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W. R. GR
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W. R. GRACE & CO.

EXECUTIVE OFFICES

7 Hanover Square
New York, New York 10005

TRANSFER AGENTS

Marine Midland Grace
Trust Company of New York
120 Broadway
New York, New York 10015

Continental Illinois
National Bank and
Trust Company of Chicago
231 South LaSalle Street
Chicago, Illinois 60690

REGISTRARS

Chemical Bank
New York Trust Company
20 Pine Street
New York, New York 10015

The First National Bank
of Chicago
38 South Dearborn Street
Chicago, Illinois 60690

ANNUAL MEETING

The annual meeting of the stockholders of W. R. Grace & Co. will be held at 11:00 A.M. Pacific daylight time on Wednesday, May 10, 1967 at the St. Francis Hotel, Union Square, San Francisco, California 94119.

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W. R. GRACE & CO.

1966 ANNUAL REPORT

RECEIVED

APR - 5 1967

SECURITIES & EXCHANGE COMMISSION

GRACE

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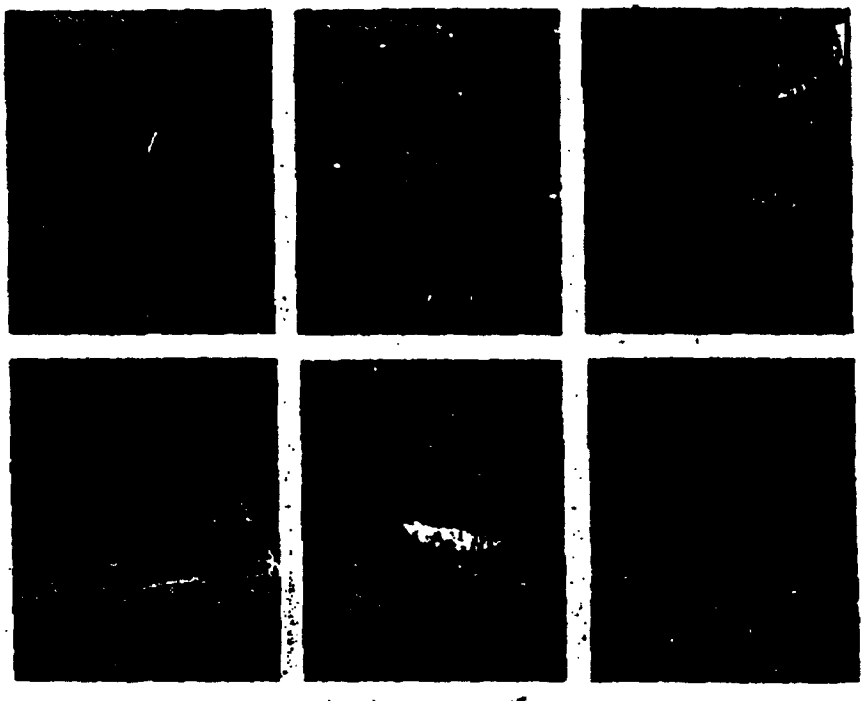
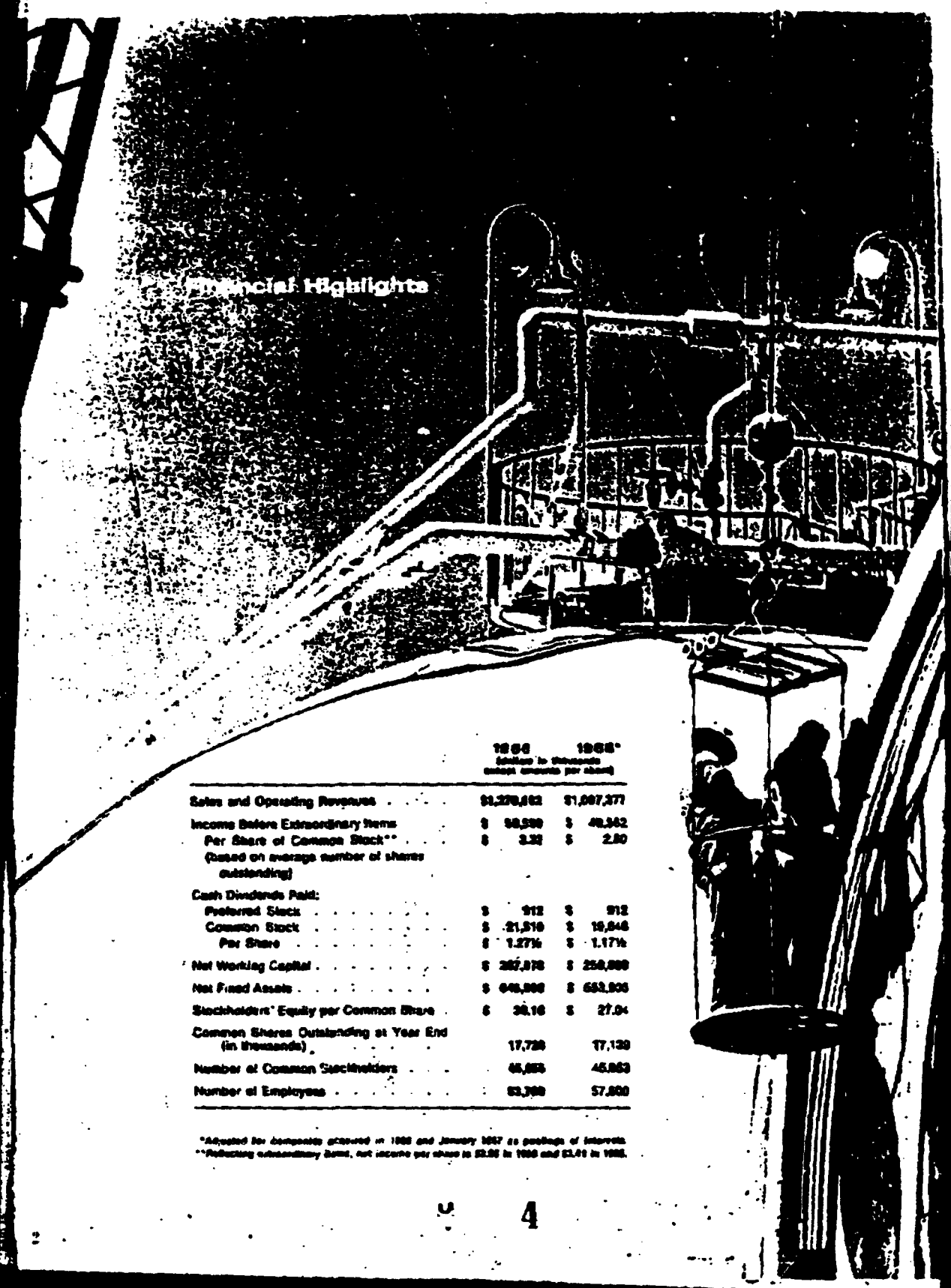




Financial Highlights

	1966	1965*
	(dollars in thousands except amounts per share)	
Sales and Operating Revenues	$1,270,[illegible]	$1,097,377
Income Before Extraordinary Items	$ [illegible]	$ 49,362
Per Share of Common Stock** (based on average number of shares outstanding)	$ 3.32	$ 2.80
Cash Dividends Paid:		
Preferred Stock	$ 912	$ 912
Common Stock	$ 21,510	$ 19,646
Per Share	$ 1.27½	$ 1.17½
Net Working Capital	$ [illegible]	$ [illegible]
Net Fixed Assets	$ [illegible]	$ 653,[illegible]
Stockholders' Equity per Common Share	$ 30.16	$ 27.04
Common Shares Outstanding at Year End (in thousands)	17,728	17,139
Number of Common Stockholders	[illegible]	45,[illegible]
Number of Employees	[illegible]	57,800

*Adjusted for companies acquired in 1966 and January 1967 as pooling of interests.
**Reflecting extraordinary items, net income per share is $3.[illegible] in 1966 and $3.41 in 1965.

To the Stockholders:



Allen S. Ripley, Chairman *(left)* and J. Peter Grace, President

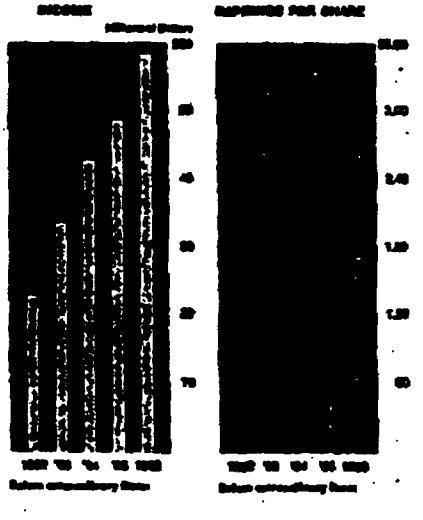
The theme of this annual report, GRACE PRODUCTS REACH THE WORLD'S CONSUMERS, highlights the Company's increasing interest in consumer products in fields in which it is established—chemicals, food and beverages, and paper. I am glad to report that continued growth in all these fields in 1966, supplemented by improved results of other operations, again resulted in new highs in sales and profits.

Sales and revenues totaled $1,278,682,000, an increase of 17% over 1965. Income before extraordinary items amounted to $58,599,000 in 1966, an increase of 21%. Per share of common stock it was $3.32, compared with $2.80 the previous year, an improvement of 19%. This was the sixth consecutive year in which earnings increased. The average annual increase in per share earnings during this period was 14%.

Net income after extraordinary items, specifically the after-tax profit on the sale of the Company's interest in Panagra in 1966 and in Grace National Bank in 1965, amounted to $69,518,000, or $3.95 per share, in 1966 and $58,939,000, or $3.41 per share, in 1965.

W. R. Grace & Co.'s equity in the earnings of its principal unconsolidated 50%-owned companies in excess of dividends received amounted to $1,638,000, compared with $623,000 in 1965. Were these companies consolidated, reported earnings per share for 1966 would be increased by 9 cents.

With a strong position in chemicals encompassing a broad spectrum of products and technologies, and with a long history of international operations, the Company decided several years ago that its base for future growth would be further strengthened by the addition of consumer-oriented businesses and managements. Major steps to achieve this objective were taken in 1966.



Anhydrous ammonia sphere, Memphis, Tennessee

One significant event during the year was the acquisition in September of a 53% interest in Miller Brewing Company of Milwaukee, Wisconsin. Miller High Life is one of the three nationally distributed premium-priced beers. The company's continuing growth has resulted in an increase in its share of the market. Net sales for the year were $112,000,000.

Another major step was the addition of Nalley's Fine Foods Division of Tacoma, Washington in June, 1966. Nalley's potato chips and other snack and specialty foods are well known to consumers in the Pacific states and in Western Canada. In January, 1967, Leaf Brands, Inc. of Chicago, Illinois, a manufacturer of confectionery products and chewing gum, was acquired.

In March, 1967, SeaPak of St. Simons Island, Georgia became a part of Grace. SeaPak, a leading processor of frozen shrimp and other seafood products, has national distribution to institutional and retail outlets.

Total worldwide food and beverage sales for the Company in 1966 were $243,311,000. At year end they were at an annual rate in excess of $360,000,000.

Sales of chemicals in 1966 totaled $200,275,000, an increase of 16% over 1965. Both new and existing products contributed to this growth.

For example, sales of petroleum catalysts increased by 22% as a result of the widespread acceptance of the new molecular sieve catalyst. Facilities for its production were expanded. The plant of Nuclear Fuel Services, Inc. (80%-owned) went into operation in April, 1966, reprocessing spent nuclear fuels from both private and government sources.

Sales of DuBois cleaning compounds increased during the year. Strengthening of the sales force and development of unique application equipment for the division's products contributed to the increase. The Dearborn division introduced new products for water treatment in boiler and cooling water systems and extended its activities into the waste water treatment field.

Increased sales of agricultural chemicals in part reflected the worldwide emphasis on increased food production. Another important factor was the Company's program to establish outlets throughout the rich farm areas of the United States to provide many of the products and services the farmer needs. Grace now has more than 12,000 distribution points in the United States.

Production of ammonia from the Federation Chemicals Limited plant in Trinidad increased by 30% but was below expectations. Present production rates indicate that output in 1967 will be substantially greater.

Chemical earnings, before taxes and any allocation of corporate overhead and interest expense, amounted to $79,051,000, or 71% of the total for the Company in 1966. All major chemical operating units had higher sales and earnings than in the previous year.

Capital expenditures amounted to $148,136,000 in 1966. Cash flow (income before extraordinary items, depreciation and provision for deferred taxes) amounted to $112,000,000, or $6.46 per share. This was an increase from $94,950,000, or $5.53 a share, in 1965. In the past five years, total cash flow has increased at an average annual rate of 19%.

In accordance with the loan agreements negotiated in 1965, $60,000,000 was taken down in 1966. The second $50,000,000 will be taken down on March 15, 1967. The interest rate on this loan is 5½%. W. R. Grace Overseas Development Corporation, a wholly owned subsidiary, sold $15,000,000 of 5% convertible debentures in Europe in April, 1966. Their sale provides additional funds for the expansion of operations outside the United States on a basis consistent with the U.S. Government's balance of payments objectives.

The sale of the Company's interest in Pan American-Grace Airways, Inc. and the expected sale of shares of The Ruberoid Co., after capital gains taxes, provide an additional $40,833,000 in cash.

A tragedy struck the Grace organization in January, 1967 when a plane crash in Peru took the lives of seven officials and employees of South American subsidiaries. We mourn the loss of Albert Meiser, General Manager in Bolivia; M. Powers Kane, Assistant General Manager in Peru; Raul Parrinello, Tulio Pochiera and Derek Brennan of Grace's Peruvian paper business; Bruce Simmons and Roberto Lara, pilots.

It is with deep regret that we record the death in November, 1966 of John T. Cahill, who had been a Director of the Company since 1951. Mr. Cahill was senior partner of Cahill, Gordon, Reindel & Ohl, New York attorneys.

At the 1966 Annual Meeting, stockholders elected four new Directors. Frank M. Freimann, President of The Magnavox Co., and Dr. J. Mark Hiebert, Chairman of the Board of Sterling Drug Inc., are distinguished industrialists. Alexander T. Dalgnault and D. Walter Robbins, Jr. are senior officers of the Company.

During the year, two additional Directors were appointed. Paul F. Hellmuth is senior managing partner of Hale & Dorr and Senior Vice President of Cabot, Cabot & Forbes Co. in Boston. Lawrence J. McKay is a senior partner of Cahill, Gordon, Sonnett, Reindel & Ohl.

George W. Blackwood, Thomas C. Gibian and Edward L. Hutton, Group Executives, were elected Vice Presidents of the Company during the year.

A number of executive changes were made in operating divisions. Robert D. Goodall, formerly President of the Davison Chemical Division, was appointed President of the new Agricultural Products Division. William L. Taggart, formerly Executive Vice President, was appointed President of the Dewey and Almy Chemical

Division. Page Edmunds, formerly Vice President, was appointed President of the Davison Chemical Division, and Dr. Robert R. White was appointed President of the Research Division. Charles W. Miller, formerly Vice President of the Consumer Products Group, was named Chief Executive Officer of Miller Brewing Company, succeeding the late Norman R. Klag.

In June, 1966 the dividend on the common stock was raised to an annual rate of $1.30, an increase of 10 cents per share. This was the fifth consecutive year in which an increase was voted.

In 1966, principally through a tender offer, the Company acquired 1,030,200 shares of The Ruberoid Co. at an average cost of $25.42 per share. Discussions with Ruberoid looking to a merger were unsuccessful and were terminated in December, 1966. On March 2, 1967 W. R. Grace & Co. agreed to sell the Ruberoid shares to General Aniline & Film Corporation for $27.50 per share. General Aniline's obligation to purchase these shares is subject to its merger with Ruberoid. This transaction will result in a profit after capital gains taxes of $1,700,000.

While the improvement in both overall earnings and earnings from Latin American operations in 1966 was substantial, results for the year and particularly for the last three months would have been greater had it not been for two events. In October, paper and chemical facilities at Paramonga, Peru were damaged by a severe earthquake. Fortunately, there were no injuries. The plants were back in operation by year end, but loss of production and extraordinary expenses adversely affected earnings by an estimated $800,000. In February of this year, the Brazilian currency was devalued by 18%. In accordance with conservative accounting practice, the resultant unrealized foreign exchange loss of $400,000 was reflected in 1966 results. These two events penalized earnings by 7 cents per share in 1966.

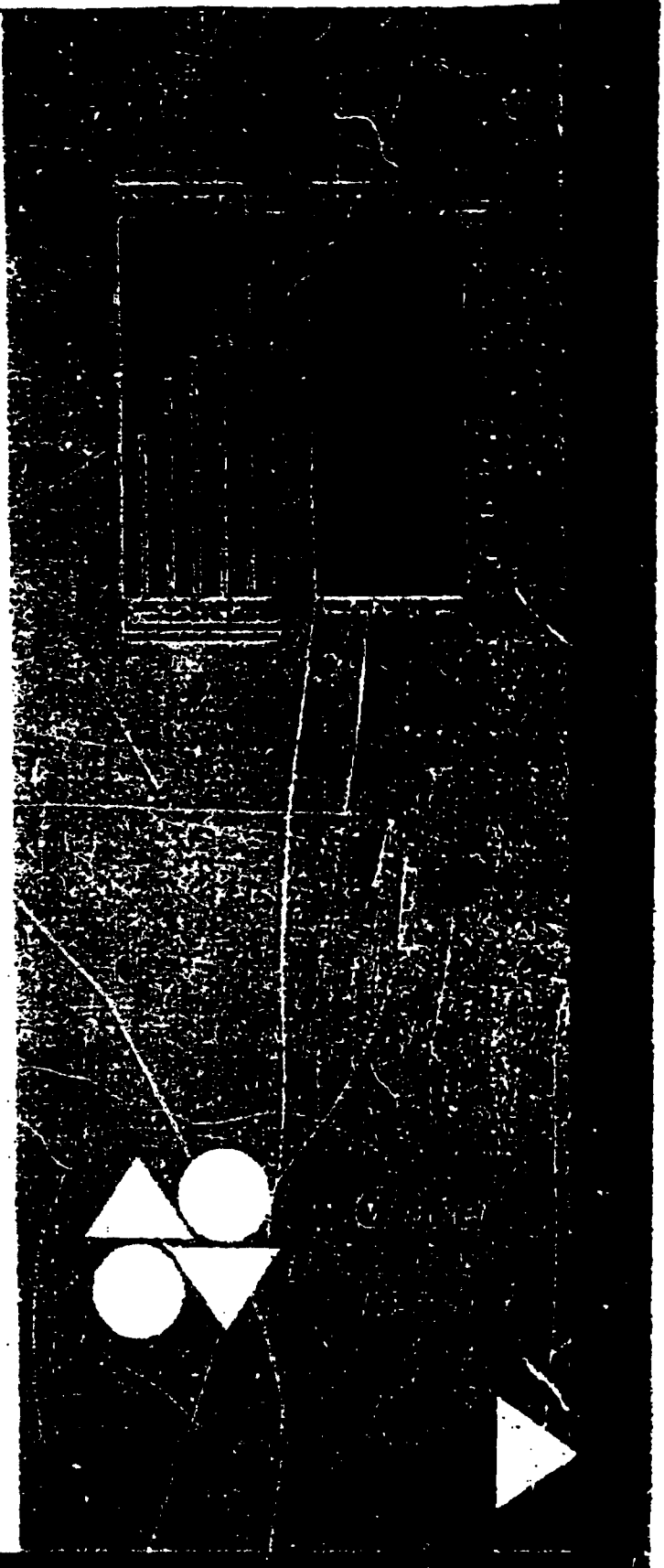
Looking to the future, we foresee continuing growth in our chemical activities. In addition, the increased emphasis on consumer products, with the opportunity they offer for innovation and growth, is providing an important second thrust to the Company effort.

With further contribution from facilities recently brought into production, and with a high level of capital expenditures programmed for the next several years, we are optimistic that all major segments of the Company will continue to move ahead in sales and earnings.

Respectfully submitted,

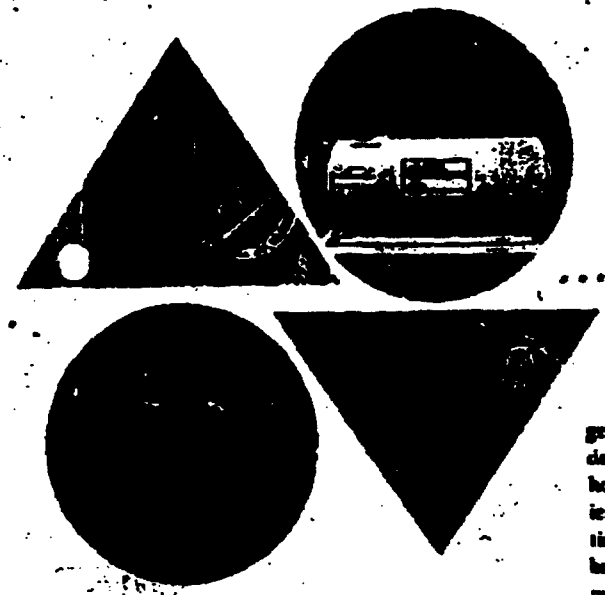
J. Peter Grace
PRESIDENT

March 9, 1967





Grace products reach the world's consumers



... in Chemicals

For the housewife, vinyl for shower curtains; for the farmer, GRACE SEEDTAPE service; for the sportsman in Little America, vinyl for golf boots; for the homeowner, adhesive insulating material.

The chemical industry, in which there has been so much technical innovation in the past 25 years, encompasses a wide range of products and processes. At one extreme are the many bulk industrial chemicals which lose their identity long before the products to which they contribute reach the ultimate consumer. At the other extreme are specialty and converted chemicals which reach the consumer either as finished products or as important components of those products.

Since its entry into the chemical industry, W. R. Grace & Co. has concentrated on building a leadership position in chemical specialties and converted products, as well as in situations where it has a strong technological position. Not only is it possible to build into such products special characteristics which differentiate them from those offered by other producers, but also they are less vulnerable to cyclical swings in demand than the majority of bulk industrial materials.

Chemical sales of W. R. Grace & Co. have increased 18% annually over the past 10 years, while pre-tax profits from these sales have increased 16%. This growth is the result of marketing chemical products whose range is as wide as the spectrum of consumer needs.

In agriculture, for example, Grace fertilizers make possible higher crop yields for farmers; Grace animal feed supplements and supervised feeding programs improve product quality and reduce costs for those who raise livestock.

Institutional cleaning compounds, disinfectants and germicides help meet the high standards of sanitation demanded by the public in hospitals, restaurants and hotels. Disposable medical supplies provide convenience and protection in the offices of doctors and dentists. Petroleum catalysts used for gasoline refining, battery separators and sound-deadening materials improve the performance and reliability of automobiles.

Sealing compounds for cans, bottles and jars provide essential protection for long storage periods, while CRYOVAC shrinkable films lengthen the shelf life of frozen and refrigerated poultry, meat, cheese and bakery products.

The sections which follow describe W. R. Grace & Co.'s chemical activities in three broad categories. These are Agricultural Chemicals with sales in 1966 of $226,000,000—37% of total chemical sales; Industrial and Specialty Chemicals with sales of $264,000,000—33% of the total; and Packaging and Plastics with sales of $243,000,000—30% of the total.

Grace chemical products reach the world's consumers from 227 manufacturing plants through 226 sales offices in 33 countries.

AGRICULTURAL CHEMICALS

W. R. Grace & Co. has always sought to develop products and services to satisfy the constantly changing requirements of the farmer-consumer. The Company's contribution to successful farming operations today is based on the increasing need for a scientific approach to farming. For example, a fertilizer formulation compatible with a farmer's particular crop and soil requirements is essential if he is to get the maximum yield from his acreage.

Distribution is the key factor in serving the farmer-consumer. The Company's Agricultural Products Division markets its products through more than 12,000 distribution outlets. These range from independent

Air bubble controlling thickness of CRYOVAC film

dealers as Grace Growmore retail service outlets. The program to establish these outlets in the Corn Belt continued at a rapid pace in 1966. At Growmore centers, the farmer may obtain his supplies of fertilizer, feed supplements, seeds and pesticides.

Large and modern production facilities are required to keep the distribution centers filled. Early in 1966, additional production facilities for phosphates and high analysis fertilizers went into operation at the Company's agricultural chemical complex in Bartow, Florida. Demand for phosphate fertilizers has increased at a rate far exceeding government projections.

In Trinidad, West Indies, a second major expansion of nitrogen production capacity was completed by Federation Chemicals Limited, a wholly owned subsidiary. This expansion brings ammonia capacity in Trinidad to 500,000 tons annually, and overall capacity to more than 900,000 tons. Worldwide use of nitrogen fertilizers since 1960 has grown at the rate of 12% annually.

A new facility for production of high analysis and mixed fertilizers and for ammonia distribution in a strategic Corn Belt area has just been completed at Henry, Illinois. The Company also expanded ammonia terminal facilities at Searsport, Maine and Fort Dodge, Iowa.

Slurry fertilizer, a product developed by Grace and introduced in 1963, continues to receive wide acceptance among farmers. Sales of this unique new product increased by 75% in 1966, and the outlook for further increases is promising. Slurry is a balanced mixture of plant nutrients in semi-liquid form, specifically blended for the particular soil needs and crop requirements of a farmer in a given area.

The Company also has expanded its agricultural feed and feed supplement business throughout the Midwest and Southwest. A new plant was completed at Garden City, Kansas which will produce 60,000 tons of protein supplements annually for use by farmers, ranchers and commercial feeders in that area. Additional feed supplement facilities now supply similar products in Illinois, Indiana, Iowa, Colorado, Nebraska and Texas. Bulk feed supplement outlets, called Grace Feedlineups, are being planned at locations adjacent to Grace Growmore service centers.

The Company expanded its marketing activities in pesticides and field seeds. Distribution centers for these products are being added in many areas of the country. Expansion of the hybrid seed corn product line currently is being planned.

Agricultural chemicals continue to grow in importance to the Company in other parts of the world. In Australia, Cresco Fertilizers Limited, a majority-owned subsidiary, is constructing a plant in Victoria which will increase total available capacity for phosphate fertilizers by more than 50%. The demand for agricultural products in Australia and New Zealand reflects that area's strategic location as a major food producer for the Far East. The Cotonite phosphate-rock facility in





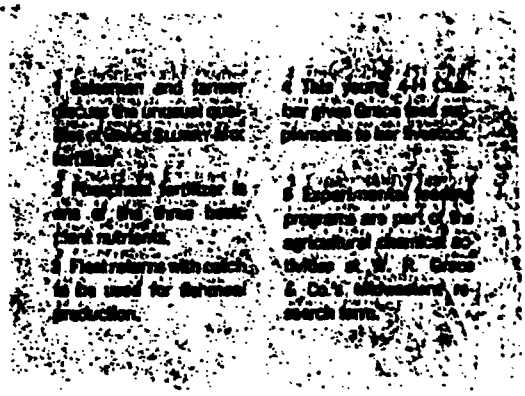
Togo, West Africa, in which the Company has a 57% interest, expanded its capacity for the production of high-grade phosphate rock. This company substantially increased its profits, and dividends paid were higher than in previous years.

One of the important sources of protein used in the formulation of poultry and animal feeds throughout the world is fishmeal. Subsidiaries of the Company are among the leaders in this industry in both Peru and





Chile. During 1966, production and profits were up substantially as a result of improved fishing conditions. For years it has been the hope of many that fishmeal would provide an ample and economical source of protein for human consumption in the areas of the world where protein supply is inadequate. The step taken early in 1967 by the U.S. Food and Drug Administration, giving limited approval for the use of fishmeal protein for human consumption in the form of fish



flour, is important to the achievement of this objective.

There is no end in sight to the need for expanding production of agricultural products and livestock in order to meet the food requirements of the world's growing population. W. R. Grace & Co. will continue to enlarge its production capability and provide related distribution outlets to fulfill the requirements of farmers.



INDUSTRIAL AND SPECIALTY CHEMICALS

Many consumer products are based on or incorporate Grace specialty chemicals.

The consumer demand for service has been a factor in the increased sales of specialty products for industrial and institutional cleaning. These products are sold directly to the consumer through a sales force totaling more than 1,000. Dubois Chemicals Division compounds are specifically designed for restaurants, hotels and food processors, making it possible for these industries to maintain maximum sanitary conditions. Special products are also formulated for the transportation and industrial manufacturing industries. Hospitals across the nation use Vestal Laboratories' germicidal detergents, surgical scrub soaps and disinfectant sprays.



Hospitals and patients benefit from Grace germicides.

Grace is taking the marketability of its detergents and cleaning products on a direct basis to the housewife.

Other Grace products also have important consumer applications, although in many instances they are incorporated into the finished products of other manufacturers, fabricators or converters. W. R. Grace & Co. maintains its leadership position in many of the products it has developed and produced.

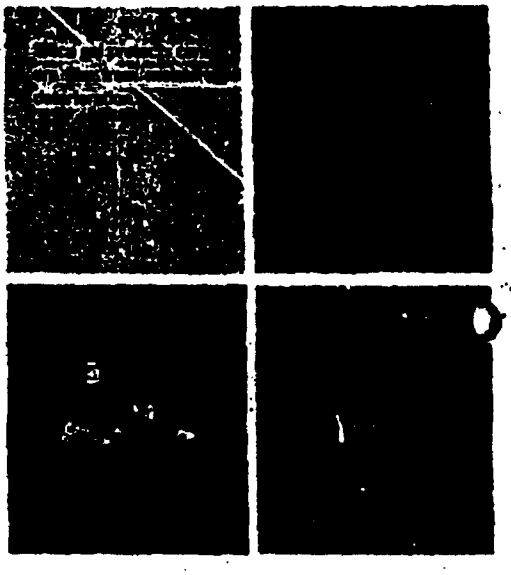
For example, Grace is the leading manufacturer of petroleum cracking catalysts used by refiners to produce gasoline. With more than 90 million automobiles now in use in the United States, consumption of fuel continues to rise annually. The Company's new zeolite catalysts increases the gasoline yield from crude oil. Demand for this catalyst has led to expansion of facilities in Cincinnati, Ohio and Lake Charles, Louisiana.

Another product important to the consumer is the battery separator. W. R. Grace & Co. is the leading producer of impregnated fiber insulators used to separate positive and negative plates. They greatly increase the life and reliability of storage batteries.

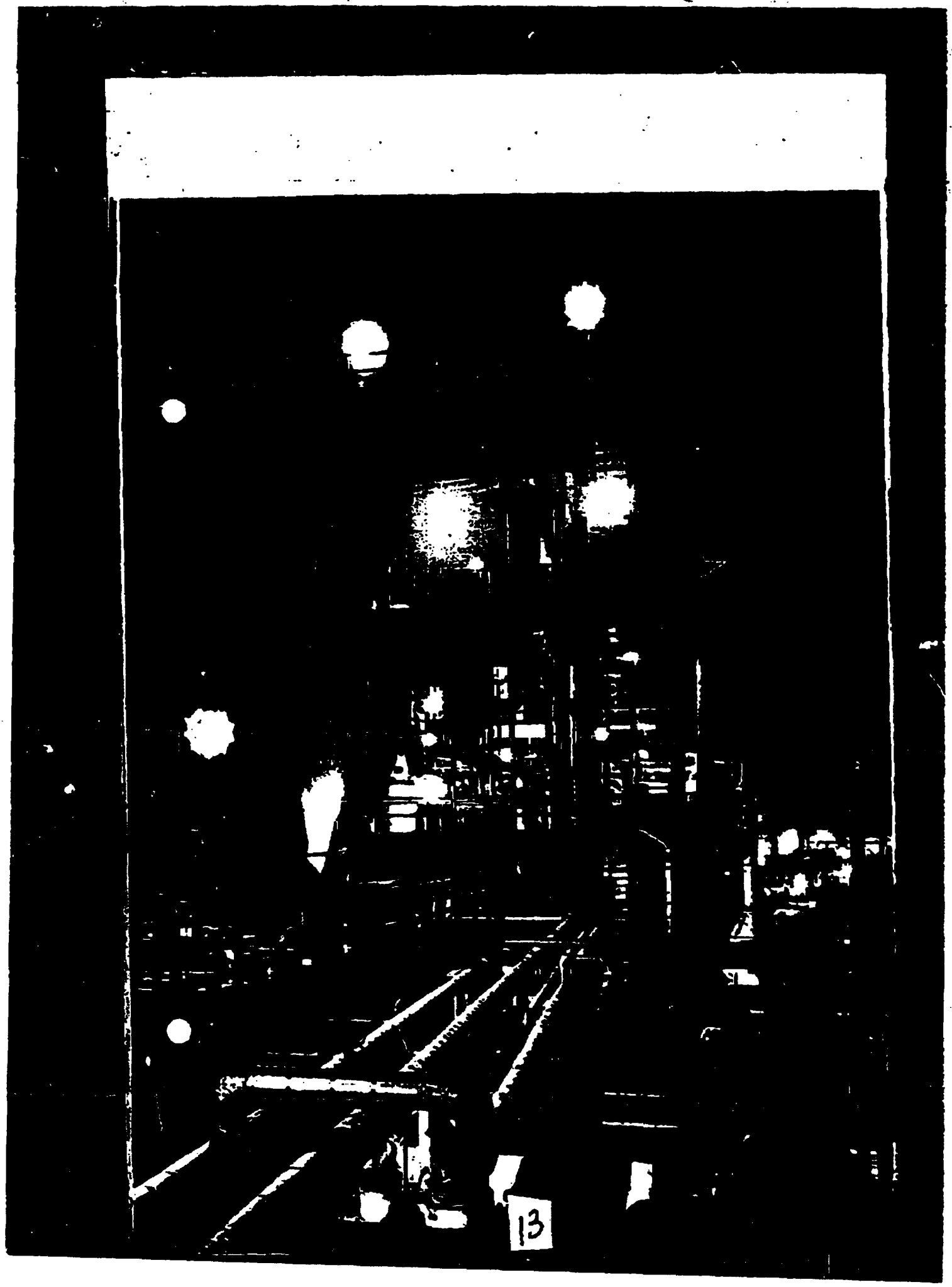
The Company produces chemical specialties for the construction industry, many of which find ultimate consumer use. Zonolite Division vermiculite is an outstanding lightweight aggregate with insulating and fireproofing characteristics. As attic insulation, this is a "do-it-yourself" product which has proved highly successful for home owners looking for a quick and economical way to reduce heating costs.

The consumer benefits from many Grace products which are not immediately identifiable. Davison silica gel protects color film from moisture deterioration, and also protects moisture-sensitive electronic and optical gear used by the military and by industry. Other products which benefit the consumer are Syloid silica gel, an anti-caking and free-flow aid to such items as granular sugar, cake mixes and dessert powders; rare earths used to make color phosphors for television picture tubes; vinyl latexes, the basis of quick-drying paints for home use; and letterpress printing blankets which facilitate top-quality reproduction in publications.

Chelating agents—chemical compounds which neutralize the metallic impurities in hard water—are used in detergent formulations to brighten fabrics. A plant to produce an important chelating agent, NTA, was completed in Nashua, New Hampshire in November, 1966. Expansion of this plant is already under way. A similar plant being constructed in Sweden will serve the growing European market for these products.



Phthalic anhydride facilities, Ferdo, New Jersey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Also in Europe, a Grace subsidiary sells a wide range of pressure-sensitive cellophane and vinyl tapes for office and household use.

The consumer often takes for granted the availability of electric power. W. R. Grace & Co., through an 80%-owned subsidiary, Nuclear Fuel Services, Inc. (NFS), began commercial reprocessing of spent nuclear fuel received from nuclear-powered public utilities in 1966 at a new plant in Western New York. This plant, the only privately owned nuclear fuel reprocessing facility in the world, will increase its activities as the major public utilities change from conventional power generation to nuclear reactors. Utility companies placed orders for $2 billion worth of nuclear power plants, equivalent to nearly half of all the electrical generating capacity ordered in 1966.

In these specific areas as well as in many others, W. R. Grace & Co. is providing products and services that benefit consumers throughout the world.

PACKAGING AND PLASTICS

W. R. Grace & Co. reaches consumers through a wide range of packaging materials which protect many items found on supermarket and department store shelves. Packaging innovations created from a wealth of new materials have resulted in improved merchandising techniques. They have also enabled the consumer to obtain fresher and more appealing products, and in many cases they provide added convenience for the user.

CRYOVAC films are an important example of Grace's leadership in packaging. The first CRYOVAC shrinking plastic film obtained commercial acceptance in the late 1940's. The availability of CRYOVAC films, which afford a high degree of protection against loss of moisture and deterioration from exposure to air, revolutionized the turkey industry. An industry which had always been highly seasonal found itself with year-'round demand.

Since introduction of the first film, more than 90 new specialized films have been added. These protect the flavor and quality of poultry, meat, cheese and other foods. CRYOVAC films are also used to add sales appeal to such self-service merchandise as record albums, textiles, toys, games and paper products.

As a natural development of its packaging business, the Cryovac Division broadened the range of products it offers its customers by entering the rigid-plastic container field. A new plant in Reading, Pennsylvania began production of thermoformed polystyrene containers for the packaging of bakery and confectionery items, foamed polystyrene containers used as disposable dinnerware in institutions, and trays for packaging consumer meats, poultry and produce.

AMERCOAT containers of blow-molded polyethylene are durable and attractive cases for electric hand tools, artists' sets, small appliances and other consumer items.

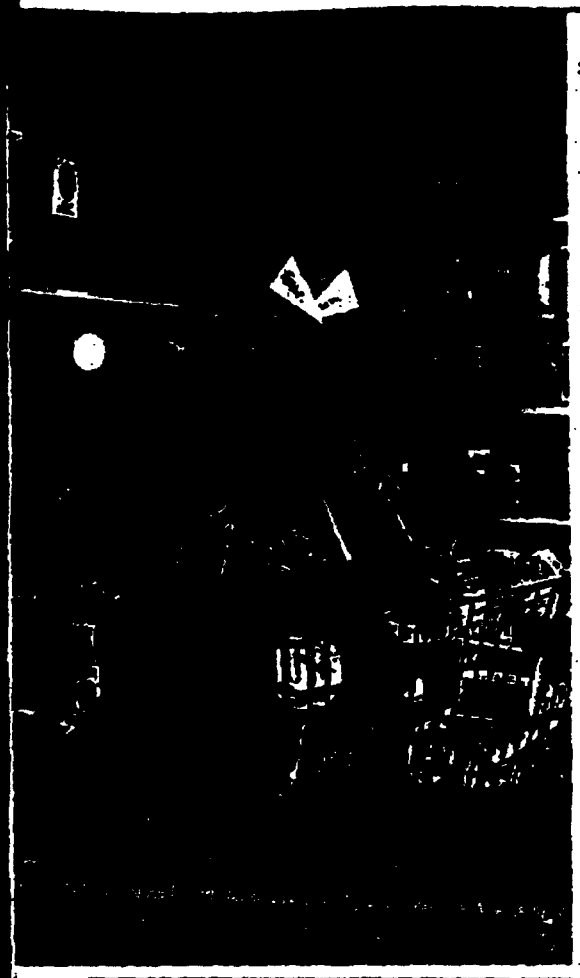
W. R. Grace & Co.'s Dewey and Almy Chemical Division, a pioneer in container sealing compounds, continues to supply sealants not only for cans but also for easy-open bottle tops which tear or turn to open. Other important products include flowed-in sealants for jar caps and lids, and compounds for aerosol containers. DARAN carton coatings provide moisture and vapor barriers needed to protect packaged products.

Sales of all Grace packaging materials continue to grow in the United States, Europe, Latin America, Australia and Japan.

Vinyl plastic products are increasing in popularity with the world's consumers because they are more economical, have a wider range of uses and are generally more durable than the conventional materials they are replacing. Through the Hatco Chemical Division, the Company is a leading supplier of vinyl products.

Modern styling in shoes, handbags and outer wear has created an important consumer market for vinyl





materials. In addition, calendered vinyl film and sheeting are used increasingly for automobile upholstery, outdoor furniture, luggage and shower curtains. Other end uses include electrical insulation tape and floor tile.

Style considerations have also been important to the Company's vinyl business in Latin America and Europe, where consumers seek the most wide range of products. With 15 vinyl plants world-wide, Grace has established itself internationally as a major supplier of high-quality calendered vinyl film.

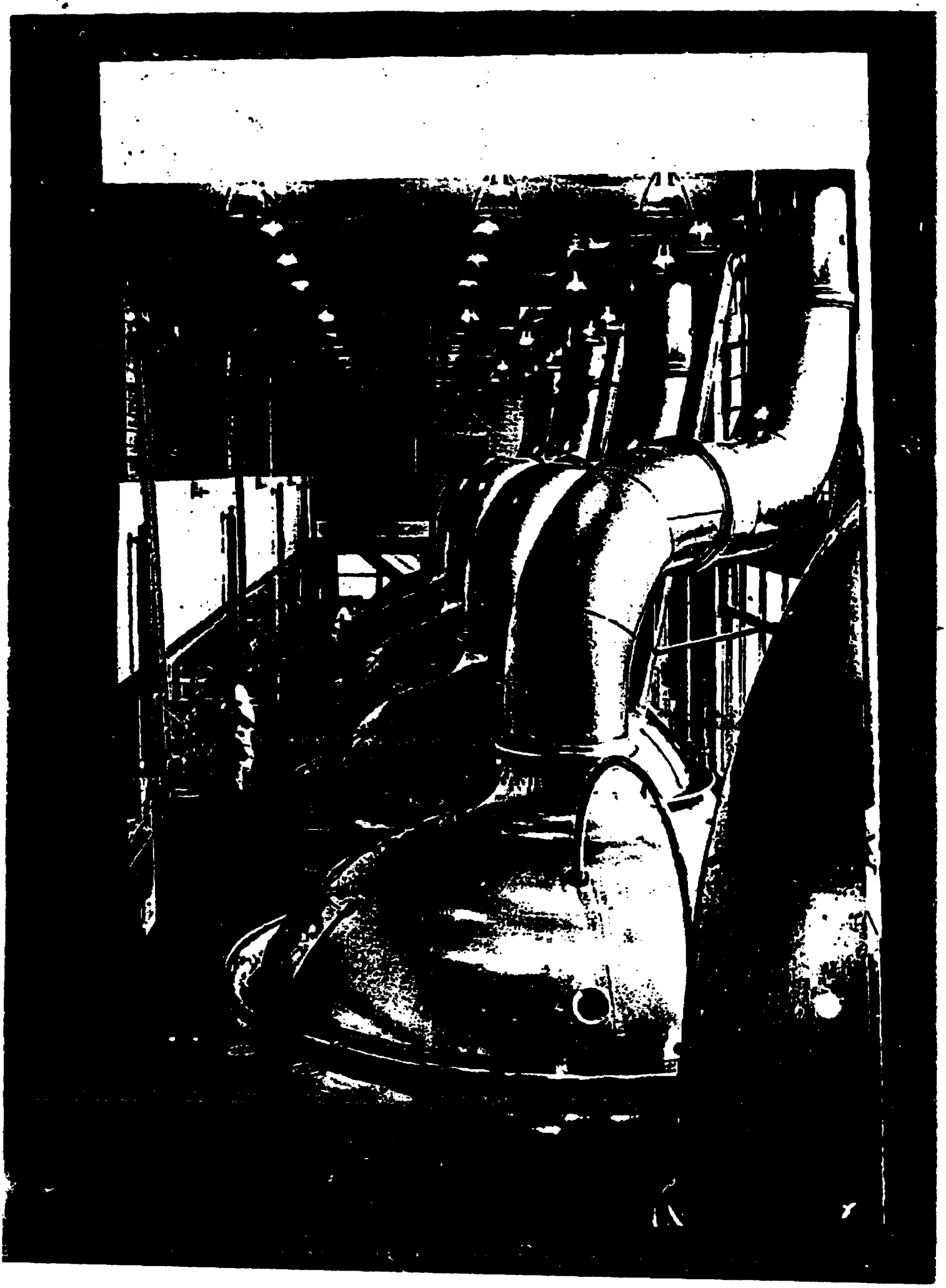
The Company also manufactures and markets polyester resins. These extremely versatile materials are being widely used in the manufacture of hulls for yachts and other pleasure craft. The exceptional durability of these resins also has resulted in their use in the automotive and home furnishing fields.

Polypropylene monofilament, multifilament and ribbon fibers are also produced and marketed by Grace. One important consumer-related segment of this activity involves weaving polypropylene ribbon in 12- and 15-foot widths for use as carpet backing.

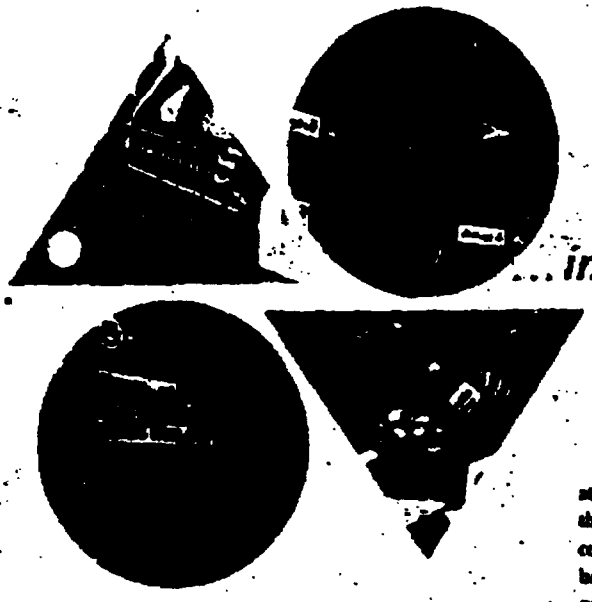
Through research and development, W. R. Grace & Co. will continue to provide new materials to meet packaging requirements and to create new plastic products for consumer use.







Grace products reach the world's consumers



...in Food and Beverages

Bragg Chocolates, Dublin, Ireland; Hellerup Ice Cream, Copenhagen, Denmark; Leaf Brands candy, Chicago, Illinois; Marble snack products, London, England

Significant expansion of W. R. Grace & Co.'s activities in food and beverages took place in 1966. Important positions were established in the brewing and snack and convenience food fields to complement the existing food operations in Latin America and those of the Chocolate and Confectionery Division in Europe and the United States. Sales of these products in 1966 of $243,311,000 represented 19% of the Company's total, although the profit contribution was not this large.

Miller Brewing Company of Milwaukee, Wisconsin became a majority-owned subsidiary on September 22, 1966. This 111-year-old brewer produces MILLER HIGH LIFE, *The Champagne of Bottle Beer*, one of the three national premium-priced beers. Miller's reputation for making a quality product of the highest standard has made it an important factor in the United States brewing industry. Its unique crystal-clear bottles have become well known to the consuming public, and its imaginative advertising programs have enabled it consistently to increase its share of the market.

For many years MILLER HIGH LIFE was brewed only in Milwaukee, Wisconsin. As the demand for MILLER continued to increase, existing facilities became inadequate, and in 1966 a second brewery was acquired in Azusa, California. This facility was completely renovated and modernized. Quality controls were established to ensure that the MILLER HIGH LIFE produced at Azusa would be identical in taste and quality to the beer brewed in Milwaukee. This brewery, which commenced operations in September, will add 600,000 barrels to Miller's capacity in 1967 and ultimately will produce 1,000,000 barrels annually.

In order to serve growing markets in the Southwest, Miller acquired another brewery in Fort Worth, Texas in the latter part of 1966. This plant is currently being converted to produce MILLER HIGH LIFE beer.

In 1966, Miller produced 4,146,000 barrels of beer, and sales reached an historic high of $111,953,000, excluding excise taxes. The production increase represented a gain of 13% over 1965. In the past ten years, Miller's sales have increased almost 85%.

MILLER HIGH LIFE is sold through more than 700 independent distributors in every one of the 50 states. It is also available in many foreign countries and is a favorite of service personnel in Viet Nam.

Since June, 1966 Nalley's Fine Foods Division, a processor of a diversified line of snack food products marketed on the West Coast, has been a part of W. R. Grace & Co. Nalley's, with headquarters in Tacoma, Washington, has six plants in the United States and two in Canada. Sales in 1966 totaled $47,440,000, an increase of 9% over 1965.

In the Pacific Northwest, Nalley's Fine Foods items are found in nearly all food stores. Nalley's markets the leading line of snack products such as potato and corn chips. Frozen and canned convenience foods, pickles, sauces, dressings and dips are also produced under the Nalley's label. A wide variety of Mexican foods is also marketed.

During 1966 Nalley's continued its development in new market areas. Sales in the State of Arizona, which is becoming a major sales territory, increased 20% over the previous year. Distribution of Nalley's products has

The Miller brewhouse, Milwaukee, Wisconsin

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also increased in the San Francisco Bay area and in Southern California. Entry into these markets was supported by extensive consumer advertising programs.

Institutions constitute an important and fast-growing market for the food industry. Nalley's is developing products for quantity feeding in hospitals, schools and factories. These products have special characteristics such as the ability to withstand the sustained heat of steam tables. In 1966 a complete line of specially formulated canned products was introduced.

In March, 1967, SeaPak of St. Simons Island, Georgia became a division of W. R. Grace & Co. SeaPak, with plants in Georgia, Florida and Texas, processes and freezes high-quality seafood, principally shell fish, which is marketed in grocery outlets under the SEAPAK and TRADE WINDS labels. Shrimp products account for about 70% of sales, which totaled $28,000,000 in 1966.

In recent years prepared fish portions, fish fillets and breaded products have become increasingly important, and SeaPak is augmenting its facilities to process such products. SeaPak, a leading supplier of high-quality fish products to the institutional trade, also brings into the Company an organization with distribution in retail frozen food markets.

Leaf Brands, a Chicago-based confectionery and chewing gum manufacturer with subsidiaries in Canada, Ireland, Belgium and Japan, became a part of the Chocolate and Confectionery Division in January, 1967. Its product line includes children's specialties, expanded candies, sugar wafers and freeze pops. Leaf's sales volume in 1966 was $23,000,000.

Overall results of the Chocolate and Confectionery Division improved in 1966. New chocolate products were introduced successfully by Van Houten in the Netherlands and by Urney Chocolates in Ireland. Cacaofabriek de Zaan, a leading producer of cocoa butter and cocoa powder, reported its highest profits since becoming a part of W. R. Grace & Co.

Another subsidiary, Drankenindustrie Raak, substantially increased its sales of LONDON TONIC and other soft drink and snack food products in the Netherlands with profits showing a corresponding increase.

Consumption of ice cream in Europe continues to increase. This has benefited Hughes Brothers in Ireland and Hellerup Flode Is in Denmark.

Marela Limited of London, England became a part of the European Consumer Products Division last year. Marela produces a line of snack foods, including a wide variety of pickle products.



In Latin America, continued improvement in living standards has greatly increased the demand for snack and convenience foods which formerly were regarded as luxuries. Grace subsidiaries have produced and marketed these items for many years and currently are expanding facilities and product lines.

Results of the candy and biscuit making subsidiaries in Chile, Colombia and Peru improved in 1966. Hucke Hermanos in Chile is expanding its chocolate production facilities and installing automatic packaging equipment for both chocolate and biscuits to meet increased demand for these products. Using the technical assistance of Nalley's, Arturo Field in Peru installed a new snack production line.

In Central America, the Company expanded its food interests by acquiring Alimentos Kern in Guatemala, a producer of fruit nectars, juices and tomato products. Also in Guatemala, Ducal, whose principal products are fruit juices, ketchup and baby foods, introduced a

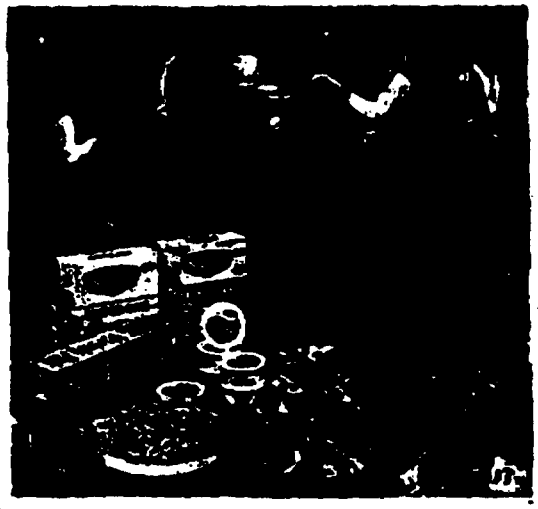
line of canned and Cryovac packaged meat products. Pozuelo, S.A. in Costa Rica manufactures biscuits and candy, and plans to expand production of these products and add confectionery lines in 1967.

The economic improvement resulting from the Central American Common Market provides a firm base for continuing growth.

As W. R. Grace & Co. develops its worldwide food and beverage interests, the operating units benefit from exchange of production technologies and marketing techniques. This has already resulted in higher quality products, lower production costs and increased sales. These benefits should become even more important in future years.

Grace food and beverage interests range from (left) Van Houten chocolate and cocoa products, distributed throughout the world, and Rank soft drinks popular in the Netherlands, to (right) Arturo Field biscuits and candies in Peru and (below) Miller High Life, *The Champagne of Bottle Beer.*











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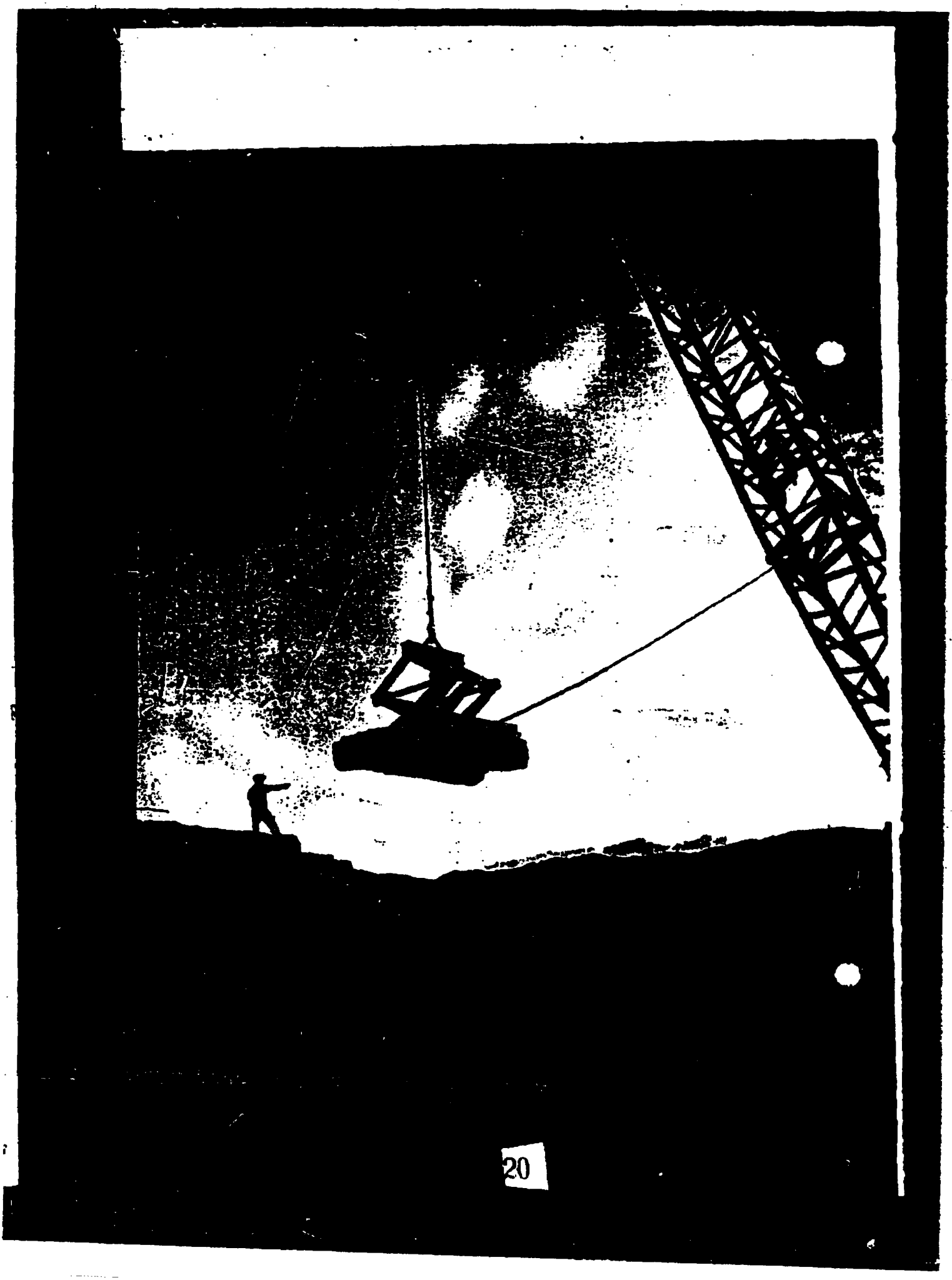
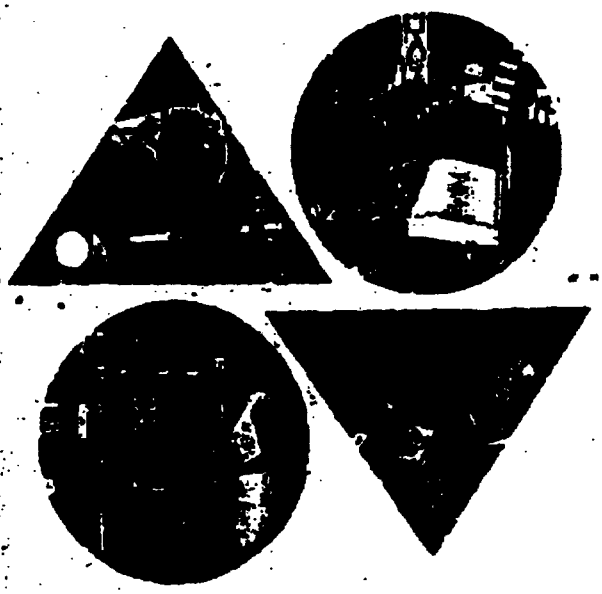


Grace products reach the world's consumers



... in Paper

Grace paper products for the consumer range from kraft and board to fine book stock and include paperboards and school materials as well as boxes and cartons.

The use of paper and paper products in a developing country increases rapidly as the standard of living improves.

The use of paper in Latin America is growing at the rate of 15% a year. W. R. Grace & Co. has important paper interests in three Latin American countries—Peru, Colombia and Ecuador.

The potential for further growth in paper consumption is impressive. Latin Americans currently use only 25 pounds per capita annually compared to U.S. consumption of 400 pounds per capita, excluding newsprint.

W. R. Grace & Co.'s principal interest in paper is Sociedad Paramonga Limitada, a wholly owned subsidiary operating the largest pulp and paper mill in Peru. Grace also has a joint interest, with subsidiaries of International Paper Co., in Productora de Papeles, S.A. in Cali, Colombia. Both mills use bagasse, the fibrous sugar cane residue, as the principal raw material. The Grace process was pioneered from Grace technology and has been employed successfully in these operations for many years. Use of this locally available raw material benefits the foreign exchange position and stimulates local employment, making these operations welcome additions to the economies of these countries.

Production from five paper machines at Paramonga amounted to 72,000 tons in 1965, while in Colombia output from three machines totaled 52,000 tons.

The Paramonga plant produces a variety of paper stocks, including heavy-duty kraft papers, paperboard of various thicknesses, bond and writing paper, and tissues. Much of the Colombian production is consumed in cultural and uses such as books, magazines, and writing materials for home, school and office.

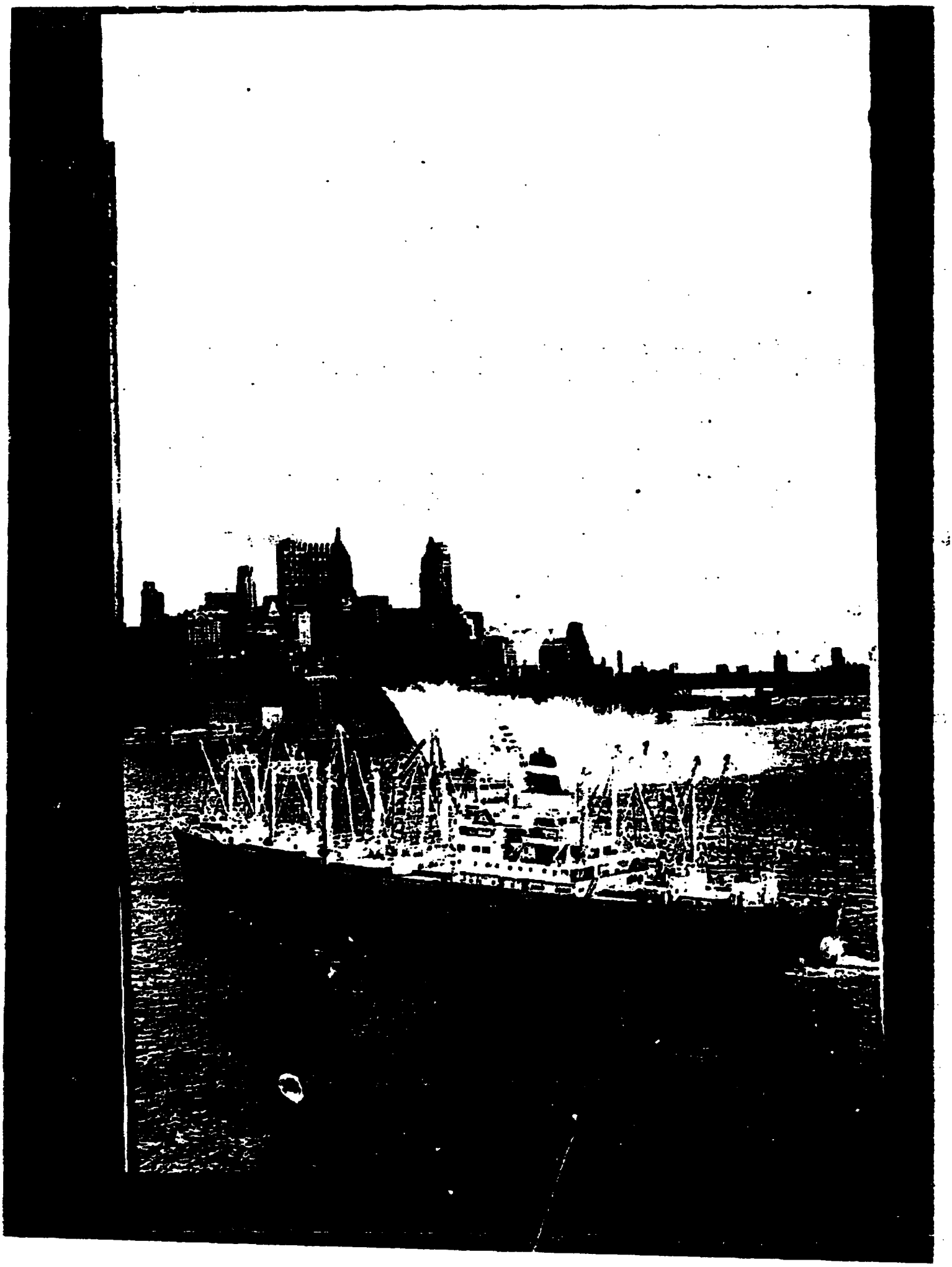
The plant in Peru also supplies paper for conversion into other products used in packaging both consumer and industrial products. Four converting plants of Grace subsidiaries produce such items as bathroom, shirt and shoe boxes, food containers, multi-wall and grocery bags, and corrugated cartons in a wide variety of sizes and shapes.

An important spur to the growth of the paper business in Ecuador is the use of corrugated boxes for the shipment of bananas to world markets. A Grace subsidiary manages Industria Cartonera Ecuatoriana S.A., the world's largest supplier of banana boxes, in which the Company has a one-third interest.

To meet the demands of the growing economy in Peru, Grace has embarked upon a major expansion program which will double its paper operations in the next two years. The capacity of the Paramonga mill for all existing forms of paper will be increased. Existing pulp and bleaching facilities also will be expanded. A new pulp and paper plant will be erected at the sugar mill near Caravio in northern Peru. A paper machine with an initial capacity of 44,000 tons will use as its raw material bagasse available from the sugar operation.

While expansion of Grace operations is meeting anticipated demand in the countries presently served, potential new markets in Latin America are being actively considered.

Bagasse stockpile, Cali, Colombia



in Transportation

Revenues and operating earnings of Grace Line Inc. in 1966 improved substantially over 1965 resuming the upward trend begun in the early 1959's. Results in 1965 had been adversely affected by extended strikes against the U.S. maritime industry.

Total revenues of $98,818,000 from steamship operations were the highest in history. The Line's operating earnings were the highest since 1957.

Participation in cargo movement to and from South America was maintained at a satisfactory level. The volume of trade between the United States and South America showed improvement.

Grace Line continues to be the dominant carrier of cruise passengers to Latin America, with record passenger revenues in 1966 contributing significantly to overall profits. The *Santa Rosa* and *Santa Paula* have long been established in the Caribbean cruise trade, while new *Santa Magdalena*-class ships provide an interesting cruise itinerary to historic cities on the West Coast of South America.

In 1966, the Pacific Coast service of Grace Line was expanded by the acquisition of the Pacific Republics Line from Moore-McCormack Lines, Inc. The combination of this operation with Grace Line service improves efficiency and frequency of scheduled service to Central and South America, and adds Argentina, Uruguay and Brazil to the countries served from the West Coast of the United States. Substantial overhead savings are also being realized.

Three new cargo liners of the *Santa Lucia* class were placed in service from the Atlantic Coast of the United States to the West Coast of South America, and three additional ships of this class are scheduled for delivery in 1967. These ships are larger and faster and require less crew than the ships they are replacing. They have substantially increased capacity for containers and refrigerated and heavy-lift cargo.

Delivery of these ships will mark the completion of over half of the Line's replacement program. Completing the remainder of the program depends largely upon clarification of U.S. policies regarding the Merchant Marine. These policies are under study by the Executive Branch of the Government.

In addition to its commercial operations, the Line is operating nine ships for Military Sea Transport Service and three Grace Line vessels in support of Viet Nam operations. No significant profit is derived from the operation of these vessels.

In 1967 Grace Line should benefit from completion of the phasing-in of the *Santa Lucia*-class ships and a full year's operation of the Pacific Republics Line service.

Profits of Gulf and South American Steamship Co., Inc., owned jointly with Lykes Bros. Steamship Co., Inc., showed substantial improvement in 1966.

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In January, 1967 W. R. Grace & Co. transferred its 50% interest in Pan American-Grace Airways, Inc. to Braniff Airways, and on February 1 Panagra was merged into Braniff International. Braniff also acquired the 50% interest in Panagra of Pan American World Airways, Inc.

Panagra, founded in 1928, provided service for the West Coast countries of South America and Buenos Aires. The merger with Braniff International creates a stronger airline which should provide improved service and accelerate the development of trade and travel between the Americas.

Excellent cuisine is a hallmark of Grace Line cruises.



The Santa Lucia outbound, New York Harbor

Developments in Petroleum and Mining

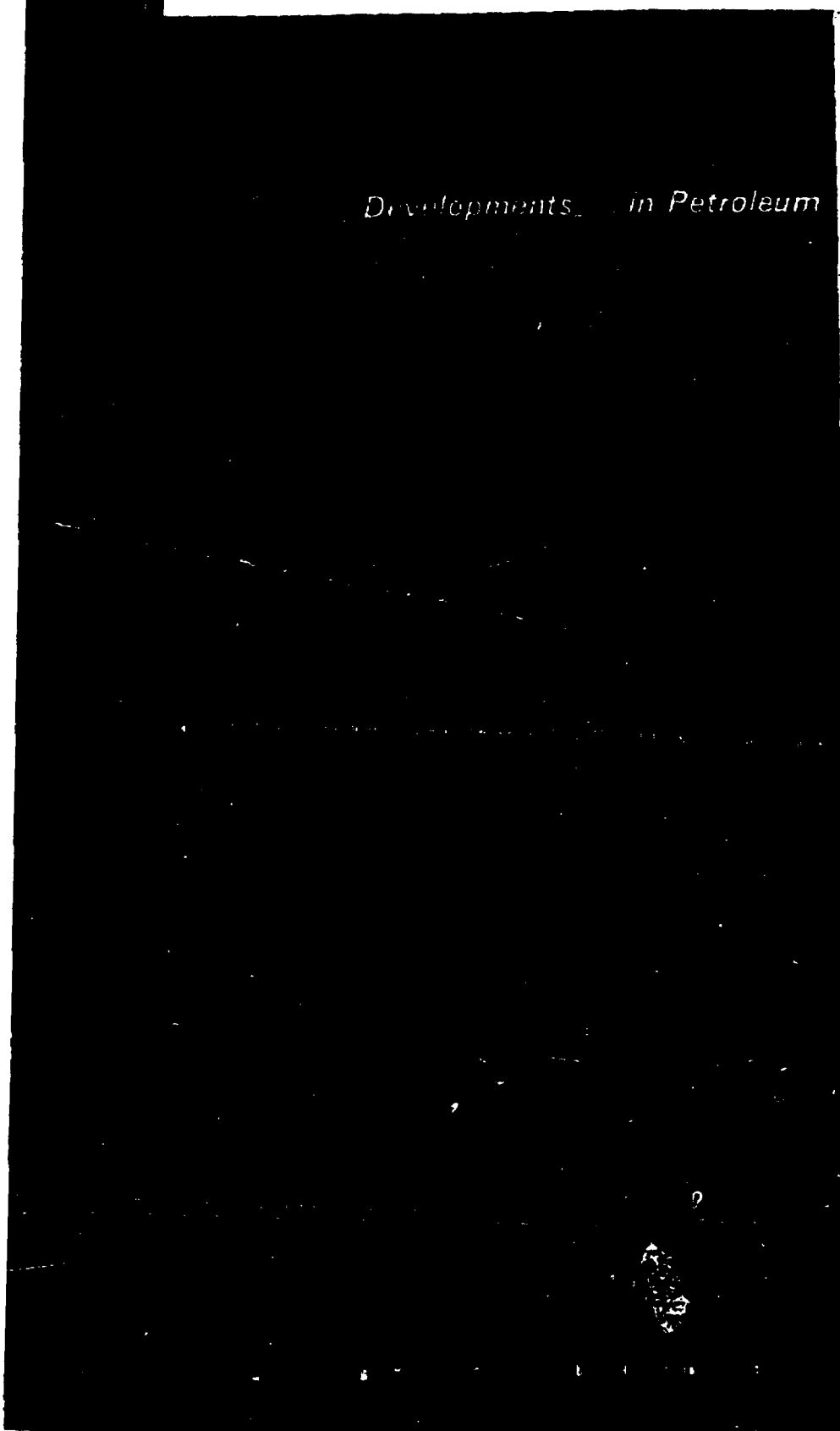
Grace Petroleum Corporation reported slightly higher net income in 1966 compared with 1965. Oil production from the Raguba Field in Libya, in which the Company has a 24½% working interest, averaged 96,750 barrels a day, which was somewhat higher than the production of the previous year. The oil produced is marketed to Esso Sirte Inc. and to European refiners.

Exploratory drilling continued in the Sirte Basin, where the Company has an interest with subsidiaries of Standard Oil Company (New Jersey) and Sinclair Oil Corporation. The future exploration drilling program will be based on an extensive seismic survey completed late in 1966.

• • •

The Ore and Mining Division of the Latin American Group has for many years engaged in worldwide trading and marketing, primarily of nonferrous minerals and metals. The Company also operates mining properties in Bolivia and Peru and conducts mineral exploration activities in various parts of the world.

Results of these operations continue to be satisfactory. A major dredging operation of a tin placer in the Aviaya Valley in Bolivia is expected to be brought into production during the latter part of 1967.



Drilling rig, Sirte Basin, Libya


GRACE
Net Sales
FOOD AND
BEVERAGES
25

GRACE

Consolidated Statement of Income and Retained Earnings

	1966	1965*
	(IN THOUSANDS)	
REVENUES		
Sales and operating revenues	$1,278,682	$1,097,377
Dividends and interest	11,249	7,395
Net gain on disposition of properties and investments	2,116	3,729
	1,292,047	1,108,501
COSTS AND EXPENSES		
Cost of goods sold and operating expenses—Note 2	889,466	760,905
Selling, general and administrative expenses	216,901	187,875
Depreciation and depletion	50,320	43,901
Research and development expenses	17,037	15,943
Interest expense	32,025	24,760
U.S. and foreign taxes on income—Note 3	22,571	24,007
Unrealized foreign exchange losses	942	651
Income applicable to minority stockholders	3,186	1,577
	1,233,448	1,059,919
Income before extraordinary items	58,599	48,682
Gain (less tax) on sale of Pan American-Grace Airways, Inc. (1966); gain on sale of business and assets of Grace National Bank (1965)—Note 1	10,919	10,357
Net income	69,518	58,939
Retained earnings at beginning of year—Note 1	284,881	246,500
Dividends paid:		
W. R. Grace & Co.		
Preferred	912	912
Common ($1.27½ per share in 1966; $1.17½ in 1965)	21,101	18,201
Pooled companies—prior to combination with the Company	409	1,445
Retained earnings at end of year	$ 321,977	$ 284,881
PER SHARE OF COMMON STOCK		
Income before extraordinary items	$3.32	$2.80
Extraordinary items	.63	.61
Net income	$3.95	$3.41

Retained earnings include: (a) [illegible] (1965—[illegible]) of the retained earnings of Grace Line Inc., a wholly owned subsidiary, deemed not available for dividends since it is related to special funds under joint control with the U.S. Maritime Administration or invested therefrom in subsidized vessels; (b) [illegible] (1965—$13,[illegible]) set aside by foreign subsidiaries, principally as required by statute; (c) approximately [illegible] (1965—$35,[illegible]) which has been transferred to capital stock accounts on the books of subsidiary companies.

Parent company unappropriated retained earnings at December 31, 1966 amounted to $155,113,[illegible] (1965—$128,[illegible]). Of these retained earnings $42,200,000 were free of the restriction on payment of cash dividends imposed by the terms of the most restrictive of the Company's loan agreements.

*Certain figures have been restated

Consolidated Statement of Capital Surplus

	1966	1965*
	(IN THOUSANDS)	
Balance at beginning of year—Note 1	$161,354	$148,359
Excess of par or stated value of capital stock of companies acquired in poolings of interests transactions over the par value of the Company's shares issued in exchange—Note 1	—	1,892
	161,354	150,251
Excess over par value of common stock issued upon:		
Exercise of stock options	654	1,972
Conversion of 3½% subordinate debentures	1,989	3,960
Acquisition of various companies	20,614	8,441
Expenditures relating to acquisition of companies in poolings of interests transactions	(1,481)	(3,996)
Other	645	726
Balance at end of year	$183,865	$161,354

Consolidated Statement of Source and Application of Funds

	1966	1965*
	(IN THOUSANDS)	
SOURCE		
Net income	$ 69,618	$ 58,939
Provision for depreciation and depletion	50,320	43,901
Provision for deferred income taxes	4,071	2,476
Increase in long-term debt	54,918	124,154
Market value of common stock issued for Miller Brewing Company—Note 1	18,882	—
Proceeds from exercise of stock options, etc.	1,334	2,854
Other transactions	25,723	15,025
	$224,766	$247,370
APPLICATION		
Cash dividends	$ 32,422	$ 20,556
Net additions to properties and equipment and increase in investments	185,256	175,767
Increase in working capital	57,089	51,054
	$224,766	$247,370

For comparative purposes — See Note 1

GRACE

Consolidated Balance Sheet

ASSETS	December 31, 1966	1965*
	(In thousands)	
CURRENT ASSETS		
Cash, including time deposits of $51,247,000 (1965—$27,868,000)	$ 96,810	$ 84,712
U.S. Government and other marketable securities, at cost (approximate market value)	9,015	21,448
Notes and accounts receivable, less reserves of $7,866,000 (1965—$7,092,000)	272,605	196,970
Inventories—See page 28	254,183	216,985
Prepaid expenses	8,791	8,013
TOTAL CURRENT ASSETS	641,404	520,028
SPECIAL FUNDS AND DEPOSITS—Note 2	22,790	38,619
OTHER ASSETS—Note 1		
Investment in Marine Midland Corporation	30,515	30,515
Investment in The Ruberoid Co., at cost	27,714	—
Investments in and advances to unconsolidated subsidiaries and 50% owned companies, at cost	12,646	11,146
Miscellaneous investments, at cost or less, and other assets	45,973	40,599
Goodwill, less amortization of $3,327,000 (1965—$2,460,000)	32,615	18,609
TOTAL OTHER ASSETS	149,463	100,869
PROPERTIES AND EQUIPMENT, at cost less accumulated depreciation and depletion of $405,383,000 (1965—$338,632,000)—See page 28	646,928	553,905
	$1,461,585	$1,213,441

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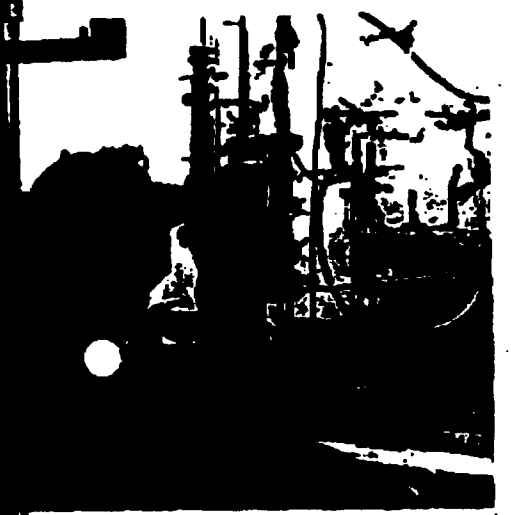
*Certain figures have been restated



Microsphere research, Washington Research Center

	December 31, 1968	1968*
LIABILITIES	(IN THOUSANDS)	
CURRENT LIABILITIES		
Loans payable—See page 29	$ 180,277	$ 95,784
Accounts and acceptances payable	149,810	128,101
U.S. and foreign taxes on income—Note 5	25,191	20,983
Other current liabilities	28,948	24,291
TOTAL CURRENT LIABILITIES	383,426	269,159
DEFERRED TAXES ON INCOME—Note 3	27,543	24,550
FOREIGN SOCIAL-LAW OBLIGATIONS AND OTHER NON-CURRENT LIABILITIES	24,997	28,349
DEFERRED INCOME	7,184	6,189
LONG-TERM DEBT—See page 29	443,829	388,911
EQUITY OF MINORITY STOCKHOLDERS IN CONSOLIDATED SUBSIDIARIES	48,705	20,613
	915,664	737,751
STOCKHOLDERS' EQUITY		
CAPITAL STOCK—Note 4		
Preferred stock outstanding	12,331	12,336
Common stock issued and outstanding—$1.00 par	17,728	17,139
CAPITAL SURPLUS, per accompanying statement	183,865	161,334
RETAINED EARNINGS, per accompanying statement	331,977	284,881
	545,901	475,710
	$1,461,565	$1,213,461

*For comparative purposes—See Note 1

GRACE

Notes to Financial Statements

NOTE 1—PRINCIPLES OF CONSOLIDATION:

The consolidated financial statements include the accounts of W. R. Grace & Co. and all majority owned and controlled domestic and foreign subsidiary companies. The assets and liabilities of the Company's foreign subsidiaries have been translated into United States dollars at year-end rates of exchange (for Brazil the devalued rate which took effect in February 1987 was used), except that fixed assets and related depreciation and certain imported inventories have been translated at rates prevailing at dates of acquisition. Income and expenses (other than depreciation) have been translated at rates prevailing during the year.

The Company's equity in the aggregate net earnings of its principal 50%-owned companies (Gulf & South American Steamship Co., Inc. and Productora de Papeles S.A.) for 1986 exceeded dividends received from these companies by $1,680,000. The Company's equity ($18,340,000) in the net assets as shown by the financial statements of these companies at December 31, 1986 exceeded the cost of its investments in the companies by $10,200,000.

During 1986 the Civil Aeronautics Board approved the sale of the Company's 50% interest in Pan American-Grace Airways, Inc. to Braniff Airways, Incorporated and in January 198[illegible] Company received the total proceeds of $15,000,000. In accordance with the Accounting Principles Board Opinion No. 9, "Reporting the Results of Operations," the gain on this transaction of $10,319,000, net of related U.S. income taxes of $5,581,000, has been shown as an extraordinary item in the Consolidated Statements of Income and Retained Earnings. In compliance with the Opinion, the Company's equity in the gain on the sale of business and assets of Grace National Bank ($10,357,000) which had been credited directly to retained earnings in 1985 has been shown as an extraordinary item in the 1986 Consolidated Statements of Income and Retained Earnings.

In September 1986 the Company acquired approximately 59% of Miller Brewing Company in exchange for $10,000,000

INVENTORIES	December 31, 1986	December 31, 1985*
	(IN THOUSANDS)	
Raw and packaging materials	$ 72,125	$ 56,434
In process	20,058	14,698
Finished products	106,387	89,587
General merchandise, commodities, etc.	31,022	27,849
Stores and supplies	24,581	18,517
	$254,183	$206,885

Inventories are stated at the lower of cost or market. Market for raw and packaging materials and stores and supplies is based on replacement cost and for other inventory classifications on net realizable value. Due to the diversified nature of the companies' operations, several bases of determining cost are used, including first in-first out, last in-first out, average and specific cost.

*Restated for comparative purposes—See Note 1.

PROPERTIES AND EQUIPMENT	Gross Book Value	Depreciation & Depletion
	(IN THOUSANDS)	
Land	$ 61,308	$ 3,161
Producing and undeveloped oil properties	5,708	863
Buildings	304,760	79,813
Machinery, equipment, etc.	557,714	273,805
Vessels and marine property	141,750	47,741
Projects under construction	81,051	—
	$1,052,291	$405,383

in cash and 402,801 shares of its common stock. The Consolidated Statement of Income and Retained Earnings includes the results of Miller's operations for the period from September 22, 1966 to December 31, 1966. The excess of the purchase [illegible] over the equity in the book value of the underlying net assets of Miller amounted to $8,544,000. This amount was charged to goodwill and is not being amortized since it is considered to represent a continuing trade-name value.

In 1966 and January 1967 the Company acquired the assets and businesses or stock of Nalley's, Inc., Leaf Brands, Inc. and several other companies in exchange for shares of its common stock. For accounting purposes certain of these transactions have been treated as poolings of interests. Accordingly, the Consolidated Statement of Income and Retained Earnings includes the results of operations for the entire year and the comparative financial statements for 1965 have been restated to include the accounts of these companies.

The investment in Marine Midland Corporation consists of 277,005 shares of a $5.00 Convertible Preferred Stock received upon liquidation of Grace National Bank of New York. The investment is carried at the value established when the stock was received.

In March 1966 the Company purchased 1,005,120 shares of the capital stock of The Ruberoid Co. for $25 a share pursuant to a tender offer and purchased in the open market during 1966 an additional 85,080 shares (all amounts adjusted for a two-for-one stock split in December 1966). On March 2, 1967 the Company entered into an agreement providing for the sale of its investment in The Ruberoid Co. to General Aniline & Film Corporation for $27.50 a share. General Aniline's obligation to purchase this investment is subject to the merger of Ruberoid and General Aniline.

Miscellaneous investments and other assets include $8,835,000 at December 31, 1966 and $4,630,000 at December 31, 1965, representing deferred preoperating costs of two subsidiaries, Nuclear Fuel Services, Inc. and Federation Chemicals Limited. These costs are being amortized over future periods.

LONG-TERM DEBT	Interest Rates	Years of Maturity	Due Within One Year(1)	Due After One Year
			(IN THOUSANDS)	
W. R. GRACE & CO.				
Promissory notes	5-5½	1967-80	$ 5,222	$120,112
Promissory notes (2)	5¼	1972-91	—	50,000
Promissory note	4½	1969	—	20,000
Promissory notes	5¼-6.45	1967-80	155	6,405
Subordinate debentures (3)	4¼	1976-80	—	83,469
Sundry indebtedness			1,709	16,617
			7,086	304,601
SUBSIDIARY COMPANIES				
Grace Line Inc.*				
Merchant Marine Bonds (4)	4.20-4.25	1967-78	**	12,664
Merchant Marine Bonds (4)	4.20	1967-87	**	23,520
Mortgage notes	5¼	1967-70	**	4,800
Nuclear Fuel Services, Inc.				
Promissory notes	5½	1967-75	1,358	10,065
W. R. Grace Overseas Development Corporation				
Debentures (5)	5¾	1968-80	—	20,000
Debentures (6)	5	1976-86	—	15,000
Federation Chemicals Limited (7)				
Bank loan	5	1967-68	500	500
Subordinated notes, Series A	5¼-5¾	1968-77	—	27,220
Subordinated notes, Series B	5½-6½	1967-69	700	2,380
Sundry indebtedness			13	503
Other Subsidiaries			5,380	21,776
			$15,037	$443,829

(1) Included in current liabilities under loans payable.
(2) Under the loan agreements covering these notes, an additional $50,000,000 is scheduled to be taken down on March 15, 1967.
(3) Convertible into one share of common stock for each $95 principal amount.
(4) Sinking fund bonds—U.S. Government insured.
(5) Guaranteed by W. R. Grace & Co.
(6) Guaranteed by and convertible on and after August 1, 1967 into one share of the common stock of W. R. Grace & Co. for each $85 principal amount.
(7) See Note 6 for further information with respect to the long-term debt of Federation Chemicals Limited.
* See Note 5 for recent financing.
** Amount due within one year is payable out of special funds and deposits (see Note 8).

NOTE 3—SPECIAL FUNDS AND DEPOSITS:

The following amounts were included under this caption:

Special funds of Grace Line Inc. (including U.S. Government and other marketable securities at cost of $8,380,000)	$20,181,000
Other special and guaranty deposits	3,609,000
	$23,790,000

Grace Line Inc. operates under an operating-differential subsidy agreement with the United States Maritime Subsidy Board covering all of the company's regular routes and expiring on December 31, 1977.

The Grace Line Inc. special funds are composed of funds required under this agreement and escrow funds required in connection with financing agreements for the construction of specific ships. The agreement requires deposits in the special funds of (a) the company's 50% share of profits in excess of 10% of capital necessarily employed in subsidized operations (the remaining 50% being subject to recapture), (b) amounts equal to or in lieu of depreciation charges on subsidized vessels and containers, to the extent earned, and (c) proceeds from insurance, indemnity or sale of subsidized vessels and containers. The special funds may be used to purchase, construct or reconstruct vessels and containers (see Note 5) and to pay the principal of mortgage notes on vessels and under specified conditions may be transferred to the general funds of Grace Line Inc.

Under this agreement Grace Line Inc. is entitled to a subsidy representing the excess of certain of its costs over similar costs incurred by foreign-flag competitors. The subsidy is subject to recapture by the United States to the extent of 50% of the amount by which earnings from subsidized operations in each ten-year period exceed 10% of the capital necessarily employed in such operations. Any recapture is withheld by the United States from the subsidy receivable. Net subsidy of $20,417,000 (1965—$16,161,000) has been deducted from cost of goods sold and operating expenses in the Consolidated Statement of Income and Retained Earnings.

NOTE 2—U.S. AND FOREIGN TAXES ON INCOME:

The United States Internal Revenue Service has not completed examinations of the consolidated income tax returns of the Company and its domestic subsidiaries for 1956 and subsequent years. Examinations of tax returns in foreign countries have in some cases not been completed for the most recent years. It is believed, however, that provisions made in 1966 and earlier years are adequate.

Additional foreign and United States taxes might become payable if undistributed earnings of foreign subsidiaries were to be paid out as dividends, but such taxes, if any, have not been fully reserved for since a substantial portion of such earnings has been or will be reinvested.

Profits deposited in the special funds by Grace Line Inc. (see Note 3) are not subject to federal income taxes in the year earned. In the event that any profits are withdrawn from the special funds and paid into general funds the amounts would have to be included in taxable income of the year of withdrawal. No provision has been made for such taxes since the amounts, if any, are not presently determinable.

Depreciation is generally computed on the straight-line method over the estimated useful lives of the assets, whereas for income tax purposes depreciation is generally computed on accelerated bases. The excess depreciation taken for tax purposes over depreciation as recorded on the books has resulted in a tax deferral which has been included in the income taxes charged against earnings and credited to deferred taxes on income.

The application of the investment credit permitted w[illegible] the provisions of the 1962 Revenue Act has reduced the [illegible] tax provision by $3,821,000.

NOTE 4—CAPITAL STOCK:

The preferred stock (of $100 par) issued and outstanding is listed below:

	Shares Authorized and Issued	Shares in Treasury	Outstanding Shares	Outstanding Amount
6% Cumulative	40,000	2,774	37,226	$ 3,722,600
5% Cumulative Class A	50,000	1,868	48,132	4,813,200
5% Noncumulative Class B	40,000	2,049	37,951	3,795,100
				$12,330,900

In addition the Company's Certificate of Incorporation, as amended by the stockholders in May 1966, authorizes 3,000,000 shares of a Class C Preferred Stock, without par value, none of which was issued or outstanding at December 31, 1966.

Under the Company's Certificate of Incorporation the authorized common stock of the Company is 30,000,000 shares. Changes in the common stock during the year are summarized below:

	Shares
Balance, December 31, 1965	15,929,357
Exchange of common stock in poolings of interests transactions—Note 1	1,209,998
	17,139,355
Common stock issued upon:	
Conversion of 3½% subordinate debentures	84,076
Exercise of stock options	25,403
Exercise of stock options of pooled companies	24,777
Acquisition of various companies	452,000
Other transactions	165
Balance, December 31, 1966	17,727,836

On March 2, 1967 Sea-Pak Corporation was merged into the Company. In connection therewith the Company issued 220,797 shares of its common stock. For accounting purposes this transaction will be treated as a pooling of interests.

Of the unissued common stock, 1,853,626 shares have been reserved for conversion of the 4½% subordinate debentures and the 5% debentures of a subsidiary and for exercise of stock options.

At the beginning of 1966 options were outstanding for the purchase of 273,670 shares of common stock and 180,112 shares were available for granting of additional options. During 1966 options for 120,685 shares were granted at an average option price of $54.80. The option prices were not less than 100% of market on the respective dates of grant.

During the year options for 32,987 shares were exercised at an average option price of $28.18 and options for 17,904 shares terminated. At the end of the year options were outstanding for 343,464 shares at prices ranging from $19.56 to [illegible] per share or an average of $50.46, options for 106,348 [illegible]es were exercisable and 86,027 shares were available for granting of additional options. In addition 94,884 shares were available to cover options which may be assumed or granted in lieu of existing options granted by companies which may be acquired.

NOTE 5—COMMITMENTS AND CONTINGENT LIABILITIES:

Under the operating-differential subsidy agreement referred to in Note 2, Grace Line Inc. has agreed to award contracts during the period 1967-1972 to complete the replacement of its fleet if certain conditions of economic feasibility are met, subject, among other things, to the United States Government granting construction-differential subsidies to aid in the construction of the new ships. The estimate cost of the program is not presently determinable. In connection with this program Grace Line Inc. has construction contracts, and also construction-differential subsidy agreements with the United States Maritime Subsidy Board for six new cargo ships. Three of these cargo ships entered service in 1966 and the remaining three are scheduled to enter service in 1967. The cost to Grace Line Inc. of these six vessels is estimated at $42,200,000 of which approximately $35,000,000 has been expended or accrued at December 31, 1966. The cost is being financed from Grace Line's special funds and by $30,000,000 of U.S. Government Insured Merchant Marine Bonds which were issued in February 1967.

In connection with the issuance by Federation Chemicals Limited, a wholly owned subsidiary, of its 5¼-5½% Series A Subordinated Notes, due 1969 to 1977, and its 5¼-6½% Series B Subordinated Notes, due 1967 to 1969, the Company has agreed (1) to purchase, at a set price, all of the ammonia produced by Federation in excess of its requirements and (2) in addition to the Company's outstanding guarantee of Federation's 5% bank loan, due 1967 to 1968, under certain conditions to advance cash to Federation to meet payments required under its Series A and Series B Subordinated Notes. The Company is a party to a twenty-year charter arrangement for two specially constructed tankers to transport ammonia and a twenty-year lease for an ammonia conversion plant in North Carolina. The annual rentals under the charter and the lease are approximately $2,400,000.

There are several domestic and foreign pension plans presently in effect. The aggregate pension cost of the Company and its subsidiaries (excluding Latin American subsidiaries) in 1966 was $5,372,000. The unfunded amount of past service benefits, which are being provided for by payments to trustees over a period of years, at December 31, 1966 was estimated to be $8,429,000. Pension payments are made to employees of the Latin American subsidiaries in accordance with the social laws of those countries in which operations are conducted. The costs of these plans have not been actuarially determined, but their estimated costs are being provided by periodic charges to income.

There are various lawsuits, claims, commitments and contingent liabilities but they are not expected to have any material adverse effect on the consolidated financial position or results of operations.

Opinion of Independent Accountants

PRICE WATERHOUSE & CO. 60 Broad Street, New York 10004

To the Stockholders and Board of Directors of W.R. Grace & Co.

In our opinion, the accompanying consolidated balance sheet, the related consolidated statements of income and retained earnings and capital surplus and the consolidated statement of source and application of funds present fairly the financial position of W. R. Grace & Co. and its consolidated subsidiary companies at December 31, 1966, the results of their operations and the supplementary information on funds for the year, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year as restated (see Note 1). Our examination of these statements was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

March 9, 1967

Price Waterhouse & Co.

GRACE

Ten-Year Financial Summary

EARNINGS STATISTICS[1] (IN THOUSANDS EXCEPT AMOUNTS PER SHARE)

Year	Sales and Operating Revenues	Income Before Depreciation and U.S. and Foreign Taxes	Depreciation and Depletion	U.S. and Foreign Income Taxes	Income Before Extraordinary Items	
					Total	Per Share[2]
1957	$ 499,736	$ 44,124	$17,821	$10,200	$16,103	$1.56
1958	494,234	48,178	20,718	8,485	18,995	1.84
1959	476,790	50,508	21,925	12,197	16,486	1.51
1960	502,871	54,251	23,201	9,860	16,220	1.48
1961	534,809	61,108	23,218	15,000	18,830	1.73
1962	561,532	72,901	31,500	18,784	22,617	1.58
1963	609,587	84,595	30,694	20,640	33,499	2.29
1964	876,201	104,348	37,542	24,065	42,740	2.72
1965	1,007,377	115,490	43,981	24,807	48,502	2.80
1966	1,270,482	152,490	50,300	23,571	58,998	3.32

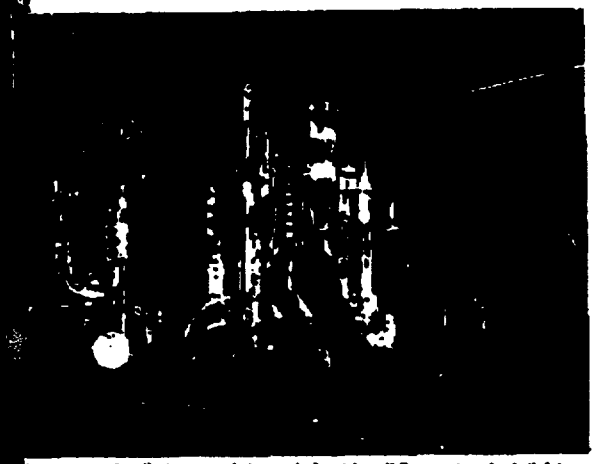
BALANCE SHEET STATISTICS[1] (ALL DOLLARS IN THOUSANDS EXCEPT AMOUNTS PER SHARE)

Dec. 31	Net Working Capital	Properties and Equipment		Capital Expenditures	Long-Term Debt
		Gross	Net		
1957	$120,632	$ 337,084	$207,546	$ 63,674	$126,849
1958	130,296	362,602	221,552	41,211	163,503
1959	158,136	392,136	252,735	54,242	168,310
1960	153,652	475,107	275,332	51,529	194,501
1961	136,035	512,923	297,184	55,925	203,486
1962	146,908	588,953	340,928	61,552	233,944
1963	157,368	649,882	347,769	74,875	226,228
1964	188,841	710,403	438,864	100,595	261,978
1965	250,880	892,557	555,975	154,784	388,911
1966	287,978	1,052,291	646,968	148,196	448,829

(1) Includes data with respect to companies acquired in poolings of interests transactions but only for the year in which such transactions occurred and the preceding year. On the basis of including the operations of pooled companies prior to 1965, results for the years 1962 through 1964 would have been as follows:

	Sales and Operating Revenues	Income Before Extraordinary Items	Per Share	Net Income	Per Share
1962	$623,500	$30,511	$1.68	$30,511	$1.68
1963	684,636	37,322	2.35	37,322	2.35
1964	906,206	45,098	2.71	44,798	2.69

32 34



Applied research is carried out by all Grace chemical divisions.

Net Income		Average Number of Common Shares Outstanding	Dividends on Common Stock (2)		Year
Total	Per Share(3)		Total	Per Share(3)	
$16,353	$1.56	9,888	$10,541	$1.07	1957
10,995	1.01	9,920	9,683	.98	1958
16,406	1.51	10,271	7,343	.72	1959
16,239	1.48	10,304	7,580	.74	1960
18,830	1.73	10,365	7,779	.75	1961
22,617	1.93	11,251	9,261	.84	1962
33,489	2.29	14,189	13,704	.96	1963
45,900	2.93	15,362	16,647	1.08	1964
58,939	3.41	17,021	19,646	1.18	1965
69,518	3.93	17,357	21,516	1.28	1966

Minority Interest	Stockholders' Equity		Book Value Per Share(3)	Number of Common Stockholders	Dec. 31
	Preferred Stock	Common Stock			
$12,070	$12,608	$222,369	$22.33	24,530	1957
6,884	12,608	223,616	22.30	28,052	1958
7,305	12,608	235,269	22.58	30,052	1959
28,947	12,608	240,253	23.21	31,306	1960
30,234	12,608	254,444	24.13	27,814	1961
36,841	12,608	288,236	24.88	30,919	1962
15,175	12,608	339,199	25.43	40,142	1963
19,201	12,346	391,141	25.27	41,790	1964
20,613	12,336	463,374	27.04	45,053	1965
18,705	12,331	533,570	30.10	45,655	1966

(2) The aggregate amount of cash dividends on common stock includes the dividends paid by pooled companies while the per share amount represents the rate paid by the Company only.

(3) Per share figures have been adjusted to reflect two-for-one stock split in 1963 and 2% stock dividends paid on common stock each year from 1959 through 1964. Income per share is after deducting dividends paid on preferred stocks.

Sales and Revenues (DOLLARS IN MILLIONS)

	1957	1958	1959	1960	1961	1962	1963	1964	1965	1966
CHEMICALS	$171 [illegible]	$175 40%	$216 45%	$237 43%	$259 48%	$331 56%	$430 64%	$564 61%	$688 63%	$809 63%
FOOD AND CONSUMER PRODUCTS	$ 32 7%	$ 26 6%	$ 27 6%	$ 30 5%	$ 26 5%	$ 27 4%	$ 89 13%	$109 12%	$200 18%	$213 [illegible]
LATIN AMERICAN MANUFACTURING AND COMMERCIAL OPERATIONS*	$ 82 18%	$ 83 19%	$ 75 16%	$ 74 14%	$ 67 13%	$ 57 10%	$ 60 9%	$ 81 9%	$ 92 8%	$101 8%
STEAMSHIP OPERATIONS	$ 84 18%	$ 78 18%	$ 74 15%	$ 69 12%	$ 65 13%	$ 71 12%	$ 75 11%	$ 84 10%	$ 73 7%	$ 94 7%
PETROLEUM AND OTHER ACTIVITIES	$ 91 20%	$ 70 17%	$ 85 18%	$143 26%	$117 21%	$105 18%	$ 26 3%	$ 38 5%	$ 44 4%	$ 41 3%
TOTAL	$460	$434	$477	$553	$535	$591	$700*	$876	$1,097	$1,279

Capital Expenditures

This table compares capital expenditures, including those of pooled companies, for 1965 and 1966. Net fixed assets of other companies acquired are included in the year of acquisition.

	1965	1966
CHEMICALS	$122,300,000	$ 75,300,000
FOOD AND CONSUMER PRODUCTS*	6,100,000	39,600,000
LATIN AMERICAN MANUFACTURING	5,700,000	9,700,000
OCEAN TRANSPORTATION	17,500,000	22,300,000
OTHER	3,200,000	1,200,000
	$154,800,000	$148,100,000

Net Fixed Assets (DOLLARS IN MILLIONS)

	1957	1958	1959	1960	1961	1962	1963	1964	1965	1966
CHEMICALS	$109 [illegible]	$111 [illegible]	$115 [illegible]	$128 47%	$144 48%	$165 49%	$220 63%	$277 65%	$375 68%	$391 [illegible]
FOOD AND CONSUMER PRODUCTS	$ 11 [illegible]	$ 13 6%	$ 13 6%	$ 13 4%	$ 14 5%	$ 20 6%	$ 25 7%	$ 41 9%	$ 53 9%	$103 [illegible]
LATIN AMERICAN MANUFACTURING AND COMMERCIAL OPERATIONS*	$ 25 [illegible]	$ 28 [illegible]	$ 34 [illegible]	$ 17 6%	$ 19 6%	$ 20 6%	$ 19 6%	$ 24 6%	$ 26 5%	$ 32 [illegible]
STEAMSHIP OPERATIONS	$ 44 [illegible]	$ 52 [illegible]	$ 52 [illegible]	$ 46 17%	$ 50 17%	$ 53 18%	$ 72 21%	$ 72 17%	$ 85 15%	$102 [illegible]
PETROLEUM AND OTHER ACTIVITIES	$ 19 [illegible]	$ 18 [illegible]	$ 19 [illegible]	$ 71 26%	$ 70 21%	$ 73 21%	$ 12 3%	$ 14 3%	$ 15 3%	$ 16 [illegible]
TOTAL	$208	$222	$233	$275	$297	$341	$348	$428	$554	$617

*Other than Chemicals and Food and Consumer Products.

GRACE

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