davison* maintains its leadership position by listening to customers and responding with technologically enhanced products and services that meet their rapidly evolving needs. In fact, 75% of Grace's FCC products today reflect technology that is less than three years old.

Grace Davison introduced a high performance fluid cracking catalyst—*RAMCAT*™—in 1995 to serve the growing residuum oil processing segment. The immediate success of two other newly introduced, leading-edge FCCs—*Spectra*™ and *Ultima*™—led to a significant increase in European sales. To better manage R&D expenditures and speed commercialization of new catalysts, *Grace Davison* has formed alliances with some of the world's leading oil and petrochemical companies.

Also in 1995, Grace introduced new silica-supported polyolefin catalysts for modified polymer products. This is a major effort to satisfy a growing demand for catalysts to synthesize unique plastic resins.



New Silicas & Adsorbents Expand Growth Horizon

Capitalizing on the broadening application of silica products Grace has increased sales and market penetration through the introduction of a series of new products. "Smart" desiccants and odor scavengers improve quality and extend the shelf life of packaged materials. New *SYLOID*® flatting agents are used in environmentally friendly, water based paints and ink jet paper coatings; and new *SYLOBLOC*® anti-blocking and slip aids improve handling and clarity of plastic films. *PHONOSORB MTX*™ is a "hot melt" desiccant mix for automated production of insulating glass.

Growth through Geographic Expansion

Grace Davison continues its global expansion with significant gains recorded in Asia Pacific and Europe in 1995. Asia Pacific will account for 50% of Grace's volume growth for cracking catalysts over the next five years. Overall FCC volume in the region potentially will double by the year 2000. Demand for silica products in the region prompted Grace to construct a plant in Kuantan, Malaysia, with a startup of mid-1996. To meet growing worldwide demand for molecular sieve products, Grace enhanced operations in Worms, Germany and Curtis Bay, Maryland. It also expanded FCC operations in Curtis Bay

Grace Construction Products

STRENGTHENING & PROTECTING THE WORLD'S STRUCTURES

Grace cement additives, concrete admixtures, waterproofing systems, fireproofing and masonry products strengthen and protect the world's most important structures. The market leader in North America and Southeast Asia and a growing force in other regions, *Grace Construction Products* offers customers value-building technology with superior technical support in both commercial and residential construction.

Growth through Value-Added Product Developments

Meeting increased demand for improved structural integrity with lower long-term maintenance costs, Grace leverages its technical expertise and market knowledge to develop value-added product solutions for the construction industry. Significantly improved from earlier technology, *CBA*™ cement additives enhance cement flowability and performance while helping customers lower production costs. An environmentally friendly, liquid waterproofing membrane to complement *Bituthene*® sheet membrane is in field testing. A new *Monokote*® *6HY* (high-yield) fireproofing material provides customers with significant product application cost advantages.

Growth through Geographic Expansion

1995 was a strong growth year for developing economies in the Asia Pacific region. Leveraging an expanded manufacturing, sales and support base, *Grace Construction Products* capitalized on infrastructure and commercial development in the region, achieving a 24% increase in sales relative to 1994. All construction product lines contributed to the growth.

Grace waterproofing products were specified in the construction of Hong Kong's new Chek Lap Kok Airport. Grace concrete admixtures were chosen for the Port of Singapore Authority expansion and several construction projects in northern China. Grace fireproofing materials are protecting the new Lotte Tower and Koryo Securities Building in Seoul, Korea.

The Company secured its first sale of *Bituthene*® *Pre-Prufe* waterproofing at the Crossness Beckton sewage sludge incineration plant in the U.K., the largest such project ever built in Europe. Working with the Central European Cement Association, the Company obtained significant sales of cement additives from new customers in Poland, the Czech Republic and Hungary.

Grace also recorded its first fireproofing sale in Latin America, where *Monokote 6* was specified to protect structural steel in the new Downtown Tower in Buenos Aires, Argentina.

Focused on Outstanding Quality & Service

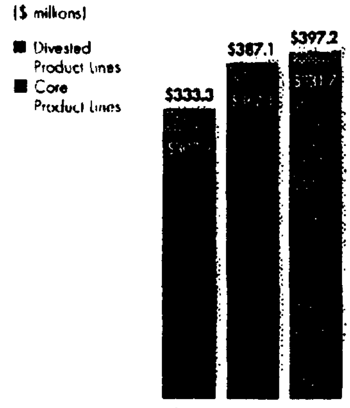
Grace's focus on high-quality technical service and support, backed by innovative technology, applications know-how and market knowledge, offers customers a strong competitive advantage. Noting that Grace was the supplier most instrumental and effective in contributing to its success, customer J. L. Manta named Grace its "supplier of the year" for outstanding product quality and customer support. J. L. Manta ordered 250,000 bags of *Monokote* fireproofing for the one million sq. ft. expansion of McCormick Place convention center in Chicago, Illinois.

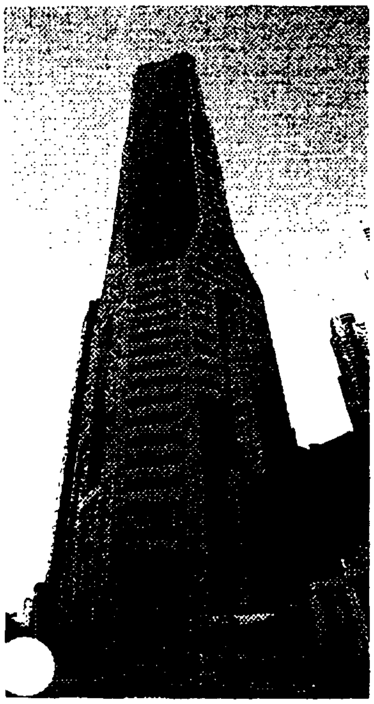
Profit Improvement through Increased Productivity

Grace Construction Products continues to improve resource productivity, using the tools of total quality management and business process engineering. Nearly 70% of its workforce has completed training in quality management techniques. Other major initiatives include a lower-cost overhead structure, facility consolidations, product cost reductions, and the divestment of underperforming noncore product lines.

Core Product Lines Lead Sales Growth

($ millions)





Republic Tower in Singapore is one of many construction projects around the world where Grace's technology is meeting critical performance standards. Addressing a long-standing problem for structural engineers, Grace's innovative shrinkage-reducing admixture—successfully field-tested in the 110° F heat of the Arizona desert—minimizes concrete cracking. *Grace Ice & Water Shield®* membrane roofing underlayment protects against water infiltration caused by ice dams and wind-driven rain.

Innovative technology and superior technical service in support of customers make Grace the world leader in container sealing technology. Grace's newest container technical center in Manila provides advanced technical support and field service assistance to local and globalizing customers as they grow their businesses in the Asia Pacific region. In 1995, an estimated 2.5 billion beer bottles were sealed using *Darafresh* oxygen-absorbing technology, which increases shelf life and enhances taste.

Grace Container Products

TAKING TECHNOLOGY AROUND THE WORLD

Grace sealants are vital to the safety and sealing integrity of more than 450 billion cans and bottles each year. Grace is committed to customer satisfaction and quality in the delivery of water-based and environmentally friendly solvent-based sealants and coatings for the rigid container market. Grace's position as the world leader in can sealing technology is founded on continual product innovation and strong technical support, close customer partnerships and a focus on adding measurable value to each step in the development, manufacture and sale of its products.

Breakthrough Sealing Technology

Product taste tests by major North American and European breweries are proving the outstanding ability of unique *Darafresh*™ oxygen-absorbing technology to maintain product quality—with minimal added preservatives—and increase shelf life, thereby reducing product rotation and distribution costs. Beer is particularly sensitive to oxygen—as little as one part per billion of oxygen in the headspace of a beer bottle will start the degradation process. This can impede market acceptance as major breweries expand into developing regions where optimal product distribution controls are sometimes lacking. Focused initially on beer and beverage producers, Grace is commercializing a full range of *Darafresh* closure sealant systems and evaluating growth opportunities for this technology in other container packaging markets.

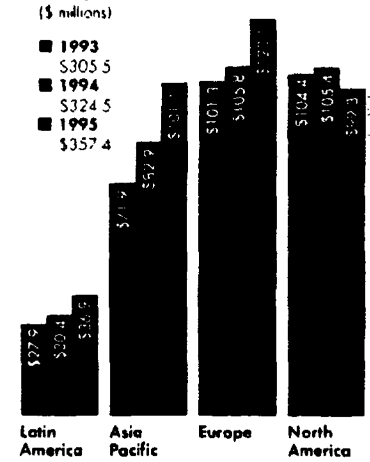
Best-in-Class Sealants

Grace offers its customers a wide range of advanced, environmentally friendly can and closure sealants. Available globally, Grace's best-in-class sealants facilitate ultra-high-speed application, providing excellent product protection on a full range of metal, glass and plastic containers.

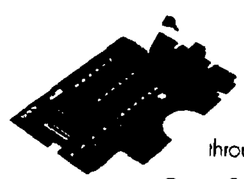
Supporting a Global Customer Base

To ensure successful transition of its sealing and coating technologies from the lab to the production line, Grace extended its global customer support network with a new container technical center in the Philippines. With a comparable facility planned for São Paulo, Brazil, Grace can provide quick, professional response with the latest technology and quality support in every market region.

Europe Leads in Sales



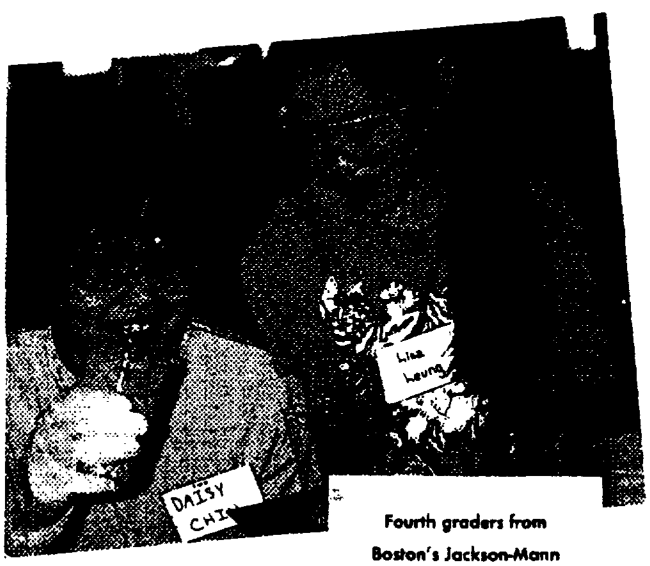
Supporting globalizing customers with local sourcing for high-performance can and closure sealants, the Company's 51%-owned joint venture, *A/O Grace KRIZ*, manufactures can sealing compounds for food canning and closure compounds for beverage bottling in Russia and other C.I.S. republics. In 1995, *Grace KRIZ* upgraded existing equipment and opened a new can and closure sealant production facility.



Grace Specialty Polymers

Related to *Grace Container Products* through shared polymer technology resources, *Grace Specialty Polymers* is a leading developer of formulated engineered polymers for printed circuit board and component assembly in the electronics, electrical, automotive and defense industries.

To Care



Fourth graders from Boston's Jackson-Mann School learned a lot about the construction industry when they competed to make the strongest, lightest concrete possible. They tested their product in Grace's lab, one of the world's largest privately owned cement and concrete research facilities.

Enhancing Global Performance

Grace's *Commitment to Care*™ program, signifying a responsibility to employees, customers and community neighbors, extended its reach beyond North America in 1995 to achieve worldwide implementation. *Commitment to Care* embraces specific performance objectives in six key areas: product stewardship, employee health and safety, community awareness and emergency response, process safety, distribution and pollution prevention.

Committed to Continuous Improvement

Grace is committed to continuously improving environmental, health and safety (EHS) performance in its global operations. The Company has pledged to operate according to the highest standards of performance as well as to incorporate sound EHS management concepts into the design and construction of new facilities.

In 1995, Grace adopted worldwide standards for product stewardship, process safety and employee health and safety. A new global program to collect, evaluate and benchmark waste and emissions data should enable Grace to monitor continuing reductions in waste and emissions on a worldwide basis.

Building Better Communities

Grace's success depends upon the health and vitality of the communities in which it operates—this philosophy drives the Company's community outreach efforts. During 1995, Grace Foundation and direct corporate contributions to support education, human services, youth development, health care, economic development and environmental organizations totaled $3.6 million. Education continues to be a major focus, capturing 57% of the Grace Foundation's 1996 budget. School partnerships also figure prominently in Grace's community outreach activities.

Grace employees work with Baltimore, Maryland's Southern High School to encourage students to attend school, graduate and aim for higher education. The program emphasizes math and science, while exposing students to engineering and manufacturing. Grace offers to hire one Southern High graduate for every two openings at its Curtis Bay Works in Maryland.

Through "Creating Lasting Links," Grace scientists helped elementary school teachers develop—and teach—a new science curriculum focusing on science skills and principles, such as measurement, observation, cause and effect

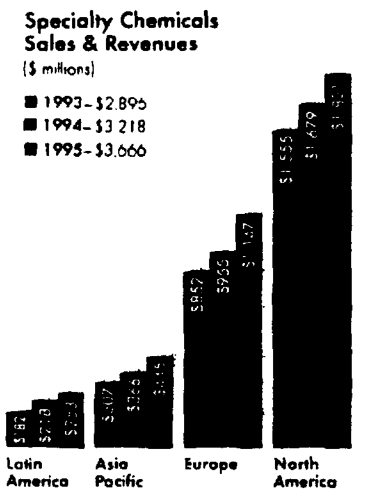
MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

REVIEW OF OPERATIONS

Overview

Sales and revenues increased 14% in 1995 over 1994, as compared to an increase of 11% in 1994 over 1993.

(Loss)/income from continuing operations was $(196.6) million, $(41.4) million and $19.1 million in 1995, 1994 and 1993, respectively. These results reflected (a) 1995, 1994 and 1993 pretax provisions of $275.0 million, $316.0 million and $159.0 million ($178.7 million, $200.0 million and $100.0 million after-tax), respectively, relating to asbestos-related liabilities and insurance coverage (see "Financial Condition: Asbestos-Related Matters" below and Note 2 to the Consolidated Financial Statements for further information); (b) 1995 and 1994 pretax provisions of $77.0 million and $40.0 million ($50.0 million and $26.0 million after-tax), respectively, relating to environmental liabilities (see "Financial Condition: Environmental Matters" below for further information); (c) a 1995 pretax charge of $220.0 million ($144.0 million after-tax) relating to restructuring costs, asset impairments and other costs (see "Statement of Operations: Restructuring Costs, Asset Impairments and Other Costs" below for further information); (d) a 1995 pretax charge of $30.0 million ($18.6 million after-tax) relating to corporate governance matters; and (e) a 1994 gain of $27.0 million (pre- and after-tax) on the sale of Grace's remaining interest in The Restaurant Enterprises Group, Inc. Excluding these provisions and charges from all years, income from continuing operations in 1995 increased 24%, to $194.7 million, as compared to 1994, and in 1994 increased 32%, to $157.6 million, over 1993.



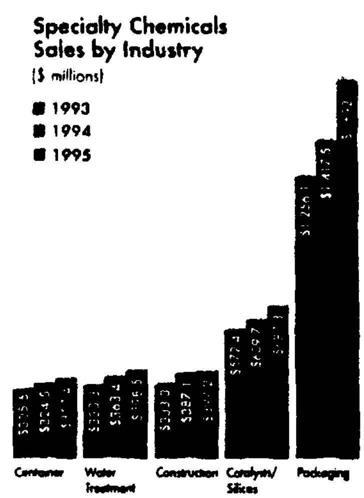
Income from continuing operations reflects corporate expenses of $37.8 million, $37.1 million and $37.4 million in 1995, 1994 and 1993, respectively, previously allocated to the discontinued health care operations. These expenses will not be assumed by National Medical Care, Inc. (NMC), Grace's principal health care subsidiary, following completion of its proposed separation from Grace, and it is expected that these costs will be eliminated. See below for additional information regarding the proposed separation of NMC from Grace and Grace's cost management efforts.

For all periods presented, the Consolidated Statement of Operations has been restated to reflect the classification of certain businesses as discontinued operations, as discussed in Note 7 to the Consolidated Financial Statements.

Specialty Chemicals

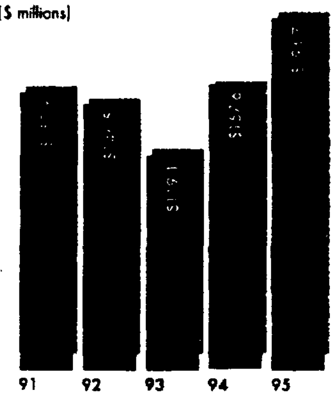
Operating Results – 1995 Compared to 1994

As noted above, sales and revenues increased 14% in 1995 as compared to 1994, reflecting favorable volume, price/product mix and currency translation variances estimated at 7%, 4% and 3%, respectively. All product lines experienced improved volumes in 1995. Packaging volume increases reflected higher sales of bags and films in all regions, and higher sales of laminates in all regions other than Latin America. Volume increases in catalysts and other silica-based products reflected higher sales in all regions, especially refinery catalysts in Asia Pacific and Europe, and silica/adsorbent products in Europe and Asia Pacific. Container volume increases were due to increased sales of specialty polymers and can sealing products in Asia Pacific, and coating products in Latin America. Volume increases in water treatment reflected higher paper industry process chemicals sales in Europe and North America caused by market share gains, as well as higher water treatment chemicals sales in Latin America. Construction products experienced volume increases, primarily in Asia Pacific, due to increased construction activity, partially offset by volume decreases in both fire protection products in North America (due to a small market share loss) and waterproofing products in Europe and North America.



Operating income before taxes (which excludes for all years the items discussed in the second paragraph of "Overview" above) increased by 15% in 1995 as compared to 1994. North American results in 1995 improved, reflecting strong growth in packaging due to the volume increases noted above (especially in bags). However, this was partially offset by reduced profitability in refinery catalysts, as North American refiners continued to experience low margins. The narrow spread between light and heavy crude oil prices led customers to crack higher quality light crude rather than heavy crude oil (which requires more catalysts). In addition, water treatment chemicals in North America experienced lower profitability due to ongoing market consolidations. European results in 1995 improved significantly versus 1994, primarily in packaging, reflecting volume increases caused by an economic recovery that revitalized key markets, partially offset by unfavorable results in construction waterproofing products due to higher material costs and a slowdown in the nonresidential construction market. European results also benefited from the absence of costs incurred in 1994 to streamline European packaging, water treatment and container operations. In Asia Pacific, favorable results were achieved versus 1994, primarily in refinery catalysts and silica/adsorbent and construction products (due to the volume increases noted above), partially offset by higher operating costs incurred to increase market share in the region. Latin American 1995 results declined slightly versus 1994, primarily due to the effect of inflation indexation on wage and employee benefit costs in the Brazilian water treatment operations, partially offset by increased profitability in packaging due to improved volumes and in container products due to market share gains in coating products. The above results reflect the allocation of corporate overhead and corporate research expenses; corporate interest and financing costs and nonallocable expenses are not reflected in the results of specialty chemicals.

Income from Continuing Operations
(before special items)
($ millions)



Operating Results – 1994 Compared to 1993

Sales and revenues increased by 11%, and operating income before taxes increased by 19%, in 1994 as compared to 1993. The increase in sales and revenues reflected favorable volume, price/product mix and currency translation variances estimated at 9%, 1% and 1%, respectively. Volume increases were experienced by all core product lines. North American results in 1994 were positively affected by strong growth in construction and packaging, mainly due to the volume increases, partially offset by reduced profitability in refinery catalysts due to volume decreases as a result of customers' use of higher quality crude oil and an increase in customer maintenance shutdowns. European results in 1994 improved significantly versus 1993, primarily due to improvements in refinery and polyolefin catalysts and construction products (due to the volume increases), partially offset by costs associated with streamlining European operations. In Asia Pacific, favorable results were achieved versus 1993, primarily due to volume increases in refinery and polyolefin catalysts and container products. Latin American 1994 results improved versus 1993, primarily due to increased profitability in packaging (due to increased volumes in bags, films and laminates). Latin American results also benefited from improved economic conditions in Brazil; however, this was partially offset by the devaluation of the Mexican peso in late 1994.

STATEMENT OF OPERATIONS

Other Income

See Note 4 to the Consolidated Financial Statements for information relating to other income.

Interest Expense and Related Financing Costs

Excluding amounts allocated to discontinued operations (as discussed in Note 7 to the Consolidated Financial Statements), interest expense and related financing costs of $71.3 million in 1995 increased 44% versus 1994. Including amounts allocated to discontinued operations, interest expense and related financing costs increased 50% in 1995 over 1994, to $164.8 million, primarily due to higher average effective short-term interest rates and higher debt levels.

Grace's debt and interest rate management objectives are to reduce its cost of funding over the long term, considering economic conditions and their potential impact on Grace, and to improve liquidity by developing and maintaining access to a variety of long-term and short-term capital markets. To manage its exposure to changes in interest rates, Grace enters into interest rate agreements; during 1995, most of these agreements effectively converted fixed-rate debt into variable-rate debt. These agreements have readily identifiable impacts on interest cost and are characterized by broad market liquidity. See Note 11 to the Consolidated Financial Statements for further information on interest rate agreements.

See "Financial Condition: Liquidity and Capital Resources" below and Note 10 to the Consolidated Financial Statements for information on borrowings.

Research and Development Expenses

Research and development spending increased 13% in 1995 versus 1994. Research and development spending continues to be directed toward Grace's core specialty chemicals businesses. As discussed below, during 1995 Grace undertook a worldwide restructuring program, including a study of company-wide research and development expenses. Certain actions have already been taken based on this study, including the shutdown of Grace's Japan research center and the phase-out of certain research programs related to noncore operations.

Restructuring Costs, Asset Impairments and Other Costs

Restructuring Costs

As discussed in Note 5 to the Consolidated Financial Statements, during the third quarter of 1995, Grace began implementing a worldwide restructuring program aimed at streamlining processes and reducing general and administrative expenses, factory administration costs and noncore corporate research and development expenses. The program is expected to be substantially completed by the end of 1996. In the third and fourth quarters of 1995, Grace recorded pretax charges totalling $44.3 million and $91.7 million ($27.2 million and $61.9 million after-tax), respectively, comprised of $77.4 million for employee termination benefits, $13.4 million for plant closure and related costs, including lease termination costs; $15.5 million for prior business exits and related costs; $20.8 million for asset writedowns, and $8.9 million for other costs. The $77.4 million for employee termination benefits primarily represents severance pay and other benefits associated with the elimination of approximately 1,000 positions worldwide; more than 50% of the total cost reductions will come from corporate staff functions worldwide.

Grace expects to implement additional cost reductions and efficiency improvements beyond those discussed above, as its businesses further evaluate and reengineer their operations. These reductions and efficiencies are expected in areas such as purchasing, logistics, working capital management and manufacturing.

Asset Impairments

During 1995, Grace determined that, due to various events and changes in circumstances (including the worldwide restructuring program described above), certain long-lived assets and related goodwill were impaired. As a result, in the fourth quarter of 1995, Grace recorded a $43.5 million pretax charge ($29.0 million after tax), the majority of which related to assets that will continue to be held and used in Grace's continuing operations; the charge included no significant individual components. Grace determined the amount of the charge based on various valuation techniques, including discounted cash flow, replacement cost and net realizable value for assets to be disposed of.

Other Costs

Also, in the fourth quarter of 1995, Grace recorded pretax charges totalling $40.5 million ($25.9 million after-tax) relating to the writedown of corporate assets ($27.0 million) and working capital assets ($13.5 million). These amounts are included in "Cost of goods sold and operating expenses" in the Consolidated Statement of Operations.

Income Taxes

Grace's effective tax rates were (37.1)%, (53.0)% and 34.6% in 1995, 1994 and 1993, respectively. Excluding the items discussed in the second paragraph of "Review of Operations: Overview" above, Grace's effective tax rates were 32.8%, 34.6% and 36.7% in 1995, 1994 and 1993, respectively. The lower effective tax rate in 1995, as compared to 1994, was largely due to the reversal of the valuation allowance on foreign net operating losses and lower state income taxes, partially offset by higher taxes on foreign operations. The lower effective tax rate in 1994, as compared to 1993, was largely due to lower taxes on foreign operations.

Grace has recognized a valuation allowance relating to uncertainty as to the realization of certain deferred tax assets, including U.S. tax credit carryforwards, state and local net operating loss carryforwards and net deferred tax assets. As a result of the favorable resolution of an audit, the valuation allowance on net operating loss carryforwards in foreign jurisdictions was reversed in 1995. Based upon anticipated future results, Grace has concluded, after consideration of the valuation allowance, that it is more likely than not that the remaining balance of the net deferred tax assets will be realized.

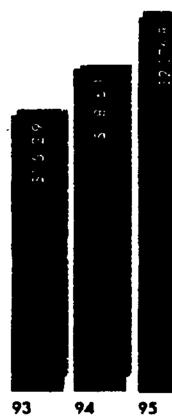
See Note 6 to the Consolidated Financial Statements for further information on income taxes.

DISCONTINUED OPERATIONS

Health Care

In June 1995, the Company announced that its Board of Directors had approved a plan to spin off NMC. As a result, Grace classified its health care business as a discontinued operation in the second quarter of 1995 and, accordingly, NMC's operations are included in "(loss)/income from discontinued operations" in the Consolidated Statement of Operations.

Health Care Sales & Revenues
($ millions)



Following NMC's receipt in October 1995 of five investigative subpoenas from the Office of the Inspector General of the U.S. Department of Health and Human Services (OIG), as discussed below, the completion of the spin-off of NMC, originally expected in the 1995 fourth quarter, was delayed.

In February 1996, Grace and Fresenius AG (Fresenius) entered into a definitive agreement to combine NMC with Fresenius' worldwide dialysis business (FWD) to create Fresenius Medical Care (FMC). As a result of the combination, FMC would acquire NMC, which would remain responsible for all liabilities arising out of the investigations, discussed below. However, Grace would retain certain health care assets, primarily a bioseparation sciences business, a health care services company and other assets (including cash and marketable securities).

The combination would follow a borrowing of approximately \$2.3 billion by NMC, a tax-free distribution of the proceeds by NMC to Grace, and a tax-free distribution by the Company, with respect to each share of its Common Stock, of one share of a newly formed corporation holding all of Grace's businesses (principally its specialty chemicals businesses) other than NMC. As a result of the separation of Grace's specialty chemicals businesses from NMC and the subsequent combination of NMC and FWD, the holders of the Company's Common Stock would own 100% of the specialty chemicals company and 44.8% of FMC, and Fresenius and other shareholders would own 55.2% of FMC. The holders of the Company's Common Stock would also own preferred stock, the value of which would be linked to the performance of FMC. Completion of the various transactions is subject to customary conditions, including the approval of the shareholders of the Company and Fresenius; U.S., German and European regulatory actions; and obtaining financing on satisfactory terms. Commitments for financing have been received, and it is expected that the various transactions will be completed by the third quarter of 1996.

Operating Results – 1995 Compared to 1994

Health care sales and revenues for 1995 increased by 11% over 1994, due to increases of 13%, 3% and 10%, respectively, in kidney dialysis services, home health care and medical products operations. The increase in kidney dialysis services reflects acquisitions in 1995 and 1994, and the increase in home health care reflects the full-year ownership of Home Nutritional Services, Inc., a national provider of home infusion therapy services acquired in April 1994. The number of centers providing dialysis and related services increased 15%, from 590 at December 31, 1994 to 681 at December 31, 1995 (574 in North America, 62 in Europe, 33 in Latin America and 12 in Asia Pacific).

Operating income before taxes in 1995 increased 10%, to \$315.6 million, as compared to 1994, excluding 1995 pretax charges totalling \$117.5 million (\$102.4 million after-tax). These pretax charges are comprised of (a) asset impairments of \$84.3 million (\$83.6 million after-tax); (b) the phase-out of certain of Grace's health care research programs of \$8.8 million (\$5.6 million after-tax); (c) changes in accounting estimates totalling \$8.7 million (\$1.8 million after-tax); (d) additional costs associated with Grace's long-term incentive programs applicable to NMC of \$8.3 million (\$4.8 million after-tax); and (e) other items totalling \$7.4 million (\$6.6 million after-tax). Health care results reflect the allocation of Grace's health care-related research expenses; however, corporate interest and financing costs allocated to the health care business are not reflected in operating income before taxes. These allocations are not necessarily indicative of the costs that would be incurred by the health care business on a stand-alone basis.

Health Care Pretax Operating Income
(before special items)
($ millions)

The 1995 asset impairments totalling $84.3 million pretax, referred to above, are comprised of: (a) NMC's investment in a German dialysis machine manufacturing operation – $39.8 million (pre- and after-tax); (b) NMC's investment in a dialyzer development operation in Ireland – $16.6 million (pre- and after-tax); (c) Grace's investment in a health care services company – $26.2 million (pre- and after-tax); and (d) other items of $1.7 million pretax ($1.0 million after-tax).

Operating Results – 1994 Compared to 1993

Sales and revenues for 1994 increased by 24% over 1993, due to increases of 28% and 47%, respectively, in kidney dialysis services and home health care operations, partially offset by a decrease of 7% in medical products revenues. The decrease in medical products operations reflects a decline in bloodline sales resulting from warning letters and import alerts issued by the U.S. Food and Drug Administration (FDA) in the second quarter of 1993. Operating income before income taxes for 1994 increased 23%, to $287.5 million, over 1993, reflecting the continued growth of all health care businesses, as well as improvements in cost controls, operating efficiencies and capacity utilization. These favorable results were partially offset by the costs of improving and expanding quality assurance systems for medical products manufacturing operations, as a result of the FDA warning letters and import alerts.

Other Significant Health Care Matters

In October 1995, NMC received five investigative subpoenas from the OIG. The subpoenas call for the production of extensive documents relating to various aspects of NMC's business. A letter accompanying the subpoenas stated that they had been issued in conjunction with an investigation being conducted by the OIG, the U.S. Attorney for the District of Massachusetts and others concerning possible violations of Federal laws relating to health care payments and reimbursements. The results of the investigation and its impact, if any, cannot be predicted at this time. In the event that any government agency believes that wrongdoing related to the investigation has occurred, civil and/or criminal proceedings could be instituted, and if any such proceedings were to be instituted and the outcome were unfavorable, NMC could be subject to fines, penalties and damages or could become excluded from government reimbursement programs. Any such result could have a material adverse effect on NMC's financial position or the results of operations of NMC and Grace.

NMC's business, financial position and results of operations could also be materially adversely affected by (a) an adverse outcome in the pending litigation concerning the implementation of certain provisions of the Omnibus Budget Reconciliation Act of 1993 relating to the coordination of benefits between Medicare and employer health plans in the case of certain dialysis patients, (b) an adverse outcome in the pending challenge by NMC of changes effected by Medicare in approving reimbursement claims relating to the administration of intradialytic parenteral nutrition (IDPN) therapy, or (c) the adoption of pending Medicare proposals to change IDPN coverage prospectively.

See Note 7 to the Consolidated Financial Statements for additional information relating to the above matters.

Cocoa and Other Businesses

In the second quarter of 1993, Grace classified as discontinued operations its cocoa business; its battery separators business; certain engineered materials businesses, principally its printing products, material technology and electromagnetic radiation control businesses (collectively, EMS); and other noncore businesses. At that time, a provision of $105.0 million (net of an applicable tax benefit of $22.3 million) was recorded to reflect the losses expected on the divestment of these businesses.

During the fourth quarter of 1995, Grace revised the divestment plan for its cocoa business. As a result of this revised divestment plan, recent trends and a reassessment of forecasts for all remaining discontinued operations, Grace recorded an additional provision of $151.3 million (net of an applicable tax benefit of $48.7 million) related to its remaining discontinued operations, principally the cocoa business.

See Note 7 to the Consolidated Financial Statements for additional information relating to the above matters.

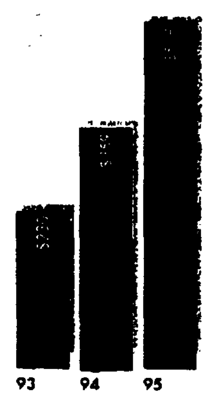
FINANCIAL CONDITION

Liquidity and Capital Resources

During 1995, the net pretax cash provided by Grace's continuing operating activities was $229.7 million, versus $210 9 million in 1994. The increase was primarily due to net cash inflows of $97.0 million in 1995 from settlements with certain insurance carriers for asbestos-related litigation, net of amounts paid for the defense and disposition of asbestos-related litigation (see discussion below), as compared to the net outflow of $60.0 million for asbestos-related litigation in 1994. However, the 1995 increase was offset by an increase in the use of operating working capital. After giving effect to the net pretax cash provided by operating activities of discontinued operations (including an increase in the use of operating working capital by NMC in 1995) and increased payments of income taxes (attributable to taxable income resulting from settlements of asbestos-related litigation, as well as audit adjustments to prior years' Federal income tax returns), the net cash provided by operating activities was $107.0 million in 1995 versus $453.5 million in 1994.

Investing activities used $801.6 million of cash in 1995, largely reflecting capital expenditures of $537.6 million (more than 75% of which relates to Grace's packaging and catalyst and other silica-based businesses) and the acquisition of dialysis centers and medical products facilities for a total of $37.4 million in the first quarter of 1995. Also, investing activities of discontinued operations for 1995 used $295.2 million, primarily reflecting the classification of the health care segment as a discontinued operation in the second quarter. Management anticipates that the level of capital expenditures in 1996 will approximate that of 1995. In 1995, Grace launched a $350.0 million global capital expansion program in its packaging product line, including $50.0 million to build a plant in Seneca, South Carolina to serve the fresh-cut produce market. In 1996, Grace is also scheduled to open new silica and packaging plants in Kuantan, Malaysia.

Capital Expenditures — Continuing Operations
($ millions)



Net cash provided by financing activities in 1995 was $655.7 million, primarily reflecting an increase in total debt from December 31, 1994 and the exercise of employee stock options, offset by the payment of $112.6 million of dividends. Total debt was $1,933.8 million at December 31, 1995, an increase of $404.1 million from December 31, 1994. Grace's total debt as a percentage of total capital (debt ratio) increased from 50.4% at December 31, 1994 to 61.1% at December 31, 1995, primarily due to the reduction in shareholders' equity (due to the charges discussed in the second paragraph of "Review of Operations: Overview" and "Statement of Operations: Discontinued Operations" above) and the increase in total debt. At December 31, 1995, the net assets of the discontinued health care segment included $226.7 million of debt.

Grace expects to receive a substantial amount of cash in 1996 from the expected distribution by NMC (as discussed in "Statement of Operations: Discontinued Operations" above and Note 7 to the Consolidated Financial Statements), the sale of the Grace Dearborn water treatment and process chemicals business (see discussion below), and, to a lesser extent, funds generated by operations. Grace expects to apply a substantial portion of the cash proceeds generated by these transactions to the reduction of borrowings. Any net excess is expected to be applied to the repurchase of shares of the Company's Common Stock and selected strategic acquisitions that complement existing businesses.

In the third quarter of 1995, Grace announced that its Board of Directors had authorized management to pursue options to maximize the value of its Grace Dearborn water treatment and process chemicals business. In March 1996, Grace announced that it had entered into a definitive agreement to sell Grace Dearborn to Betz Laboratories, Inc. for $632.0 million. The transaction is expected to be completed in the second quarter of 1996

In October 1995, in anticipation of the then pending spin-off of NMC, the Company's Board of Directors declared a quarterly cash dividend of 12.5 cents per share on the Company's Common Stock, a reduction from the previous quarterly cash dividend of 35 cents per share. At that time, the Board also approved a policy of paying dividends at a rate of 20% - 30% of the prior year's net earnings and authorized the repurchase of up to 10 million shares of the Company's Common Stock. In February 1996, after entering into the definitive agreement to combine NMC with FWD, the Board increased the number of shares that may be repurchased to 20% of the Company's outstanding Common Stock (see "Statement of Operations: Discontinued Operations" above and Note 7 to the Consolidated Financial Statements).

Asbestos-Related Matters

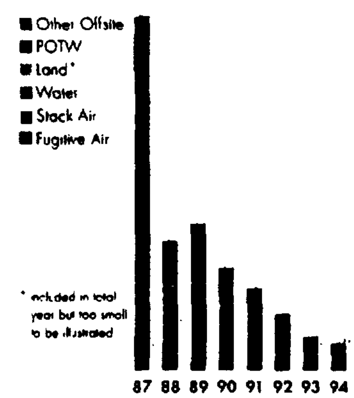
As reported in Note 2 to the Consolidated Financial Statements, Grace is a defendant in lawsuits relating to previously sold asbestos-containing products and is involved in related litigation with certain of its insurance carriers. In 1995, Grace received $97.0 million under settlements with certain insurance carriers, net of amounts paid for the defense and disposition of asbestos-related property damage and personal injury litigation. During the fourth quarter of 1995, Grace recorded a noncash pretax charge of $275.0 million ($178.7 million after-tax), primarily to reflect the estimated costs of defending against and disposing of personal injury lawsuits and claims expected to be filed through 1998. The balance sheet at December 31, 1995 includes a receivable due from insurance carriers, a portion of which is subject to litigation, of $321.2 million. Grace has also recorded notes receivable of $130.0 million ($118.4 million after discounts) for amounts to be received in 1996 to 1999 pursuant to settlement agreements previously entered into with certain insurance carriers.

Although the amounts to be paid in 1996 in respect of asbestos-related lawsuits and claims cannot be precisely estimated, Grace expects that it will be required to expend approximately $40.0 million (pretax) in 1996 to defend against and dispose of such lawsuits and claims (after giving effect to payments to be received from certain insurance carriers, as discussed above and in Note 2 to the Consolidated Financial Statements). As indicated therein, the amounts reflected in the Consolidated Financial Statements with respect to the probable cost of defending against and disposing of asbestos-related lawsuits and claims and probable recoveries from insurance carriers represent estimates; neither the outcomes of such lawsuits and claims nor the outcomes of Grace's continuing litigations with certain of its insurance carriers can be predicted with certainty.

Environmental Matters

Grace incurs costs to comply with environmental laws and regulations and to fulfill its commitment to industry initiatives and Grace standards. Worldwide expenses of continuing operations related to the operation and maintenance of environmental facilities and the disposal of hazardous and nonhazardous wastes totalled $43.5 million, $35.7 million and $40.7 million in 1995, 1994 and 1993, respectively. Such costs are estimated to be approximately $45.0 million and $47.0 million in 1996 and 1997, respectively. In addition, worldwide capital expenditures for continuing operations relating to environmental protection totalled $14.9 million in 1995, compared to $21.5 million and $19.3 million in 1994 and 1993, respectively. Capital expenditures to comply with environmental initiatives in future years are estimated to be $20.0 million and $17.0 million in 1996 and 1997, respectively. Grace has also incurred costs to remediate environmentally impaired sites. These costs were $31.3 million, $30.8 million and $44.4 million in 1995, 1994 and 1993, respectively. These amounts have been charged against previously established reserves. Future cash outlays for remediation costs are expected to total $30.0 million in 1996 and $20.0 million in 1997. Expenditures have been funded from internal sources of cash and are not expected to have a significant effect on liquidity.

SARA Emissions Continue to Decline
(millions of pounds)



Grace accrues for anticipated costs associated with investigatory and remediation efforts relating to the environment in accordance with Statement of Financial Accounting Standards No. 5, "Accounting for Contingencies," which requires estimating the probability and amount of future costs. At December 31, 1995, Grace's liability for environmental investigatory and remediation costs related to continuing and discontinued operations totalled approximately $280.3 million, which amount does not take into account any discounting for future expenditures or possible future insurance recoveries. The measurement of the liability is evaluated quarterly based on currently available information. In 1995 and 1994, periodic provisions were recorded for environmental and plant closure expenses, which include the costs of future environmental investigatory and remediation activities. Additionally, in the fourth quarter of 1995 and first quarter of 1994, Grace recorded pretax provisions of $77.0 million and $40.0 million ($50.0 million and $26.0 million after-tax), respectively, principally to provide for future costs related to remediation activities required at former manufacturing sites.

CONSOLIDATED FINANCIAL STATEMENTS
W. R. GRACE & CO. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF OPERATIONS

Dollars in millions, except per share amounts	**1995**	1994	1993
Sales and revenues	**$3,665.5**	$3,218.2	$2,895.5
Other income (Note 4)	**41.9**	42.6	57.8
Total	**3,707.4**	3,260.8	2,953.3
Cost of goods sold and operating expenses	**2,243.7**	1,900.8	1,746.7
Selling, general and administrative expenses	**905.6**	773.6	673.1
Depreciation and amortization	**186.3**	165.0	153.5
Interest expense and related financing costs (Note 10)	**71.3**	49.5	42.9
Research and development expenses	**120.6**	106.8	111.5
Corporate expenses previously allocated to health care operations	**37.8**	37.1	37.4
Restructuring costs and asset impairments (Note 5)	**179.5**	–	–
Provision relating to asbestos-related liabilities and insurance coverage (Note 2)	**275.0**	316.0	159.0
Total	**4,019.8**	3,348.8	2,924.1
(Loss)/income from continuing operations before income taxes	**(312.4)**	(88.0)	29.2
(Benefit from)/provision for income taxes (Note 6)	**(115.8)**	(46.6)	10.1
(Loss)/income from continuing operations	**(196.6)**	(41.4)	19.1
(Loss)/income from discontinued operations (Note 7)	**(129.3)**	124.7	6.9
Net (loss)/income	**$ (325.9)**	$ 83.3	$ 26.0
(Loss)/earnings per share:			
Continuing operations	**$ (2.05)**	$ (.45)	$ .20
Net (loss)/earnings	**$ (3.40)**	$ .88	$ .28
Fully diluted (loss)/earnings per share:			
Continuing operations	$ –[1]	$ –[1]	$ .20
Net (loss)/earnings	$ –[1]	$ .88	$ .28

The Notes to Consolidated Financial Statements, pages 26 to 49, are integral parts of these statements.

[1] Not presented as the effect is antidilutive.

CONSOLIDATED STATEMENT OF CASH FLOWS

Dollars in millions	1995	1994	1993
Operating Activities			
(Loss)/income from continuing operations before income taxes	**$(312.4)**	$ (88.0)	$ 29.2
Reconciliation to cash provided by operating activities:			
Depreciation and amortization	**186.3**	165.0	153.5
Provision relating to asbestos-related liabilities and insurance coverage	**275.0**	316.0	159.0
Noncash charge relating to restructuring costs and asset impairments	**159.9**	-	-
Changes in assets and liabilities, excluding effect of businesses acquired/divested and foreign exchange:			
Increase in notes and accounts receivable, net	**(44.7)**	(159.5)	(103.2)
Increase in inventories	**(62.1)**	(43.4)	(50.5)
Net (payments for)/proceeds from settlements of interest rate agreements	**-**	(4.0)	67.9
Proceeds from asbestos-related insurance settlements	**257.3**	138.6	74.6
Payments made for asbestos-related litigation settlements, judgments and defense costs	**(160.3)**	(198.6)	(177.7)
(Decrease)/increase in accounts payable	**(48.3)**	10.3	50.1
Other	**(21.0)**	74.5	(173.9)
Net pretax cash provided by operating activities of continuing operations	**229.7**	210.9	29.0
Net pretax cash provided by operating activities of discontinued operations	**114.2**	328.6	316.8
Net pretax cash provided by operating activities	**343.9**	539.5	345.8
Income taxes paid	**(236.9)**	(86.0)	(102.7)
Net cash provided by operating activities	**107.0**	453.5	243.1
Investing Activities[1]			
Capital expenditures	**(537.6)**	(444.6)	(309.6)
Businesses acquired in purchase transactions, net of cash acquired and debt assumed	**(37.4)**	(276.9)	(306.6)
Increase in net assets of discontinued operations	**(295.2)**	(32.9)	(43.1)
Net proceeds from divestments	**56.7**	583.9	464.8
Net proceeds from sale/leaseback transactions	**-**	-	27.2
Proceeds from disposals of assets	**17.9**	34.0	15.4
Other	**(6.0)**	34.9	-
Net cash used for investing activities	**(801.6)**	(101.6)	(151.9)
Financing Activities[2]			
Dividends paid	**(112.6)**	(132.0)	(128.4)
Repayments of borrowings having original maturities in excess of three months	**(68.1)**	(141.2)	(512.6)
Increase in borrowings having original maturities in excess of three months	**148.5**	535.1	373.0
Net increase in/(repayments of) borrowings having original maturities of less than three months	**414.9**	(605.8)	155.7
Stock options exercised	**164.1**	20.9	21.0
Increase/(decrease) in net financing activities of discontinued operations	**120.8**	.2	(15.5)
Other	**(11.9)**	-	.9
Net cash provided by/(used for) financing activities	**655.7**	(322.8)	(105.9)
Effect of exchange rate changes on cash and cash equivalents	**1.2**	1.6	(.5)
(Decrease)/increase in cash and cash equivalents	**(37.7)**	30.7	(15.2)
Cash and cash equivalents, beginning of year	**78.3**	47.6	62.8
Cash and cash equivalents, end of year	**$ 40.6**	$ 78.3	$ 47.6

The Notes to Consolidated Financial Statements, pages 28 to 49, are integral parts of these statements.

[1] See Note 3 to the Consolidated Financial Statements for supplemental information relating to noncash investing activities.
[2] See Notes 3 and 10 to the Consolidated Financial Statements for supplemental information relating to noncash financing activities.

CONSOLIDATED BALANCE SHEET

Dollars in millions, except par value December 31,	1995	1994
Assets		
Current Assets		
Cash and cash equivalents	**$ 40.6**	$ 78.3
Notes and accounts receivable, net (Note 8)	**596.8**	975.7
Inventories (Note 8)	**491.9**	514.2
Net assets of discontinued operations (Note 7)	**323.7**	335.6
Deferred income taxes	**206.1**	295.4
Other current assets	**22.2**	29.7
Total Current Assets	**1,681.3**	2,228.9
Properties and equipment, net (Note 9)	**1,736.1**	1,730.1
Goodwill, less accumulated amortization of $20.6 (1994 - $71.8)	**111.8**	672.5
Net assets of discontinued operations – health care (Note 7)	**1,435.3**	-
Asbestos-related insurance receivable (Note 2)	**321.2**	512.6
Deferred income taxes	**386.6**	115.7
Other assets (Note 8)	**625.3**	970.8
Total Assets	**$6,297.6**	$6,230.6
Liabilities and Shareholders' Equity		
Current Liabilities		
Short-term debt (Note 10)	**$ 638.3**	$ 430.9
Accounts payable	**339.2**	433.7
Income taxes	**103.3**	197.0
Other current liabilities	**836.4**	872.9
Minority interest (Note 13)	**297.0**	297.0
Total Current Liabilities	**2,214.2**	2,231.5
Long-term debt (Note 10)	**1,295.5**	1,098.8
Other liabilities	**789.0**	690.9
Deferred income taxes	**44.8**	92.5
Noncurrent liability for asbestos-related litigation (Note 2)	**722.3**	612.4
Total Liabilities	**5,065.8**	4,726.1
Commitments and Contingencies (Notes 2, 7, 10 and 12)		
Shareholders' Equity (Note 14)		
Preferred stocks, $100 par value	**7.4**	7.4
Common stock, $1 par value; 300,000,000 shares authorized; outstanding at December 31: 1995 – 97,375,000, 1994 – 94,083,000	**97.4**	94.1
Paid in capital	**459.8**	308.8
Retained earnings	**709.0**	1,147.5
Cumulative translation adjustments	**(39.4)**	(53.3)
Treasury stock, 53,000 common shares, at cost	**(2.4)**	-
Total Shareholders' Equity	**1,231.8**	1,504.5
Total Liabilities and Shareholders' Equity	**$6,297.6**	$6,230.6

The Notes to Consolidated Financial Statements, pages 28 to 49 are integral parts of these statements

CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

Dollars in millions	**1995**	1994	1993
Preferred Stocks			
Balance, beginning of year	**$ 7.4**	$ 7.4	$ 7.5
Other	**-**	–	(.1)
Balance, end of year	**7.4**	7.4	7.4
Common Stock			
Balance, beginning of year	**94.1**	93.5	89.9
Conversion of notes and debentures	**-**	–	2.8
Stock options and awards	**3.3**	.6	.7
Acquisition	**-**	–	.1
Balance, end of year	**97.4**	94.1	93.5
Paid in Capital			
Balance, beginning of year	**308.8**	287.8	151.4
Conversion of notes and debentures	**-**	–	109.7
Stock options and awards	**151.1**	20.5	22.9
Acquisition	**-**	–	3.7
Other	**(.1)**	.5	.1
Balance, end of year	**459.8**	308.8	287.8
Retained Earnings			
Balance, beginning of year	**1,147.5**	1,196.2	1,298.6
Net (loss)/income	**(325.9)**	83.3	26.0
Dividends paid	**(112.6)**	(132.0)	(128.4)
Balance, end of year	**709.0**	1,147.5	1,196.2
Cumulative Translation Adjustments			
Balance, beginning of year	**(53.3)**	(67.3)	(2.4)
Translation adjustments	**13.9**	14.0	(64.9)
Balance, end of year	**(39.4)**	(53.3)	(67.3)
Treasury Stock			
Balance, beginning of year	**-**	–	-
Purchases of common stock	**(12.1)**	–	-
Shares issued under stock option plans	**9.7**	–	-
Balance, end of year	**(2.4)**	–	-
Total Shareholders' Equity	**$1,231.8**	$1,504.5	$1,517.6

The Notes to Consolidated Financial Statements, pages 28 to 49, are integral parts of these statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Dollars in millions, except per share amounts

1. SUMMARY OF SIGNIFICANT ACCOUNTING AND FINANCIAL REPORTING POLICIES

W. R. Grace & Co., through its subsidiaries, is primarily engaged in the packaging and specialty chemicals businesses on a worldwide basis. W. R. Grace & Co. has classified its other businesses as discontinued operations, the most significant of which are its health care and cocoa businesses. As used in these notes to the consolidated financial statements, the term "Company" refers to W. R. Grace & Co., a New York corporation, and the term "Grace" refers to the Company and/or one or more of its subsidiaries.

Principles of Consolidation — The consolidated financial statements include the accounts of Grace and majority-owned companies. Intercompany transactions and balances are eliminated in consolidation. Investments in affiliated companies (20%-50% owned) are accounted for under the equity method.

Reclassifications — Certain amounts in the prior years' consolidated financial statements and related notes have been reclassified to conform to the current year's presentation and as required with respect to discontinued operations.

Use of Estimates — The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions affecting the reported amounts of assets and liabilities (including disclosed amounts of contingent assets and liabilities) at the date of the consolidated financial statements and the reported revenues and expenses during the reporting period. Actual amounts could differ from those estimates.

Cash Equivalents — Cash equivalents consist of highly liquid instruments with maturities of three months or less when purchased. The recorded amounts approximate fair value because of the short maturities of these investments

Inventories — Inventories are stated at the lower of cost or market. The methods used to determine cost include first-in/first-out and, for substantially all U.S. chemical inventories, last-in/first-out. Market values for raw and packaging materials are based on current cost and, for other inventory classifications, on net realizable value.

Properties and Equipment — Properties and equipment are stated at the lower of cost or net realizable value. Depreciation of properties and equipment is generally computed using the straight-line method over the estimated useful lives of the assets. Interest is capitalized in connection with major project expenditures and amortized, generally on a straight-line basis, over the estimated useful lives of the assets.

Fully depreciated assets are retained in properties and equipment and related accumulated depreciation accounts until they are removed from service. In the case of disposals, assets and related depreciation are removed from the accounts and the net amount, less any proceeds from disposal, is charged or credited to income

Goodwill — Goodwill arises from certain purchase transactions and is amortized using the straight-line method over appropriate periods not exceeding 40 years.

Impairment — Grace has adopted Statement of Financial Accounting Standards (SFAS) No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." In accordance with this Statement, Grace reviews long-lived assets and related goodwill for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable.

Income Taxes — Grace uses an asset and liability approach for the accounting and financial reporting of income taxes.

Foreign Currency Translation — Foreign currency transactions and financial statements (except for those relating to countries with highly inflationary economies) are translated into U.S. dollars at current exchange rates, except that revenues, costs and expenses are translated at average exchange rates during each reporting period. The financial statements of subsidiaries located in countries with highly inflationary economies must be remeasured as if the functional currency were the U.S. dollar. The remeasurement creates translation adjustments that are reflected in net income. Allocations for income taxes included in the translation adjustments account in shareholders' equity were not significant

Financial Instruments — Grace enters into interest rate agreements and foreign exchange forward and option contracts to manage exposure to fluctuations in interest and foreign currency exchange rates.

The cash differentials paid or received on interest rate agreements are accrued and recognized as adjustments to interest expense. Gains and losses realized upon settlement of these agreements (recorded as other liabilities and other assets, respectively) are deferred and either amortized to interest expense over a period relevant to the agreement if the underlying hedged instrument remains outstanding, or recognized immediately if the underlying hedged instrument is settled. Cash flows related to the agreements are classified as operating activities in the Consolidated Statement of Cash Flows. consistent with the interest payments on the underlying debt.

Gains and losses on foreign currency forward and option contracts offset gains and losses resulting from the underlying transactions. Gains and losses on contracts that hedge specific foreign currency commitments are deferred and recorded in net income in the period in which the related transaction is consummated. Gains and losses on contracts that hedge net investments in foreign subsidiaries are recorded in the cumulative translation adjustments account in shareholders' equity.

Earnings Per Share — Primary earnings per share are computed on the basis of the weighted average number of common shares outstanding. Fully diluted earnings per share assume the issuance of common stock equivalents related to employee stock options and, prior to 1994, the conversion of convertible debt (with an increase in net income for the after-tax interest savings).

2. ASBESTOS AND RELATED INSURANCE LITIGATION

Grace is a defendant in lawsuits relating to previously sold asbestos-containing products and anticipates that it will be named as a defendant in additional asbestos-related lawsuits in the future. Grace was a defendant in approximately 40,800 asbestos-related lawsuits at December 31, 1995 (47 involving claims for property damage and the remainder involving approximately 92,400 claims for personal injury), as compared to approximately 38,700 lawsuits at December 31, 1994 (65 involving claims for property damage and the remainder involving approximately 67,900 claims for personal injury).

Property Damage Litigation

The plaintiffs in property damage lawsuits generally seek, among other things, to have the defendants absorb the cost of removing, containing or repairing the asbestos-containing materials in the affected buildings. Through December 31, 1995, 129 asbestos property damage cases were dismissed with respect to Grace without payment of any damages or settlement amounts; judgments were entered in favor of Grace in 10 cases (excluding cases settled following appeals of judgments in favor of Grace and a case in which the plaintiff was granted a new trial on appeal); Grace was held liable for a total of $74.7 in 7 cases (2 of which are on appeal); and 177 property damage suits and claims were settled for a total of $421.8.

Included in the asbestos property damage lawsuits pending against Grace and others at year-end 1995 was a class action, conditionally certified by the U.S. Court of Appeals for the Fourth Circuit in 1993 and pending in a U.S. District Court in South Carolina, covering all public and private colleges and universities in the U.S. whose buildings contain asbestos materials.

In July 1994, a South Carolina state court judge dismissed the claims of most class members from another purported nationwide class action asbestos property damage lawsuit. In his ruling, the judge held that a South Carolina statute prohibits nonresidents from pursuing claims in the South Carolina state courts with respect to buildings located outside the state. The plaintiffs have requested that the court reconsider its decision.

In December 1995, Grace entered into an agreement to settle a Pennsylvania state court action, certified as a class action in 1992, covering all commercial buildings in the U.S. leased in whole or in part to the U.S. government on or after May 30, 1986. The terms of the settlement agreement (which is subject to judicial review and approval after class members have an opportunity to be heard) are not expected to have a significant effect on Grace's consolidated results of operations or financial position.

Personal Injury Litigation

Through December 31, 1995, approximately 10,100 asbestos personal injury lawsuits involving 24,500 claims were dismissed with respect to Grace without payment of any damages or settlement amounts (primarily on the basis that Grace products were not involved), and approximately 23,700 such suits involving 29,600 claims were disposed of for a total of $109.0.

Asbestos-Related Liability

Subject to the factors discussed below, Grace estimates that its probable liability with respect to the defense and disposition of asbestos property damage and personal injury lawsuits and claims pending at December 31, 1995 and 1994 (and, in the case of the 1995 estimate, personal injury lawsuits and claims expected to be filed through 1998), is as follows:

December 31,	**1995**	1994
Current liability for asbestos-related litigation[(1)]	**$100.0**	$100.0
Noncurrent liability for asbestos-related litigation	**722.3**	612.4
Total asbestos-related liability	**$822.3**	$712.4

(1) Included in "Other current liabilities" in the Consolidated Balance Sheet.

In the fourth quarter of 1995, Grace recorded a noncash pretax charge of $260.0 ($169.0 after-tax) for asbestos-related liabilities, primarily to reflect the estimated costs to defend against and dispose of personal injury claims expected to be filed through 1998; Grace believes that it now has adequate experience to reasonably estimate the number of personal injury claims to be filed through 1998 and the costs of defending against and disposing of these claims. Other components of the 1995 provision include increases in the estimated costs of defending against and disposing of certain property damage cases pending at year-end 1995 and personal injury lawsuits and claims filed during 1995.

While personal injury cases and claims are generally similar to each other (differing only in the type of asbestos-related illness allegedly suffered by the plaintiff), Grace's estimated liability for such cases and claims is influenced by numerous variables that are difficult to predict (including the insolvency of other former asbestos producers, cross-claims by co-defendants, the rate at which new cases and claims are filed and the defense and disposition costs associated with these cases and claims).

Consequently, actual costs may vary from any estimate. For these reasons, Grace believes that it is not possible to reasonably estimate the number of cases and claims to be filed after 1998 or the costs of defending against and disposing of such cases and claims.

Each property damage case is unique in that the age, type, size and use of the building, and the difficulty of asbestos abatement, if necessary, vary from structure to structure; thus, the amounts involved in prior dispositions of property damage cases are not necessarily indicative of the amounts that may be required to dispose of such cases in the future. In addition, in property damage cases, information regarding product identification on a building-by-building basis (i.e., whether or not Grace products were actually used in the construction of the building), the age, type, size and use of the building, the jurisdictional history of prior cases and the court in which the case is pending provide the only meaningful guidance as to potential future costs. However, much of this information is not yet available in some of the property damage cases currently pending against Grace. Accordingly, it is not possible to estimate with precision the costs of defending against and disposing of these cases. Further, Grace believes that the number of property damage cases to be filed in the future and the costs associated with these filings are not estimable.

Asbestos-Related Insurance Receivable

Grace's ultimate exposure with respect to its asbestos-related lawsuits and claims will depend on the extent to which its insurance will cover damages for which it may be held liable, amounts paid in settlement and litigation costs. The following table shows Grace's total estimated insurance recoveries in reimbursement for past and estimated future payments to defend against and dispose of asbestos-related litigation and claims:

December 31,	**1995**	1994
Notes receivable from insurance carriers – current, net of discounts of $4.3 in 1995[1]	**$ 62.0**	$127.0
Notes receivable from insurance carriers – noncurrent, net of discounts of $7.3 in 1995[2]	**56.4**	60.0
Asbestos-related insurance receivable	**321.2**	512.6
Total amounts due from insurance carriers	**$439.6**	$699.6

[1]Included in "Notes and accounts receivable, net" in the Consolidated Balance Sheet.
[2]Included in "Other assets" in the Consolidated Balance Sheet.

At December 31, 1995, settlements with certain insurance carriers provided for the future receipt by Grace of $130.0, which Grace has recorded as notes receivable (both current and noncurrent) of $118.4, after discounts. In 1995 Grace received a total of $257.3 pursuant to settlements with insurance carriers in reimbursement for monies previously expended by Grace in connection with asbestos-related litigation; of this amount, $127.0 was received pursuant to settlements entered into in 1993 and 1994, which had previously been classified as notes receivable.

During 1995, Grace settled with an affiliated group of carriers that had agreed to a settlement in 1993, had made a series of payments under that agreement and had subsequently notified Grace that it would no longer honor the agreement. Pursuant to the 1995 settlement, the group of carriers paid Grace $44.0 in 1995 and agreed to make additional payments totalling $60.2 in 1996 and 1997 (which Grace has recorded as notes receivable, after discounts, of $54.5). Pursuant to a settlement with another group of carriers, Grace received $26.8 in 1995 and expects to receive an additional payment of $9.7 in 1996. Under both settlements, Grace will continue to receive payments based on future cash outflows for asbestos-related litigation and claims; such payments are estimated to represent approximately $237.3 of the asbestos-related receivable of $321.2 at December 31, 1995.

As a result of these settlements and a reassessment of its insurance receivable, Grace recorded a noncash net pretax charge of $15.0 ($9.7 after-tax) during the fourth quarter of 1995 to reflect a reduction in the receivable, primarily due to lower than anticipated settlements with insurance carriers and a discount on notes receivable in connection with prior settlements, partially offset by an increase in expected future reimbursements of costs to defend against and dispose of property damage cases pending at year-end 1995 and personal injury claims to be filed through 1998.

Insurance Litigation

Grace continues to seek to recover from its excess insurers the balance of the payments it has made with respect to asbestos-related litigation. As part of this effort, Grace continues to be involved in litigation with certain of its insurance carriers (having previously settled with certain primary and excess carriers, as discussed above). For the period October 1962 through June 1985 — the most relevant period for asbestos-related litigation — Grace purchased, on an annual basis, as much as eight levels of excess insurance coverage. (In general, excess policies provide that when claims paid exhaust coverage at one level, the insured may seek payment from the carriers at the next higher level.) For that 23-year period, the first six levels of excess insurance available from the insurance companies that Grace believes to be solvent (based primarily upon reports from a leading independent insurance rating service) provide nominal coverage of approximately $1,200.0 (including the amounts reflected in the receivable discussed above). However, (a) a portion of the personal injury lawsuits and claims pending at year-end 1995 and expected to be filed against Grace through 1998 will likely relate to periods for which no excess coverage is available; and (b) even where such excess coverage is available, the number of personal injury lawsuits and claims pending at year-end 1995 and expected to be filed against Grace in the future is not expected to be sufficient to result in significant payments under such coverage. Further, as a result of the May 1994 decision of the U.S. Court of Appeals for the Second Circuit, discussed below, a significant portion of the nominal excess coverage is not available in connection with property damage lawsuits. In addition, $142.0 of the $1,200.0 relates to excess coverage written by a group of insurance carriers that, while currently solvent, has experienced financial difficulties in recent years. This group of carriers settled with Grace in 1995 (as discussed above). The asbestos-related receivable of $321.2 at December 31, 1995 includes $54.7 to be paid by this group; management believes this amount is fully collectible.

As previously reported, in September 1993 the U.S. Court of Appeals for the Second Circuit ruled that, under New York law (which governs a significant portion of the policies that provide Grace's asbestos-related insurance coverage), such coverage is triggered based on the date of installation of asbestos-containing materials. As a result of this decision (which had the effect of reducing the amount of insurance coverage available to Grace with respect to asbestos property damage litigation and claims), Grace recorded a noncash pretax charge of $475.0 ($300.0 after-tax) in the 1993 third quarter. Grace reversed $316.0 ($200.0 after-tax) of the pretax charge in the 1993 fourth quarter after the court withdrew its September 1993 decision and agreed to rehear the case, but reinstated the $316.0 pretax charge ($200.0 after-tax) in the second quarter of 1994, when the court issued a new decision confirming its September 1993 decision. Because Grace's insurance covers both property damage and personal injury lawsuits and claims, the May 1994 decision has had the concomitant effect of reducing the insurance coverage available with respect to Grace's asbestos personal injury lawsuits and claims. However, in Grace's opinion, it is probable that recoveries from its insurance carriers (including amounts reflected in the receivable discussed above), along with other funds, will be available to satisfy the personal injury and property damage lawsuits and claims pending at December 31, 1995, as well as personal injury lawsuits and claims expected to be filed through 1998. Consequently, Grace believes that the resolution of its asbestos-related litigation will not have a material adverse effect on its consolidated results of operations or financial position.

3. ACQUISITIONS AND DIVESTMENTS

Acquisitions

During 1995, Grace made acquisitions totalling $260.8 (inclusive of cash acquired and debt assumed), all of which involved cash purchases of kidney dialysis centers and medical imaging facilities by National Medical Care, Inc. (NMC), Grace's principal health care subsidiary. Acquisitions in the first quarter of 1995, prior to the classification of NMC as a discontinued operation (see Note 7), totalled $41.1 (inclusive of cash acquired and debt assumed). Acquisitions by NMC subsequent to the first quarter of 1995 are presented as an investing activity and are included in "Increase in net assets of discontinued operations" in the Consolidated Statement of Cash Flows.

In 1994, Grace made acquisitions totalling $351.7 (inclusive of cash acquired and debt assumed), primarily in health care. Grace acquired Home Nutritional Services, Inc. for approximately $131.8 (inclusive of cash and assumed debt totalling $30.4) and acquired kidney dialysis centers and other health care businesses during 1994 for an aggregate of approximately $145.3 in cash. 1994 acquisitions also included construction chemicals businesses and a European flexible packaging business.

In 1993, Grace acquired Home Intensive Care, Inc. for approximately $129.0 in cash and acquired other health care businesses for an aggregate of $115.0 in cash and $3.8 in common stock. Additionally, during 1993 Grace acquired Latin America's largest water treatment business for approximately $57.6 in cash.

Divestments

During 1995, Grace realized gross proceeds of $58.8 (inclusive of debt assumed by the buyers) from divestments, including payments received in connection with divestments completed in prior years. The operations divested in 1995 consisted of three small units of Grace's construction products business, the composite materials business (previously classified as a discontinued operation), Grace's transportation services business and various investments.

In 1994, Grace realized gross proceeds of $646.2 (inclusive of debt assumed by the buyers) from divestments, including payments received in connection with divestments completed in prior years. Substantially all of the businesses divested during 1994 had previously been classified as discontinued operations. Divestment proceeds received in 1994 included $42.8 for Grace's remaining interest in The Restaurant Enterprises Group, Inc. (REG).

In 1993, Grace completed the sale of substantially all of its oil and gas operations, as well as certain corporate investments, all of which had previously been classified as discontinued operations. Other noncore businesses divested during 1993 included a 50% interest in a Japanese chemical operation and a food industry hygiene services business for approximately $31.4 and $11.2, respectively.

See Note 7 for a discussion of divestment activity related to discontinued operations.

4. OTHER INCOME

	1995	1994	1993
Interest income	**$15.8**	$ 1.3	$22.6
Equity in earnings of affiliated companies	**.2**	2.1	.6
Gains on sales of investments	**3.1**	27.3	22.9
Other, net	**22.8**	11.9	11.7
	$41.9	$42.6	$57.8

Interest income in 1995 and 1993 includes $9.8 and $20.0, respectively, relating to the settlement of prior years' Federal income tax returns. Gains on sales of investments include a 1994 gain of $27.0 on the sale of Grace's remaining interest in REG and a 1993 gain of $21.7 on the sale of a 50% interest in a Japanese chemical operation (see Note 3). Other, net in 1995 includes a $5.4 gain on the sale of Grace's transportation services business.

5. RESTRUCTURING COSTS AND ASSET IMPAIRMENTS

Restructuring Costs

During the third quarter of 1995, Grace began implementing a worldwide restructuring program aimed at streamlining processes and reducing general and administrative expenses, factory administration costs and noncore corporate research and development expenses. The program is expected to be substantially completed by the end of 1996. In the third and fourth quarters of 1995, Grace recorded pretax charges totalling $44.3 and $91.7 ($27.2 and $61.9 after-tax), respectively, comprised of $77.4 for employee termination benefits; $13.4 for plant closure and related costs, including lease termination costs; $15.5 for prior business exits and related costs; $20.8 for asset writedowns; and $8.9 for other costs. The $77.4 for employee termination benefits primarily represents severance pay and other benefits associated with the elimination of approximately 1,000 positions worldwide; more than 50% of the total cost reductions will come from corporate staff functions worldwide.

Through December 31, 1995, Grace recorded approximately $25.4 in costs against its 1995 restructuring reserve, of which $19.6 represented cash expenditures and $5.8 represented the noncash effects of asset writedowns and losses on asset sales. The $19.6 of cash expenditures were comprised of $13.0 in partial payments of employee termination benefits for over 500 employees, $3.0 for consulting services to develop the restructuring program, and $3.6 of other costs.

Asset Impairments

During 1995, Grace determined that, due to various events and changes in circumstances (including the worldwide restructuring program described above), certain long-lived assets and related goodwill were impaired. As a result, in the fourth quarter of 1995, Grace recorded a $43.5 pretax charge ($29.0 after-tax), the majority of which related to assets that will continue to be held and used in Grace's continuing operations; the charge included no significant individual components. Grace determined the amount of the charge based on various valuation techniques, including discounted cash flow, replacement cost and net realizable value for assets to be disposed of.

6. INCOME TAXES

Grace applies SFAS No. 109, "Accounting for Income Taxes," which uses an asset and liability approach requiring the recognition of deferred tax assets and liabilities with respect to the expected future tax consequences of events that have been recorded in the consolidated financial statements and tax returns. If it is more likely than not that all or a portion of a deferred tax asset will not be realized, a valuation allowance must be recognized.

The components of (loss)/income from continuing operations before income taxes and the related (benefit from)/provision for domestic and foreign taxes are as follows:

	1995	1994	1993
Domestic	**$(424.0)**	$(181.7)	$ (70.5)
Foreign	**111.6**	93.7	99.7
	$(312.4)	$ (88.0)	$ 29.2
Federal income taxes:			
Current	**$ 34.3**	$ (80.9)	$ (.6)
Deferred	**(160.0)**	(6.4)	(30.5)
State and local income taxes – current	**.7**	1.9	3.0
Foreign income taxes:			
Current	**61.0**	44.0	39.8
Deferred	**(51.8)**	(5.2)	(1.6)
	$(115.8)	$ (46.6)	$ 10.1

The components of (loss)/income from consolidated operations before income taxes and the related (benefit from)/provision for domestic and foreign taxes are as follows:

	1995	1994	1993
Domestic	**$(480.5)**	$ 44.3	$ (4.6)
Foreign	**72.7**	94.8	95.9
	$(407.8)	$ 139.1	$ 91.3
Federal income taxes:			
Current	**$ 105.6**	$ 25.3	$114.9
Deferred	**(226.3)**	(34.8)	(147.4)
State and local income taxes – current	**21.7**	21.8	32.7
Foreign income taxes:			
Current	**68.5**	49.1	44.4
Deferred	**(51.4)**	(5.6)	20.7
	$ (81.9)	$ 55.8	$ 65.3

The components of consolidated (benefit from)/provision for taxes are as follows:

	1995	1994	1993
Continuing operations	**$(115.8)**	$ (46.6)	$ 10.1
Discontinued operations:			
Operations	**82.6**	102.4	77.5
Loss on disposals of operations	**(48.7)**	–	(22.3)
	$ (81.9)	$ 55.8	$ 65.3

At December 31, 1995 and 1994, deferred tax assets and liabilities consisted of the following items:

	1995	1994
Reserves not yet deductible for tax purposes	**$223.6**	$254.4
Provision relating to net asbestos-related expenses	**219.4**	36.2
Research and development expenses	**115.8**	107.3
Postretirement benefits other than pensions	**88.9**	93.3
State deferred taxes	**70.1**	37.5
Pension and insurance reserves	**35.2**	14.8
Capitalized inventory costs and inventory reserves	**11.9**	15.3
Net operating loss carryforwards	**47.1**	54.4
Tax credit carryforwards	**27.2**	49.0
Other	**43.9**	54.4
Total deferred tax assets	**883.1**	716.6
Depreciation and amortization	**112.6**	167.4
Prepaid pension cost	**104.8**	72.3
Other	**20.1**	21.3
Total deferred tax liabilities	**237.5**	261.0
Valuation allowance for deferred tax assets	**97.7**	137.0
Net deferred tax assets	**$547.9**	$318.6

The valuation allowance shown above arises from uncertainty as to the realization of certain deferred tax assets, including U.S. tax credit carryforwards, state and local net operating loss carryforwards and net deferred tax assets. As a result of the favorable resolution of an audit, the valuation allowance on net operating loss carryforwards in foreign jurisdictions was reversed in 1995. Based upon anticipated future results, Grace has concluded, after consideration of the valuation allowance, that it is more likely than not that the remaining balance of the net deferred tax assets will be realized.

At December 31, 1995, there were $25.3 of tax credit carryforwards with expiration dates primarily through 1996 and $1.9 of tax credit carryforwards with no expiration. Additionally, there were state and local and foreign net operating loss carryforwards with a tax benefit of $47.1 and various expiration dates.

The U.S. Federal corporate tax rate reconciles to the effective tax rate for continuing operations as follows:

	1995	1994	1993
U.S. Federal corporate tax rate	**(35.0)%**	(35.0)%	35.0%
Increase/(decrease) in tax rate resulting from:			
Nontaxable income/nondeductible expenses	**(.7)**	(1.4)	(29.5)
Basis difference on sale of investment	**-**	(10.5)	-
State and local income taxes, net of U.S. Federal income tax benefit	**.2**	1.5	6.8
U.S. and foreign taxes on foreign operations	**9.8**	3	75.0
Utilization of general business credits	**(.5)**	(9.1)	(18.5)
Impact of U.S. and foreign tax rate changes on deferred taxes	**-**	-	(25.2)
Valuation allowance for deferred tax assets	**(14.4)**	-	(2.8)
Other, net	**3.5**	1.2	(6.2)
Effective tax rate	**(37.1)%**	(53.0)%	34.6%

U.S. and foreign taxes have not been provided on approximately $256.1 of undistributed earnings of certain foreign subsidiaries, as such earnings are expected to be retained indefinitely by such subsidiaries for reinvestment. The distribution of these earnings would result in additional foreign withholding taxes of approximately $14.9 and additional U.S. Federal income taxes to the extent they are not offset by foreign tax credits. It is not practicable to estimate the total tax liability that would be incurred upon such a distribution.

7. DISCONTINUED OPERATIONS

Health Care

In June 1995, the Company announced that its Board of Directors had approved a plan to spin off NMC. As a result, Grace classified its health care business as a discontinued operation in the second quarter of 1995 and, accordingly, NMC's operations are included in "(loss)/income from discontinued operations" in the Consolidated Statement of Operations.

Following NMC's receipt in October 1995 of five investigative subpoenas from the Office of the Inspector General of the U.S. Department of Health and Human Services (OIG), as discussed below, the completion of the spin-off of NMC, originally expected in the 1995 fourth quarter, was delayed.

In February 1996, Grace and Fresenius AG (Fresenius) entered into a definitive agreement to combine NMC with Fresenius' worldwide dialysis business (FWD) to create Fresenius Medical Care (FMC). As a result of the combination, FMC would acquire NMC, which would remain responsible for all liabilities arising out of the investigations, discussed below. However, Grace would retain certain health care assets, primarily a bioseparation sciences business, a health care services company and other assets (including cash and marketable securities).

The combination would follow a borrowing of approximately $2.3 billion by NMC, a tax-free distribution of the proceeds by NMC to Grace, and a tax-free distribution by the Company, with respect to each share of its Common Stock, of one share of a newly formed corporation holding all of Grace's businesses (principally its specialty chemicals businesses) other than NMC. As a result of the separation of Grace's specialty chemicals businesses from NMC and the subsequent combination of NMC and FWD, the holders of the Company's Common Stock would own 100% of the specialty chemicals company and 44.8% of FMC, and Fresenius and other shareholders would own 55.2% of FMC. The holders of the Company's Common Stock would also own preferred stock, the value of which would be linked to the performance of FMC. Completion of the various transactions is subject to customary conditions, including the approval of the shareholders of the Company and Fresenius; U.S., German and European regulatory actions; and obtaining financing on satisfactory terms. Commitments for financing have been received, and it is expected that the various transactions will be completed by the third quarter of 1996.

OIG Investigative Subpoenas

In October 1995, NMC received five investigative subpoenas from the OIG. The subpoenas call for the production of extensive documents relating to various aspects of NMC's business. A letter accompanying the subpoenas stated that they had been issued in conjunction with an investigation being conducted by the OIG, the U.S. Attorney for the District of Massachusetts and others, concerning possible violations of Federal laws relating to health care payments and reimbursements.

The five subpoenas cover the following areas: (a) NMC's corporate management, personnel and employees, organizational structure, financial information and internal communications; (b) NMC's dialysis services business, principally medical director contracts and compensation; (c) NMC's treatment of credit balances resulting from overpayments received under the Medicare end stage renal disease (ESRD) program and its payment of supplemental medical insurance premiums on behalf of indigent patients; (d) NMC's LifeChem laboratory business, including documents relating to testing procedures, marketing, customers, competition and certain overpayments totalling approximately $4.9 that were received by LifeChem from the Medicare program with respect to laboratory services rendered between 1989 and 1993; and (e) NMC's Homecare Division and, in particular, information concerning the intradialytic parenteral nutrition (IDPN) business described below, including billing practices related to various services, equipment and supplies and payments made to third parties as compensation for administering IDPN therapy.

The results of the investigation and its impact, if any, cannot be predicted at this time. In the event that a U.S. government agency believes that any wrongdoing has occurred, civil and/or criminal proceedings could be instituted, and if any such proceedings were to be instituted and the outcome were unfavorable, NMC could be subject to fines, penalties and damages or could become excluded from government reimbursement programs. Any such result could have a material adverse effect on NMC's financial position or the results of operations of NMC and Grace.

OBRA 93

The Omnibus Budget Reconciliation Act of 1993 (OBRA 93) affected the payment of benefits under Medicare and employer health plans for certain eligible ESRD patients. In July 1994, the Health Care Financing Administration (HCFA) issued an instruction to Medicare claims processors to the effect that Medicare benefits for the patients affected by OBRA 93 would be subject to a new 18-month "coordination of benefits" period. This instruction had a positive impact on NMC's dialysis revenues because, during the 18-month coordination of benefits period, the patient's employer health plan was responsible for payment, which was generally at a rate higher than that provided under Medicare.

In April 1995, HCFA issued a new instruction, reversing its original instruction in a manner that would substantially diminish the positive effect of the initial instruction on NMC's dialysis business. Under the new instruction, no 18-month coordination of benefits period would arise, and Medicare would remain the primary payor. HCFA further proposed that its new instruction be effective retroactive to August 1993, the effective date of OBRA 93. Consequently, NMC may be required to refund payments received from employer health plans for services provided after August 1993 under HCFA's original instruction and to re-bill Medicare for the same services, which would result in a cumulative reduction of net revenues to NMC totalling approximately $120.0 as of December 31, 1995. Effective July 1, 1995, NMC ceased to recognize the incremental revenue realized under the original instruction, which has resulted in a material reduction in NMC's operating earnings in comparison to prior periods in which NMC recognized such incremental revenue. However, NMC continued to bill the employer health plans as primary payors through December 31, 1995, at which time NMC commenced billing Medicare for the patients affected by OBRA 93.

In May 1995, NMC filed suit in the U.S. District Court for the District of Columbia seeking a declaratory judgment with respect to HCFA's instructions relating to OBRA 93. In June 1995, the court granted NMC's motion for a preliminary injunction to preclude HCFA from retroactively enforcing its new instruction. The litigation is continuing with respect to NMC's request to permanently enjoin HCFA's new instruction, both retroactively and prospectively. While there can be no assurance that a permanent injunction will be issued, NMC believes that it will ultimately prevail in its claim that the retroactive reversal by HCFA of its original instruction relating to OBRA 93 was impermissible under applicable law. If HCFA's revised instruction is upheld, NMC's business, financial position and results of operations would be materially adversely affected, particularly if the revised instruction is applied retroactively.

IDPN Therapy

NMC administers IDPN therapy to chronic dialysis patients who suffer from severe gastrointestinal malfunctions. Since late 1993, Medicare claims processors have applied medical coverage interpretations in a manner that has sharply reduced the number of IDPN claims approved for payment as compared to prior periods. NMC believes that the reduction in IDPN claims currently being paid by Medicare represents an unauthorized policy coverage change. Accordingly, NMC and other IDPN providers are pursuing various administrative and legal remedies, including administrative appeals, to address this reduction. In November 1995, NMC filed a complaint in the U.S. District Court for the Middle District of Pennsylvania seeking a declaratory judgment and injunctive relief to prevent the implementation of this policy coverage change.

NMC management believes that its IDPN claims are consistent with published Medicare coverage guidelines and ultimately will be approved for payment. Such claims represent substantial accounts receivable of NMC, amounting to approximately $93.0 and $28.0 as of December 31, 1995 and 1994, respectively, and currently increasing at the rate of approximately $5.0 per month. If NMC is unable to collect its IDPN receivable, or if IDPN coverage is reduced or eliminated, depending on the amount of the receivable that is not collected and/or the nature of the coverage change, NMC's business, financial position and results of operations could be materially adversely affected. In addition, a current draft of a new coverage policy would limit or preclude continued coverage of IDPN therapy and thereby have a material adverse effect on NMC's financial position and results of operations.

Other Legal Proceedings

NMC has received multiple subpoenas from a Federal grand jury in the District of New Jersey investigating, among other things, NMC's efforts to persuade the U.S. Food and Drug Administration to lift a January 1991 import hold issued with respect to NMC's Dublin, Ireland facility, whether NMC sold defective products, the manner in which NMC handled customer complaints and the development of a new dialyzer product line. Grace has also received two subpoenas relating to this investigation. In February 1996, the U.S. Attorney for the District of New Jersey notified NMC that it is a target of the New Jersey grand jury investigation, insofar as it relates to possible violations of Federal criminal law in connection with efforts to affect the January 1991 import hold referred to above; the material element of the import hold was lifted in 1992. In addition, in December 1994, a subsidiary of NMC received a subpoena from a Federal grand jury in the Eastern District of Virginia investigating the contractual relationships between subsidiaries of NMC that provide dialysis services and third parties that provide medical directorship and related services to those subsidiaries. The outcome of these investigations and their impact, if any, on NMC's business, financial condition and results of operations cannot be predicted at this time.

Cocoa, Battery Separators and Engineered Materials and Systems

In the second quarter of 1993, Grace classified as discontinued operations its cocoa business; its battery separators business; certain engineered materials businesses, principally its printing products, material technology and electromagnetic radiation control businesses (collectively, EMS); and other noncore businesses. At that time, a provision of $105.0 (net of an applicable tax benefit of $22.3) was recorded to reflect the losses expected on the divestment of these businesses.

During the fourth quarter of 1995, Grace revised the divestment plan for its cocoa business. The revised plan focuses on the improvement of operating cash flow through the adoption of new strategies and a new global organizational structure, while simultaneously positioning the business for sale. Grace expects to implement the revised plan and to conclude the sale of its cocoa business by the fourth quarter of 1996. As a result of this revised divestment plan, recent trends and a reassessment of forecasts for all remaining discontinued operations, Grace recorded an additional provision of $151.3 (net of an applicable tax benefit of $48.7) related to its remaining discontinued operations, principally the cocoa business.

During 1994, Grace sold its battery separators business and other EMS businesses for gross proceeds of $316.2, approximating prior estimates. In February 1995, Grace sold its composite materials business for gross proceeds of $3.0, leaving its microwave business as the only unsold EMS business.

Grace Energy

In 1994, Grace sold substantially all of its interests in Colowyo Coal Company (Colowyo), Grace's only remaining significant energy operation, for proceeds of $218.3, including $192.8 of proceeds from a nonrecourse financing secured by a portion of the revenues from certain long-term coal contracts. Grace retained a limited partnership interest in Colowyo, entitling it to share in the revenues from these coal contracts. In 1993, Grace sold substantially all of its oil and gas operations for net cash proceeds of $386.0. The total proceeds received from these divestments approximated prior estimates.

Other

In 1994, Grace sold its animal genetics and Caribbean fertilizer operations for proceeds of $44.1. These and other businesses were classified as discontinued operations in 1993. In 1993, Grace completed the sale of its minority interests in Canonie Environmental Services Corporation and Grace-Sierra Horticultural Products Company for total proceeds of $41.3.

Losses from Grace's discontinued operations, other than its discontinued health care operations, subsequent to their classification as such were $45.2, $14.2 and $54.6 in 1995, 1994 and 1993, respectively; these amounts have been charged against established reserves, including adjustments to those reserves in 1995. The sales and revenues and results of the discontinued health care operations for 1995, 1994 and 1993, and the 1993 sales and revenues and results of the other discontinued operations, prior to their classification as such, are as follows:

	1995	1994	1993
Health Care			
Sales and revenues	**$2,076.8**	$1,875.1	$1,512.9
Income from operations before taxes(1)	**$ 104.6**	$ 227.1	$ 192.0
Income tax provision	**82.6**	102.4	76.7
Income from discontinued operations	**$ 22.0**	$ 124.7	$ 115.3
Cocoa, Battery Separators and EMS			
Sales and revenues	**–**	–	$ 235.9
Loss from operations before taxes(1)	**–**	–	$ (.9)
Income tax provision	**–**	–	(1.1)
Loss from discontinued operations	**–**	–	$ (2.0)
Other			
Sales and revenues	**–**	–	$ 14.4
Loss from operations before taxes(1)	**–**	–	$ (1.7)
Income tax benefit	**–**	–	.3
Loss from discontinued operations	**–**	–	$ (1.4)
Total operating results of discontinued operations	**$ 22.0**	$ 124.7	$ 111.9
Net pretax loss on disposals of operations	**(200.0)**	–	(127.3)
Income tax benefit on disposals of operations	**48.7**	–	22.3
Total (loss)/income from discontinued operations	**$ (129.3)**	$ 124.7	$ 6.9

(1) Reflects an allocation of interest expense based on the ratio of the net assets of the businesses classified as discontinued operations as compared to Grace's total capital. The above operating results include interest expense allocations of $93.5, $60.4 and $43.9 for 1995, 1994 and 1993, respectively.

For financial reporting purposes, the assets, liabilities, results of operations and cash flows of Grace Cocoa Associates, L.P. (LP) (see Note 13) are included in Grace's consolidated financial statements as a component of discontinued operations, and the outside investors' interest in LP is reflected as a minority interest in the Consolidated Balance Sheet.

The net assets of Grace's remaining discontinued operations (excluding intercompany assets) at December 31, 1995 are as follows:

	Health Care	Cocoa	Other	Total
Current assets	$ 665.9	$280.4	$21.1	$ 967.4
Properties and equipment, net	399.3	193.8	21.9	615.0
Investments in and advances to affiliated companies	–	–	35.2	35.2
Other assets	993.7	62.2	18.0	1,073.9
Total assets	$2,058.9	$536.4	$96.2	$2,691.5
Current liabilities	$ 533.8	$193.1	$12.7	$ 739.6
Other liabilities	89.8	92.5	10.6	192.9
Total liabilities	$ 623.6	$285.6	$23.3	$ 932.5
Net assets	$1,435.3	$250.8	$72.9	$1,759.0

8. OTHER BALANCE SHEET ITEMS

	1995	1994
Notes and Accounts Receivable		
Trade receivables, less allowances of $12.8 (1994 – $95.1)	**$488.5**	$742.0
Notes receivable from insurance carriers – current, net of discounts of $4.3 in 1995	**62.0**	127.0
Other receivables, less allowances of $.1 (1994 – $.1)	**46.3**	106.7
	$596.8	$975.7
Inventories		
Raw and packaging materials	**$137.1**	$129.8
In process	**78.0**	75.3
Finished products	**248.6**	289.5
General merchandise	**76.6**	62.7
Less: Adjustment of certain inventories to a last-in/first-out (LIFO) basis	**(48.4)**	(43.1)
	$491.9	$514.2
Other Assets		
Prepaid pension costs	**$245.8**	$226.6
Patient relationships, less accumulated amortization of $117.2 in 1994	**–**	214.9
Deferred charges	**106.9**	124.9
Long-term receivables, less allowances of $24.7 (1994 – $20.6)	**83.5**	92.3
Long-term investments	**69.4**	79.3
Notes receivable from insurance carriers – noncurrent, net of discounts of $7.3 in 1995	**56.4**	60.0
Patents and licenses	**34.0**	39.9
Investments in and advances to affiliated companies	**17.4**	56.0
Other	**11.9**	76.9
	$625.3	$970.8

During 1995 and 1994, Grace entered into agreements to sell up to $120.0 and $320.0, respectively, of interests in designated pools of trade receivables (excluding $180.0 in 1995 pertaining to the discontinued health care operations). At December 31, 1995 and 1994, $116.0 and $296.8, respectively, had been received pursuant to such sales (excluding $179.8 in 1995 pertaining to the discontinued health care operations); these amounts are reflected as reductions to trade accounts receivable. Under the terms of these agreements, new interests in trade receivables are sold as collections reduce previously sold trade receivables. While only interests in designated pools of trade receivables are sold, the entire designated pools are available as the sole recourse with respect to the interests sold. There is no further recourse to Grace, nor is Grace required to repurchase any of the trade receivables in the pools. The costs related to such sales are expensed as incurred and recorded as interest expense and related financing costs. There were no gains or losses on these transactions.

Inventories valued at LIFO cost comprised 21.6% and 18.9% of total inventories at December 31, 1995 and 1994, respectively. The liquidation of prior years' LIFO inventory layers in 1995, 1994 and 1993 did not materially affect cost of goods sold in any of these years.

9. PROPERTIES AND EQUIPMENT

	1995	1994
Land	**$ 44.1**	$ 52.4
Buildings	**595.5**	698.3
Machinery, equipment and other	**1,967.1**	2,080.2
Projects under construction	**548.2**	397.4
Properties and equipment, gross	**3,154.9**	3,228.3
Accumulated depreciation and amortization	**(1,418.8)**	(1,498.2)
Properties and equipment, net	**$ 1,736.1**	$ 1,730.1

Interest costs are incurred in connection with the financing of certain assets prior to placing them in service. Interest costs capitalized in 1995, 1994 and 1993 were $21.3, $9.4 and $7.4, respectively.

Depreciation and lease amortization expense relating to properties and equipment amounted to $170.4, $158.0 and $146.3 in 1995, 1994 and 1993, respectively.

Grace's rental expense for operating leases amounted to $25.7, $28.8 and $34.3 in 1995, 1994 and 1993, respectively. See Note 12 for information regarding contingent rentals.

At December 31, 1995, minimum future payments for operating leases are:

1996	$ 28.0
1997	22.6
1998	19.0
1999	15.4
2000	14.5
Later years	26.8
Total minimum lease payments	$126.3

The above minimum lease payments reflect sublease income of $11.6 per year for 1996 through 2000 and a total of $28.0 in later years.

10. DEBT

	1995	1994
Short-Term Debt		
Bank borrowings (6.2% weighted average interest rate at year-end 1995)[1]	**$ 295.3**	$ -
Current maturities of long-term debt	**22.2**	166.6
Other short-term borrowings[2]	**320.8**	264.3
	$ 638.3	$ 430.9
Long-Term Debt		
Commercial paper (6.2% and 6.0% weighted average interest rates at year-end 1995 and 1994, respectively)[1]	**$ 45.7**	$ 5.5
Bank borrowings (6.2% and 5.8% weighted average interest rates at year-end 1995 and 1994, respectively)[1]	**304.3**	103.5
8.0% Notes Due 2004[3]	**300.0**	300.0
7.4% Notes Due 2000[4]	**287.0**	300.0
7.75% Notes Due 2002[5]	**131.0**	150.0
6.5% Notes Due 1995[6]	**-**	150.0
Term Loan Agreement (6.3% weighted average interest rate at year-end 1995)[7]	**30.0**	-
Medium-Term Notes, Series A (6.9% weighted average interest rate at year-end 1995 and 1994)[8]	**128.5**	128.5
Sundry indebtedness with various maturities through 2002	**91.2**	127.9
	1,317.7	1,265.4
Less current maturities of long-term debt	**22.2**	166.6
	$1,295.5	$1,098.8
Full-year weighted average interest rate on total debt[9]	**7.8%**	5.8%

[1] *Under bank revolving credit agreements in effect at year-end 1995, Grace may borrow up to $950.0 at interest rates based upon the prevailing prime, Federal funds and/or Eurodollar rates. Of that amount, $600.0 is available under short-term facilities, with $350.0 expiring on August 29, 1996 and $250.0 expiring on September 30, 1996; and $350.0 is available under a long-term facility expiring on September 1, 1999. These agreements also support the issuance of commercial paper and bank borrowings, $645.3 of which was outstanding at December 31, 1995 (included in Short-Term and Long-Term Debt above). At December 31, 1995, the aggregate amount of net unused and unreserved borrowings under the short-term and long-term facilities was $304.7. Grace's ability to borrow under the current facilities is subject to compliance with various covenants, including maintenance of ratios of total debt to total capitalization and interest coverage*

[a] Represents borrowings under various lines of credit and other miscellaneous borrowings, primarily of non-U.S. subsidiaries

[b] During the third quarter of 1994, Grace sold $300.0 of 8.0% Notes Due 2004 at an initial public offering price of 99.794% of par, to yield 8.03%. Interest is payable semiannually, and the Notes may not be redeemed prior to maturity

[c] During the first quarter of 1993, Grace sold at par $300.0 of 7.4% Notes Due 2000. Interest is payable semiannually, and the Notes may not be redeemed prior to maturity, however, Grace has repurchased Notes from time to time in response to unsolicited offers received through banks and brokers.

[d] During the third quarter of 1992, Grace sold at par $150.0 of 7.75% Notes Due 2002. Interest is payable semiannually, and the Notes may not be redeemed prior to maturity, however, Grace has repurchased Notes from time to time in response to unsolicited offers received through banks and brokers

[e] During the fourth quarter of 1992, Grace sold $150.0 of 6.5% Notes Due 1995 at an initial public offering price of 99.758% of par, to yield 6.59%. The Notes were paid at maturity in the fourth quarter of 1995

[f] During the second quarter of 1995, Grace entered into a three-year term loan agreement with a maturity date of April 24, 1998. The agreement provides for interest at a Eurodollar floating rate, with interest payable semiannually.

[g] During the second quarter of 1994, Grace entered into an agreement providing for the issuance and sale from time to time of its Medium-Term Notes, Series A (MTNs), with an aggregate issue price of up to $300.0. The MTNs may bear interest at either fixed or floating rates and have maturity dates more than nine months from their respective dates of issuance. Interest on each fixed rate MTN is payable semiannually, and interest on each floating rate MTN is payable as established at the time of issuance

[h] Computation includes interest expense allocated to discontinued operations

Payment of a majority of Grace's borrowings may be accelerated, and its principal borrowing agreements terminated, upon the occurrence of a default under certain Grace borrowings.

Scheduled maturities of long-term debt outstanding at December 31, 1995 are: 1996 – $22.2; 1997 – $113.2; 1998 – $46.4; 1999 – $351.2; 2000 – $350.3; and thereafter – $434.4.

Interest expense, excluding related financing costs and amounts allocated to discontinued operations, for 1995, 1994 and 1993 amounted to $53.3, $30.9 and $33.7, respectively. Including amounts allocated to discontinued operations, interest payments made in 1995, 1994 and 1993, excluding related financing costs, amounted to $183.1, $101.8 and $109.0, respectively.

A registration statement that became effective in 1994 covers $750.0 of debt and/or equity securities that may be sold from time to time. At December 31, 1995, $321.5 (including up to $171.5 of MTNs) remain available under the registration statement.

11. FINANCIAL INSTRUMENTS

Long-Term Debt/Interest Rate Agreements

To manage exposure to changes in interest rates, Grace enters into interest rate agreements, most of which have the effect of converting fixed-rate debt into variable-rate debt based on the London Interbank Offered Rate. At December 31, 1995 and 1994, the notional amounts of Grace's interest rate swaps consist of the following: $1,219.5 and $1,013.5, respectively, which convert fixed-rate debt into variable-rate debt; and $626.0 and $1,200.0, respectively, which convert variable-rate debt into fixed-rate debt. Notional amounts do not quantify risk or represent assets or liabilities of Grace, but are used in the calculation of cash settlements under the agreements.

Grace's debt and interest rate management objective is to reduce its cost of funding over the long term, considering economic conditions and their potential impact on Grace. The strategy emphasizes improving liquidity by developing and maintaining access to a variety of long-term and short-term capital markets. Grace enters into standard interest rate swaps that have readily identifiable impacts on interest cost and are characterized by broad market liquidity. Grace is not a party to leveraged interest rate agreements.

During 1995 and 1994, Grace realized (negative)/positive cash flows of $(16.5) and $10.0, respectively, from interest rate agreements. Realized gains and losses on interest rate agreements are amortized to interest expense over a period relevant to the agreement (1 – 10 years); at December 31, 1995 and 1994, unamortized net gains were $31.7 and $43.0, respectively. At December 31, 1995 and 1994, Grace would have been required to pay $32.5 and $118.1, respectively, to retire these agreements. The maturities and notional amounts of the swaps closely match underlying debt instruments. This will result in the changes in the fair value of swaps being substantially offset by changes in the fair value of the debt.

Fair Value of Financial Instruments

At December 31, 1995 and 1994, the recorded value of financial instruments such as cash, short-term investments, trade receivables and payables and short-term debt approximated their fair values, based on the short-term maturities and floating rate characteristics of these instruments. Additionally, the recorded value of both long-term investments and receivables approximated fair values. At December 31, 1995 and 1994, the fair value of long-term debt was $1,361.1 and $1,212.1, respectively. Fair value is determined based on expected future cash flows (discounted at market interest rates), quotes from financial institutions and other appropriate valuation methodologies. Grace does not hold or issue financial instruments for trading purposes.

Foreign Currency Contracts

Grace conducts business in a wide variety of currencies and consequently enters into foreign exchange forward and option contracts to manage its exposure to fluctuations in foreign currency exchange rates. These contracts generally involve the exchange of one currency for another at a future date. At December 31, 1995 and 1994, Grace had notional principal amounts of approximately $45.5 and $10.0, respectively, in contracts to buy or sell foreign currency in the future. The recorded values at December 31, 1995 and 1994, which approximated fair value based on exchange rates at December 31, 1995 and 1994, were not significant.

Credit Risk

Grace is exposed to credit risk to the extent of potential nonperformance by counterparties on financial instruments. The counterparties to Grace's interest rate swap agreements and currency exchange contracts comprise a diversified group of major financial institutions, all of which are rated investment grade. Credit risk is further reduced by bilateral netting agreements between Grace and its counterparties. As of December 31, 1995, Grace's credit exposure was insignificant and limited to the fair value stated above; Grace believes the risk of incurring losses due to credit risk is remote.

Market Risk

Exposure to market risk on financial instruments results from fluctuations in interest and currency rates during the periods in which the contracts are outstanding. The mark-to-market valuations of interest rate, foreign currency agreements and of associated underlying exposures are closely monitored at all times. Grace uses portfolio sensitivities and stress tests to monitor risk. Overall financial strategies and the effects of using derivatives are reviewed periodically.

12. COMMITMENTS AND CONTINGENT LIABILITIES

Grace is the named tenant or guarantor with respect to certain leases entered into by previously divested businesses. The leases, some of which extend through the year 2015, have future minimum lease payments aggregating $121.6 (including leases assigned to the previously divested Hermans business having future minimum lease payments of $14.6), offset by $119.8 of future minimum rental income from tenants and subtenants.

In addition, Grace is the named tenant or guarantor with respect to leases entered into by a previously divested home center business that had been rejected in bankruptcy. These leases have future minimum lease payments of $47.0, fully offset by $48.5 of future minimum rental income from tenants and subtenants

Grace is also contingently liable with respect to leases entered into by REG's subsidiaries. After undergoing a reorganization in 1993, REG (now named Family Restaurants, Inc.) has agreed to indemnify Grace with respect to these leases. At December 31, 1995, these leases have future minimum lease payments of $64.2, fully offset by future minimum rental income from tenants and subtenants.

Grace believes that the risk of significant loss from the above lease obligations is remote, except that Grace may incur losses relating to the Hermans and REG leases as the result of recent developments. The likelihood and amounts of these losses cannot be reasonably estimated. In addition, Grace is liable for other expenses (primarily property taxes) relating to the above leases; these expenses are paid by the tenants and subtenants.

Grace is subject to loss contingencies resulting from environmental laws and regulations that, among other things, impose obligations to remove or mitigate the effects on the environment of the disposal or release of substances at various sites. Grace accrues for anticipated costs associated with investigatory and remediation efforts where an assessment has indicated that a loss is probable and can be reasonably estimated. At December 31, 1995, Grace's liability for environmental investigatory and remediation costs related to continuing and discontinued operations totalled approximately $280.3, as compared to $216.0 at December 31, 1994. The principal reason for this increase is a change in the estimated costs of remediation at former manufacturing sites.

In 1995 and 1994, periodic provisions were recorded for environmental and plant closure expenses, which include the costs of future environmental investigatory and remediation activities. Additionally, in the fourth quarter of 1995 and first quarter of 1994, Grace recorded pretax provisions of $77.0 and $40.0 ($50.0 and $26.0 aftertax), respectively, principally to provide for future costs related to remediation activities required at former manufacturing sites. These provisions are included in the Consolidated Statement of Operations as part of cost of goods sold and operating expenses. In 1995, 1994 and 1993, Grace incurred costs of $31.3, $30.8 and $44.4, respectively, to remediate its environmentally impaired sites. These amounts have been charged against the previously established reserves. Future cash outlays for remediation costs are expected to total $30.0 in 1996 and $20.0 in 1997. Grace considers its current reserves to be adequate to cover its environmental liabilities. Additionally, Grace's classification between current and noncurrent liabilities with respect to its environmental reserves is considered appropriate in relation to expected future cash outlays.

Grace's environmental liabilities are reassessed whenever circumstances become better defined and/or remediation efforts and their costs can be better estimated. The measurement of the liability is evaluated quarterly based on currently available information, including the progress of remedial investigation at each site, the current status of discussions with regulatory authorities regarding the method and extent of remediation at each site, and the apportionment of costs among potentially responsible parties. As some of these issues are decided (the outcome of which is subject to various uncertainties) and/or new sites are assessed and costs can be reasonably estimated, Grace will continue to review and analyze the need for adjustments to the recorded accruals.

See Note 7 for a discussion of commitments and contingent liabilities pertaining to NMC.

13. MINORITY INTEREST

Minority interest consists of a limited partnership interest in LP. The total capital of LP at December 31, 1995 was approximately $1,488.0. LP's assets consist of Grace Cocoa's worldwide cocoa and chocolate business, long-term notes and demand loans due from various Grace entities and guaranteed by the Company and its principal operating subsidiary, and cash. Grace had $347.0 of borrowings from LP at December 31, 1995. Four Grace entities serve as general partners of LP and own general partnership interests totalling 79.03% in LP; the sole limited partner of LP, which initially acquired its interest in LP in exchange for a $300.0 cash capital contribution ($297.0 of which was funded by outside investors), owns a 20.97% limited partnership interest in LP. LP is a separate and distinct legal entity from each of the Grace entities and has separate assets, liabilities, business functions and operations. For financial reporting purposes, the assets, liabilities, results of operations and cash flows of LP are included in Grace's consolidated financial statements as a component of discontinued operations and the outside investors' interest in LP is reflected as a minority interest.

14. SHAREHOLDERS' EQUITY

The weighted average number of shares of common stock outstanding during 1995 was 95,822,000 (1994 – 93,936,000; 1993 – 91,461,000).

The Company is authorized to issue 300,000,000 shares of common stock. Of the common stock unissued at December 31, 1995, approximately 7,655,000 shares were reserved for issuance pursuant to stock options and other stock incentives. In addition, at December 31, 1995, approximately 105,084,000 shares were reserved for issuance under Common Stock Purchase Rights (Rights). A Right is issued for each outstanding share of common stock; the Rights are not and will not become exercisable unless and until certain events occur, and at no time will the Rights have any voting power.

Preferred stocks authorized, issued and outstanding are:

	Shares as of December 31, 1995			Par Value of Shares Outstanding		
	Authorized and Issued	In Treasury	Outstanding	**1995**	1994	1993
6% Cumulative[1]	40,000	3,540	36,460	**$3.6**	$3.6	$3.6
8% Cumulative Class A[2]	50,000	33,644	16,356	**1.6**	1.6	1.6
8% Noncumulative Class B[2]	40,000	18,423	21,577	**2.2**	2.2	2.2
				$7.4	$7.4	$7.4

[1] 160 votes per share.
[2] 16 votes per share.

Dividends paid on the preferred stocks amounted to $.5 in each of 1995, 1994 and 1993.

The Certificate of Incorporation also authorizes 5,000,000 shares of Class C Preferred Stock, $1 par value, none of which has been issued.

15. STOCK INCENTIVE PLANS

Stock options are granted under the Company's stock incentive plans. Each option has an exercise price equal to the fair market value of the Company's Common Stock on the date of grant. Options become exercisable at the time or times determined by the Compensation Committee and may have terms of up to ten years and one month.

Changes in outstanding common stock options are summarized below:

	1995		1994		1993	
	Number of Shares	**Average Exercise Price**	Number of Shares	Average Exercise Price	Number of Shares	Average Exercise Price
Balance at beginning of year	**7,612,888**	**$38.08**	6,965,304	$36.48	6,365,187	$35.09
Options granted	**1,704,150**	**46.66**	1,358,900	42.27	1,461,425	38.00
	9,317,038		8,324,204		7,826,612	
Options exercised	**(3,551,123)**	**38.30**	(606,444)	29.21	(683,255)	25.89
Options terminated or canceled	**(71,719)**	**42.27**	(104,872)	37.33	(178,053)	40.13
Balance at end of year	**5,694,196**	**40.45**	7,612,888	38.08	6,965,304	36.48

At December 31, 1995, options covering 4,172,391 shares (1994 – 5,633,761; 1993 – 5,056,256) were exercisable and 1,913,163 shares (1994 – 3,547,094; 1993 – 1,804,122) were available for additional grants. Currently outstanding options expire on various dates between February 1996 and July 2005.

Grace will adopt the disclosure requirements of SFAS No. 123, "Accounting for Stock-Based Compensation" in 1996. However, Grace anticipates that it will continue to follow the measurement provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," as permitted by SFAS No. 123.

16. PENSION PLANS

Grace maintains defined benefit pension plans covering employees of certain units who meet age and service requirements. Benefits are generally based on final average salary and years of service. Grace funds its U.S. pension plans in accordance with Federal laws and regulations. Non-U.S. pension plans are funded under a variety of methods because of differing local laws and customs and therefore cannot be summarized. Approximately 60% of U.S. and non-U.S. plan assets at December 31, 1995 were common stocks, with the remainder primarily fixed income securities.

Pension cost/(benefit) is comprised of the following components:

	1995		1994		1993	
	U.S.	**Non-U.S.**	U.S.	Non-U.S.	U.S.	Non-U.S.
Service cost on benefits earned during the year	**$ 14.6**	**$ 10.5**	$ 19.8	$ 13.4	$ 12.7	$ 9.5
Interest cost on benefits earned in prior years	**50.6**	**21.4**	46.9	19.3	33.8	17.1
Actual (return)/loss on plan assets	**(132.3)**	**(52.0)**	16.9	10.6	(101.7)	(56.7)
Deferred loss/(gain) on plan assets	**71.1**	**26.2**	(84.6)	(37.4)	55.1	36.0
Amortization of net gains and prior service costs	**(.8)**	**(.8)**	(7.1)	(1.6)	(4.9)	(1.7)
Net pension cost/(benefit)	**$ 3.2**	**$ 5.3**	$ (8.1)	$ 4.3	$ (5.0)	$ 4.2

The funded status of these plans was as follows:

	U.S.				**Non-U.S.**			
	Assets Exceed Accumulated Benefits		Accumulated Benefits Exceed Assets		Assets Exceed Accumulated Benefits		Accumulated Benefits Exceed Assets	
	1995	1994	**1995**	1994	**1995**	1994	**1995**	1994
Actuarial present value of benefit obligation:								
Vested	**$679.6**	$536.2	**$ 52.0**	$ 39.0	**$133.5**	$114.2	**$ 67.5**	$ 57.2
Accumulated benefit obligation	**$680.4**	$540.8	**$ 52.0**	$ 39.0	**$133.9**	$115.3	**$ 75.1**	$ 64.4
Total projected benefit obligation	**$710.0**	$596.3	**$ 55.7**	$ 40.4	**$189.4**	$158.5	**$ 92.4**	$ 81.8
Plan assets at fair value	**795.8**	751.6	**-**	-	**302.5**	255.8	**7.3**	12.5
Plan assets in excess of/(less than) projected benefit obligation	**85.8**	155.3	**(55.7)**	(40.4)	**113.1**	97.3	**(85.1)**	(69.3)
Unamortized net (gain)/loss at initial adoption	**(73.7)**	(89.5)	**4.9**	5.6	**(6.3)**	(8.4)	**4.5**	4.6
Unamortized prior service cost	**41.7**	13.0	**16.3**	18.3	**3.6**	4.0	**-**	-
Unrecognized net loss/(gain)	**97.6**	62.3	**8.6**	1.1	**(16.0)**	(7.4)	**(3.2)**	(5.6)
Prepaid/(accrued) pension cost	**$151.4**	$141.1	**$(25.9)**	$(15.4)	**$ 94.4**	$ 85.5	**$(83.8)**	$(70.3)

The following significant assumptions were used in 1995, 1994 and 1993:

	1995		1994		1993	
	U.S.	**Non-U.S.**	U.S.	Non-U.S.	U.S.	Non-U.S.
Discount rate at December 31,	**7.25%**	**5.1 – 11.6%**	8.5%	5.0 – 12.0%	7.5%	4.5 – 9.2%
Expected long-term rate of return	**9.0**	**6.0 – 10.5**	9.0	6.0 – 10.5	9.0	6.0 – 10.5
Rate of compensation increase	**4.5**	**4.0 – 7.5**	5.5	4.0 – 7.5	5.5	3.5 – 7.5

Grace's Retirement Plan for Salaried Employees (Plan) contains provisions under which the Plan would automatically terminate in the event of a change in control of the Company, and Plan benefits would be secured through the purchase of annuity contracts. Upon such termination, a portion of the Plan's excess assets would be placed in an irrevocable trust to fund various employee benefit plans and arrangements of Grace, and any balance would be returned to Grace.

During 1995, Grace approved a cost-of-living increase, effective January 1, 1996, for retirees under the Plan and Grace's Retirement Plan for Hourly Employees of Canadian subsidiaries.

17. OTHER POSTRETIREMENT BENEFIT PLANS

Grace provides certain other postretirement health care and life insurance benefits for retired employees of specified U.S. units. These retiree medical and life insurance plans provide various levels of benefits to employees (depending on their date of hire) who retire from Grace after age 55 with at least 10 years of service. The plans are currently unfunded.

Grace applies SFAS No. 106, which requires the accrual method of accounting for the future costs of postretirement health care and life insurance benefits over the employees' years of service. Grace pays the costs of postretirement benefits as they are incurred.

Included in other liabilities as of December 31, 1995 and 1994 are the following:

	1995	1994
Accumulated postretirement benefit obligation:		
Retirees	**$209.0**	$192.6
Fully eligible participants	**15.2**	12.1
Active ineligible participants	**34.4**	26.3
Accumulated postretirement benefit obligation	**258.6**	231.0
Unrecognized net loss	**(54.9)**	(28.5)
Unrecognized prior service benefit	**44.3**	48.6
Accrued postretirement benefit obligation	**$248.0**	$251.1

Net periodic postretirement benefit cost for the years ended December 31, 1995, 1994 and 1993 is comprised of the following components:

	1995	1994	1993
Service cost	**$ 1.6**	$ 2.1	$ 2.2
Interest cost on accumulated postretirement benefit obligation	**18.3**	16.2	13.2
Amortization of net loss	**.2**	1.2	.2
Amortization of prior service benefit	**(4.3)**	(4.3)	(4.5)
Net periodic postretirement benefit cost	**$15.8**	$15.2	$11.1

During 1992, Grace's retiree medical plans were amended to increase cost sharing by employees retiring after January 1, 1993. This amendment decreased the accumulated postretirement benefit obligation by $44.3 at December 31, 1995 and will be amortized over an average remaining future service life of approximately 11 years.

Medical care cost trend rates were projected at 10.7% in 1995, declining to 6.0% through 2003 and remaining level thereafter. A one percentage point increase in each year's assumed medical care cost trend rate, holding all other assumptions constant, would increase the annual net periodic postretirement benefit cost by $2.5 and the accumulated postretirement benefit obligation by $20.2. The discount rates at December 31, 1995, 1994 and 1993 were 7.25%, 8.5% and 7.5%, respectively.

Effective January 1, 1994, Grace adopted SFAS No. 112, "Employers' Accounting for Postemployment Benefits," which requires accrual accounting for nonaccumulating postemployment benefits. Grace's primary postemployment obligation is for disabled workers' medical benefits. These are currently included in accrued postretirement costs under SFAS No. 106. The adoption of SFAS No. 112 did not have a material effect on Grace's results of operations or financial position.

18. GEOGRAPHIC AREA INFORMATION

The table below presents information related to Grace's specialty chemicals segment (its only industry segment) by geographic area for the years 1995-1993.

		United States	Canada	Europe	Asia Pacific	Latin America	Total
Sales and revenues	**1995**	**$1,693**	**$128**	**$1,147**	**$445**	**$253**	**$3,666**
	1994	1,558	121	955	366	218	3,218
	1993	1,432	123	852	307	182	2,896
Pretax operating (loss)/income[1]	**1995**	**(120)**	**23**	**39**	**62**	**10**	**14**
	1994	(133)	9	69	56	20	21
	1993	23	7	38	44	13	125
Identifiable assets[2]	**1995**	**2,031**	**101**	**998**	**411**	**246**	**3,787**
	1994	1,796	83	905	308	208	3,300
	1993	2,042	81	720	243	154	3,240

Pretax operating income and total identifiable assets for the specialty chemicals segment are reconciled below to income from continuing operations before income taxes and consolidated total assets, respectively, as presented in the Consolidated Statement of Operations and the Consolidated Balance Sheet. Grace allocates to its specialty chemicals segment general corporate overhead expenses, general corporate research expenses and certain other income and expense items that can be identified with specialty chemicals operations.

	1995	1994	1993
Pretax operating income – specialty chemicals segment[1]	**$ 14**	$ 21	$ 125
Interest expense and related financing costs	**(71)**	(50)	(43)
Corporate restructuring costs and asset impairments/other activities	**(122)**	–	–
Provisions relating to environmental liabilities at former manufacturing sites	**(77)**	(40)	–
Provision for corporate governance	**(30)**	–	–
Gain on sale of remaining interest in REG	**–**	27	–
Corporate expenses previously allocated to health care operations[3]	**(38)**	(37)	(37)
Other income/(expenses), net	**12**	(9)	(16)
(Loss)/income from continuing operations before income taxes	**$ (312)**	$ (88)	$ 29
Identifiable assets – specialty chemicals segment[2]	**$3,787**	$3,300	$3,240
General corporate assets[4]	**752**	860	811
Discontinued operations' net assets	**1,759**	2,071	2,058
Total assets	**$6,298**	$6,231	$6,109

[1] Includes (a) 1995, 1994 and 1993 pretax provisions of $275, $316 and $159, respectively, relating to asbestos-related liabilities and insurance coverage (see Note 2 for further information), and (b) a 1995 pretax charge of $98 relating to restructuring costs, asset impairments and other costs (see Note 5 for further information).

[2] Includes asbestos-related receivables and settlements due from insurance carriers, net of discounts, of $321 and $118, respectively, in 1995, $513 and $187, respectively, in 1994, and $962 and $114, respectively, in 1993.

[3] These costs will not be assumed by NMC following the completion of its proposed separation from Grace, and it is expected that these costs will be eliminated.

[4] General corporate assets consist principally of deferred tax assets, prepaid pension costs, and corporate receivables and investments.

19. SUBSEQUENT EVENTS

As more fully discussed in Note 7, in February 1996, Grace and Fresenius entered into a definitive agreement to combine NMC with Fresenius' worldwide dialysis business. The transaction is expected to be completed by the third quarter of 1996.

In March 1996, Grace announced that it had entered into a definitive agreement to sell its Grace Dearborn water treatment and process chemicals business to Betz Laboratories, Inc. for $632.0. The transaction is expected to be completed in the second quarter of 1996.

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

Management is responsible for the preparation, as well as the integrity and objectivity, of the consolidated financial statements and other financial information included in this report. Such financial information has been prepared in conformity with generally accepted accounting principles and accordingly includes certain amounts that represent management's best estimates and judgments.

For many years, management has maintained internal control systems to assist it in fulfilling its responsibility for financial reporting, including careful selection of personnel; segregation of duties; formal business, accounting and reporting policies and procedures; and an internal audit function. While no system can ensure elimination of all errors and irregularities, Grace's systems, which are reviewed and modified in response to changing conditions, have been designed to provide reasonable assurance that assets are safeguarded, policies and procedures are followed and transactions are properly executed and reported. The concept of reasonable assurance is based on the recognition that there are limitations in all systems and that the cost of such systems should not exceed the benefits to be derived.

The Audit Committee of the Board of Directors, which is comprised of directors who are neither officers nor employees of nor consultants to Grace, meets regularly with Grace's senior financial personnel, internal auditors and independent certified public accountants to review audit plans and results as well as the actions taken by management in discharging its responsibilities for accounting, financial reporting and internal control systems. The Audit Committee reports its findings, and recommends the selection of independent certified public accountants, to the Board of Directors. Grace's management, internal auditors and independent certified public accountants have direct and confidential access to the Audit Committee at all times.

The independent certified public accountants are engaged to conduct the audits of and render a report on the consolidated financial statements in accordance with generally accepted auditing standards. These standards require a review of the systems of internal controls and tests of transactions to the extent considered necessary by the independent certified public accountants for purposes of supporting their opinion as set forth in their report.

Albert J. Costello
Chairman, President and Chief Executive Officer

Peter D. Houchin
Senior Vice President and Chief Financial Officer

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Price Waterhouse LLP
One East Broward Boulevard
Ft. Lauderdale, FL 33301

January 31, 1996

To the Shareholders and Board of Directors of W. R. Grace & Co.
In our opinion, the consolidated financial statements appearing on pages 24 through 49 of this report present fairly, in all material respects, the financial position of W. R. Grace & Co. and subsidiaries (Grace) at December 31, 1995 and 1994, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1995, in conformity with generally accepted accounting principles. These financial statements are the responsibility of Grace's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with generally accepted auditing standards which 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

Price Waterhouse LLP

QUARTERLY SUMMARY AND STATISTICAL INFORMATION

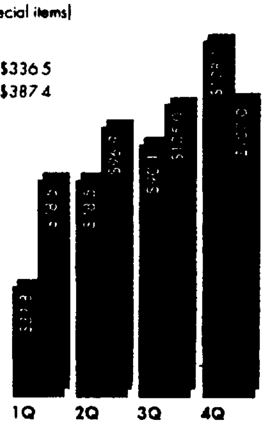
Unaudited — dollars in millions, except per share

Quarter Ended	1Q	2Q	3Q	4Q
1995				
Total sales and revenues	**$853.4**	**$ 932.3**	**$946.4**	**$ 933.4**
Cost of goods sold and operating expenses	**500.9**	**550.7**	**566.0**	**626.1**
Net income/(loss)	**47.5**[3]	**78.7**	**21.7**[4]	**(473.8)**[5]
Earnings/(loss) per share:[1]				
Net earnings/(loss)	**$ .50**	**$ .83**	**$ .22**	**$ (4.87)**
Fully diluted earnings per share:				
Net earnings/(loss)	**$ .49**	**$ .80**	**$ .22**	**$ —**[6]
Dividends declared per common share	**$ .35**	**$ .35**	**$ .35**	**$ .125**
Market price of common stock:[2]				
High	**$ 54½**	**$ 65⅜**	**$ 71¾**	**$ 66¾**
Low	**38½**	**51⅜**	**61⅜**	**54⅜**
Close	**53¾**	**61⅜**	**66⅜**	**59⅜**
1994[7]				
Total sales and revenues	$675.4	$ 782.9	$815.5	$ 944.4
Cost of goods sold and operating expenses	437.8	464.5	475.0	523.5
Net income/(loss)	38.2[8]	(134.3)[9]	76.0	103.4
Earnings/(loss) per share:[1]				
Net earnings/(loss)	$ .41	$ (1.43)	$ .81	$ 1.10
Fully diluted earnings per share:				
Net earnings/(loss)	$ .40	$ —[6]	$ .80	$ 1.09
Dividends declared per common share	$ .35	$ .35	$ .35	$ .35
Market price of common stock:[2]				
High	$ 46½	$ 43	$ 42⅜	$ 41⅜
Low	40⅜	39	38¼	36
Close	41¼	39⅞	41⅛	38⅜

[1] *Per share results for the four quarters differ from full-year per share results, as a separate computation of earnings per share is made for each quarter presented.*
[2] *Principal market: New York Stock Exchange.*
[3] *Includes a $12.5 charge for matters relating to corporate governance.*
[4] *Includes a $27.1 charge for restructuring costs; a $6.1 charge for matters relating to corporate governance; and a $33.5 charge to the discontinued health care operations, primarily relating to asset impairments.*
[5] *Includes a $178.7 provision relating to asbestos-related liabilities and insurance coverage, a $50.0 provision for environmental liabilities, a $116.9 charge for restructuring costs, asset impairments and other items; a $151.3 provision for other discontinued operations, and a $68.9 charge to the discontinued health care operations, primarily relating to asset impairments and other items.*
[6] *Not presented as the effect is anti-dilutive.*
[7] *Certain amounts have been reclassified to conform to the 1995 presentation.*
[8] *Includes a $27.0 gain on the sale of Grace's remaining interest in The Restaurant Enterprises Group, Inc. (REG), offset by a $26.0 provision, primarily for environmental liabilities.*
[9] *Includes a $200.0 reinstatement of a provision relating to asbestos-related insurance coverage.*

Specialty Chemicals Pretax Operating Income
(before special items)
($ millions)

■ 1994–$336.5
■ 1995–$387.4



CAPITAL EXPENDITURES, NET FIXED ASSETS AND DEPRECIATION AND LEASE AMORTIZATION

Dollars in millions

	Capital Expenditures[1]			Net Fixed Assets			Depreciation and Lease Amortization[2]		
	1995	1994	1993	**1995**	1994	1993	**1995**	1994	1993
Operating Group									
Specialty chemicals	**$459**	$329	$209	**$1,581**	$1,262	$1,049	**$155**	$144	$135
General corporate	**49**	30	21	**155**	144	128	**15**	14	11
Total continuing operations	**508**	359	230	**1,736**	1,406	1,177	**170**	158	146
Discontinued operations	**30**	86	80	**-**	324	277	**-**	-	-
Total	**$538**	$445	$310	**$1,736**	$1,730	$1,454	**$170**	$158	$146
Geographic Location									
United States and Canada	**$246**	$202	$126	**$ 869**	$ 714	$ 608	**$ 75**	$ 77	$ 74
Europe	**100**	75	57	**441**	382	321	**59**	51	46
Other areas	**113**	52	26	**271**	166	120	**21**	16	15
Subtotal	**459**	329	209	**1,581**	1,262	1,049	**155**	144	135
General corporate	**49**	30	21	**155**	144	128	**15**	14	11
Total continuing operations	**508**	359	230	**1,736**	1,406	1,177	**170**	158	146
Discontinued operations	**30**	86	80	**-**	324	277	**-**	-	-
Total	**$538**	$445	$310	**$1,736**	$1,730	$1,454	**$170**	$158	$146

[1] Excludes capital expenditures of discontinued operations subsequent to their classification as such.
[2] Certain 1994 and 1993 amounts have been reclassified to conform to the 1995 presentation.

FINANCIAL SUMMARY[1]

Dollars in millions except per share amounts

	1995	1994	1993	1992	1991
Statement of Operations					
Sales and revenues	**$ 3,665.5**	$3,218.2	$2,895.5	$3,061.8	$3,326.2
Cost of goods sold and operating expenses	**2,243.7**	1,900.8	1,746.7	1,871.8	2,027.9
Depreciation and amortization	**186.3**	165.0	153.5	164.5	178.3
Interest expense and related financing costs	**71.3**	49.5	42.9	49.4	73.7
Research and development expenses	**120.6**	106.8	111.5	105.2	102.0
(Loss)/income from continuing operations before income taxes	**(312.4)**	(88.0)	29.2	81.3	256.5
(Benefit from)/provision for income taxes	**(115.8)**	(46.6)	10.1	79.9	99.1
Income from continuing operations before special items[2]	**194.7**	157.6	119.1	146.5	153.9
(Loss)/income from continuing operations	**(196.6)**	(41.4)	19.1	1.4	157.4
(Loss)/income from discontinued operations[3]	**(129.3)**	124.7	6.9	(105.9)	61.2
Cumulative effect of accounting changes	**-**	-	-	(190.0)	-
Net (loss)/income	**(325.9)**	83.3	26.0	(294.5)	218.6
Financial Position					
Current assets	**$ 1,681.3**	$2,228.9	$2,077.6	$2,091.4	$1,990.0
Current liabilities	**2,214.2**	2,231.5	1,992.6	1,639.6	1,622.1
Properties and equipment, net	**1,736.1**	1,730.1	1,454.1	1,707.9	2,558.2
Total assets	**6,297.6**	6,230.6	6,108.6	5,598.6	6,007.1
Total debt	**1,933.8**	1,529.7	1,706.1	1,819.2	2,259.4
Shareholders' equity – common stock	**1,224.4**	1,497.1	1,510.2	1,537.5	2,017.7
Data Per Common Share					
Earnings from continuing operations before special items[2]	**$ 2.03**	$ 1.68	$ 1.30	$ 1.63	$ 1.76
(Loss)/earnings from continuing operations	**(2.05)**	(.45)	.20	.01	1.80
Cumulative effect of accounting changes	**-**	-	-	(2.12)	-
Net (loss)/earnings	**(3.40)**	.88	.28	(3.29)	2.50
Dividends	**1.175**	1.40	1.40	1.40	1.40
Book value	**12.57**	15.91	16.16	17.10	22.77
Average common shares outstanding *(thousands)*	**95,822**	93,936	91,461	89,543	87,236
Other Statistics					
Dividends paid on common stock	**$ 112.1**	$ 131.5	$ 127.9	$ 125.4	$ 122.0
Capital expenditures	**537.6**	444.6	309.6	398.4	447.0
% Total debt to total capital	**61.1%**	50.4%	52.9%	54.1%	52.7%
Common shareholders of record	**19,496**	18,501	19,358	20,869	21,949
Common stock price range	**71¼ – 38½**	46¼ – 36	41¼ – 34⅜	45 – 32	40¼ – 23⅜
Number of employees – continuing operations *(thousands)*	**21.2**	20.6	20.4	20.0	21.5

[1] Certain prior year amounts have been reclassified to conform to the 1995 presentation

[2] Income from continuing operations before special items reconciles to (loss)/income from continuing operations as follows:

	1995	1994	1993	1992	1991
Income from continuing operations before special items	**$ 194.7**	$ 157.6	$ 119.1	$ 146.5	$153.9
Special items (after-tax):					
Provision for corporate governance	**(18.6)**	-	-	-	-
Gain on sale of remaining interest in REG	-	27.0	-	-	-
Restructuring costs and asset impairments/other activities	**(144.0)**	-	-	-	-
Provisions for environmental liabilities at former manufacturing sites	**(50.0)**	(26.0)	-	-	-
Provision relating to a fumed silica plant	-	-	-	(140.0)	-
Postretirement benefits prior to plan amendments	-	-	-	(5.1)	-
Strategic restructuring gain	-	-	-	-	3.5
Provisions relating to asbestos-related liabilities and insurance coverage	**(178.7)**	(200.0)	(100.0)	-	-
(Loss)/income from continuing operations	**$(196.6)**	$ (41.4)	$ 19.1	$ 1.4	$157.4

The special items included in the foregoing table have also been excluded in determining earnings per common share from continuing operations before special items

[3] Includes income of $22.0, $124.7 and $115.3 in 1995, 1994 and 1993, respectively, from the discontinued health care operations. 1995 health care results reflect special charges totaling $102.4 relating to asset impairments of $83.6, the phase-out of certain of Grace's health care research programs of $5.6, additional costs associated with Grace's long-term incentive programs applicable to NMC of $4.8, changes in accounting estimates of $1.8 and other items totaling $6.6

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**Retiring May 10, 1996.*

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Audit
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Compensation, Employee Benefits and Stock Incentive
Messrs. Duffy,[1] Eckmann, Holmes, Lynch, Phipps

Corporate Responsibility
Ms. Kamsky; Mr. Lynch; Drs. Dacey, Frick[1]

Nominating
Messrs. Duffy, Holmes, Macauley, Phipps[1]

[1] *Chair*

Shareholder Information

Publications
To obtain additional information about Grace, request copies of Grace's *Commitment to Care*™ progress report on environmental, health and safety performance, the Company's annual report on Form 10-K, quarterly reports on Form 10-Q or current reports on Form 8-K. Write to Report Fulfillment, W. R. Grace & Co., One Town Center Road, Boca Raton, FL 33486-1010 or call (407)362-1380.

Annual Meeting of Shareholders
Friday, May 10, 1996, 10:30 a.m.
Boca Raton Marriott-Boca Center
5150 Town Center Circle
Boca Raton, Florida

Shareholder Assistance
Information regarding shareholder accounts, dividend payments, stock transfer and related matters should be directed to Grace's transfer agent:
Chemical Mellon
Shareholder Services
P. O. Box 3068
New York, NY 10116-3068
(800) 648-8392

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