

MANAGEMENT'S DISCUSSION AND ANALYSIS

FOUR-YEAR SUMMARY

Kuraya Sanseido Inc. and its consolidated subsidiaries
Years ended March 31

	Millions of yen			Thousands of U.S. dollars (Note 1)	
	2001	2002	2003	2004	2004
For the Year:					
Net sales	¥1,073,016	¥1,222,222	¥1,274,503	¥1,283,926	\$12,112,509
Gross profit	96,741	106,644	114,923	116,805	1,101,934
Selling, general and administrative expenses	94,792	100,863	104,763	101,450	957,076
Operating income	1,949	5,781	10,160	15,355	144,858
Net income	1,337	2,951	5,016	7,879	74,330
Depreciation and amortization	4,025	4,866	5,204	5,709	53,858
Capital expenditures (payment base)	4,287	5,663	6,206	4,974	46,925
Per Share Data:					
Net income (Note 2)	¥ 9.80	¥ 21.67	¥ 36.48	¥ 55.19	\$0.52
Diluted net income	9.02	18.92	31.50	48.65	0.46
Total shareholders' equity (Note 3)	899.68	823.75	828.14	893.84	8.43
Cash dividends applicable to the period	12.00	12.00	12.00	12.00	0.11
At Year-End:					
Total assets	¥652,368	¥644,248	¥638,589	¥626,626	\$5,911,566
Interest-bearing debt	42,681	41,177	33,730	23,275	219,576
Total shareholders' equity	122,992	110,650	112,261	128,988	1,216,868
Ratios:					
Return on assets (Note 4)	0.4%	0.9%	1.6%	2.4%	
Return on equity (Note 5)	1.1	2.5	4.5	6.5	
Number of employees	8,226	7,780	7,741	7,468	

Notes: 1. The U.S. dollar amounts in this report represent translations of Japanese yen, for convenience only, at the rate of ¥106.00 to U.S. \$1.00, the approximate exchange rate on March 31, 2004.

2. Net income per share = (Net income - Officers' bonuses) / (Average shares outstanding during the year - Average treasury stock during the year)

3. Total shareholders' equity per share = (Total shareholders' equity - Officers' bonuses) / (Shares outstanding at end of year - Treasury stock)

4. Return on assets = Operating income / Average total assets

5. Return on equity = Net income / Average total shareholders' equity

Scope of Consolidation

The Kuraya Sanseido Group consists of KURAYA SANSEIDO Inc. ("Kuraya Sanseido" or the "Company") and 10 consolidated subsidiaries, and is primarily engaged in the business of wholesale distribution of pharmaceuticals and provision of related services.

Overview of Results

In the pharmaceutical industry, despite factors such as the effect of an increase in the co-payment rate for certain patients enacted in April 2003 and a contraction in demand for influenza and pollen allergy medications and other drugs, the market overall displayed moderate growth due to market expansion from new products.

The Kuraya Sanseido Group worked to secure stable profits by maintaining its rational pricing system, and reinforced sales capabilities by opening a new operating base in the strategic Tokai region and introducing information terminals for sales representatives to increase their performance. In addition, we worked to build stronger relationships with customers by upgrading the skills of sales representatives and promoting organizational development to further the introduction of a new business model

that combines scheduled deliveries and billing by volume used.

Moreover, to actively promote cooperation among Kuraya Sanseido Group companies and enhance and strengthen its management base, we transferred business related to the wholesale of pharmaceuticals in Ibaraki, Tochigi and Gunma prefectures to USHIODA SANGOKUDO YAKUHIN CO. LTD. (Mito), took over business related to the wholesale of pharmaceuticals in Fukushima Prefecture, from the same company, and took over business related to the wholesale of over-the-counter drugs of HEISEI YAKUHIN CO., LTD. (Gifu). IZUTSU PHARMACEUTICAL CO., LTD. (Kyoto) and HEISEI YAKUHIN CO., LTD. were each made wholly owned subsidiaries of the Company through a simple exchange of shares.

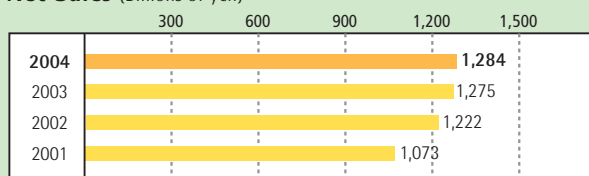
Furthermore, Kuraya Sanseido consolidated business offices and cut costs throughout the Group to reduce SG&A expenses. We also offered employees early retirement, and 102 employees applied. Moreover, we took steps to build a foundation for sharing and strengthening functions throughout the Kuraya Sanseido Group in the future. These steps included implementation of a new personnel system based on fair evaluation of performance in job standards, the integration of core systems in

the areas of sales, distribution and accounting, and construction of two new distribution centers in the city of Kazo, Saitama Prefecture, that will specialize in handling ethical drugs and healthcare products, respectively.

Sales and Operating Income

Consolidated net sales for the year ended March 31, 2004 increased 0.7 percent year-on-year to ¥1,283,926 million. Selling prices were stable due largely to the success of the Company's final cost formula and proprietary standard weighting price, which the Company created to formulate rational selling prices.

Net Sales (Billions of yen)



Gross profit increased 1.6 percent to ¥116,805 million, and the ratio of gross profit to net sales increased to 9.1 percent from 9.0 percent for the previous fiscal year. The increase reflected profit-oriented sales activities, the benefits of purchasing and distribution functions centered around mega-distribution centers, and the expansion of intragroup cooperation in marketing promotions.

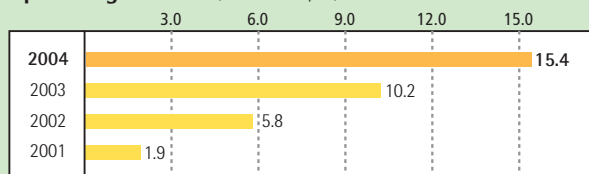
Selling, general and administrative (SG&A) expenses decreased 3.2 percent to ¥101,450 million. The ratio of SG&A expenses to net sales improved to 7.9 percent from 8.2 percent for the previous fiscal year, reflecting efficiencies from integrating systems for sales, distribution and accounting, cost reductions from the introduction of a new personnel system, and an upturn in investment returns on tax-qualified pension plan assets.

Costs, Expenses and Income as a Percentage of Net Sales

Years ended March 31	2002	2003	2004	Increase (decrease) 2004 vs. 2003
Cost of sales	91.3%	91.0%	90.9%	(0.1)
Gross profit	8.7	9.0	9.1	0.1
SG&A expenses	8.3	8.2	7.9	(0.3)
Operating income	0.5	0.8	1.2	0.4
Income before income taxes and minority interests	0.5	0.9	1.2	0.3
Net income	0.2	0.4	0.6	0.2

Operating income increased 51.1 percent to ¥15,355 million as a result of the improvement in the gross margin and success at reducing SG&A expenses.

Operating Income (Billions of yen)



Other Income (Expenses)

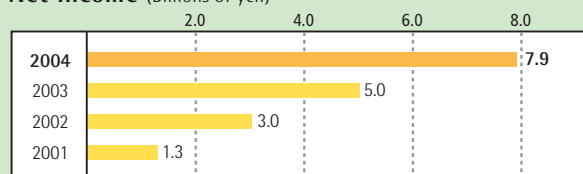
Total other income (expenses) amounted to a net expense of ¥261 million, compared to net other income of ¥1,041 million for the previous fiscal year. The primary factors in the year-on-year change were an increase in restructuring costs to ¥1,477 million and additional retirement benefits for employees in connection with the early retirement program, which totaled ¥1,362 million, compared to ¥1,079 million for the previous fiscal year. Both of these factors were included in other, net and explained in Note 11 to the Consolidated Financial Statements. Research fee income increased 10.9 percent to ¥3,201 million. Loss on devaluation of investment securities, which is a non-cash charge resulting from the application of Japan's fair value accounting standards, decreased 4.2 percent to ¥300 million. Reflecting the Company's consistent program of reducing interest-bearing debt, interest expense decreased 21.1 percent to ¥306 million, and the interest coverage ratio improved to 50.9 times, compared to 26.9 times for the previous fiscal year.

As a result of the above factors, income before income taxes and minority interests increased 34.8 percent to ¥15,094 million.

Net Income

Income taxes net of deferrals increased 20.9 percent to ¥6,859 million, primarily reflecting payment of deferred income taxes during the fiscal year. Net income increased 57.1 percent to ¥7,879 million. Net income per share improved to ¥55.19, compared to ¥36.48 for the previous fiscal year, and diluted net income per share improved to ¥48.65 from ¥31.50 for the previous fiscal year.

Net Income (Billions of yen)



Dividends

The Company places high priority on returning profits to shareholders. By increasing profitability, the Company strives to generate higher retained earnings for use in future business development and strengthening of operations, while also providing stable dividends to shareholders, taking recent performance into account. Cash dividends per share applicable to the fiscal year remained unchanged at ¥12.00. The payout ratio for the fiscal year was 26.8 percent.

Financial Strategy

The financial strategy of Kuraya Sanseido and its subsidiaries centers on maintaining sufficient liquidity and capital for operating needs and a sound balance sheet. Capital investment in plant and equipment is carried out according to clearly defined plans.

Liquidity and Financial Position

Net cash provided by operating activities increased 15.1 percent to ¥13,247 million. Cash generated through changes in working capital complemented the increase in income before income taxes and depreciation and amortization. Although the Kuraya Sanseido Group reduced trade payables, trade receivables, inventories and other current assets decreased, and other current liabilities increased. Working capital increased 46.2 percent from the previous fiscal year end to ¥24,658 million, and the current ratio was 1.05 times, compared to 1.04 times at March 31, 2003.

Net cash used in investing activities decreased 35.2 percent to ¥4,240 million. Net payments for purchase of property, plant and equipment decreased 25.7 percent to ¥3,680 million, and consisted of outlays for the Healthcare Higashinippon Distribution Center and other facilities.

Net cash used in financing activities decreased 28.2 percent to ¥7,270 million. The year-on-year change primarily resulted because the Company did not repurchase shares as it did in the previous fiscal year. The Kuraya Sanseido Group continued to reduce debt to strengthen its financial structure and reduce fixed interest expenses. Net decrease in short-term bank loans used cash totaling ¥4,960 million, and net repayment of long-term debt used cash totaling ¥630 million.

As a result, cash and cash equivalents at the end of the year increased 2.5 percent to ¥70,112 million.

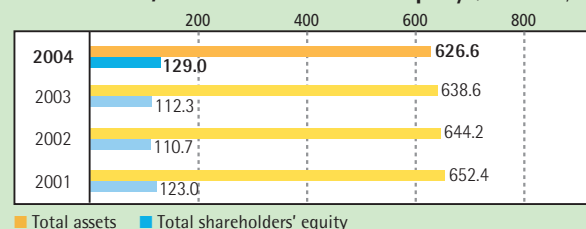
Cash Flow Highlights

Years ended March 31	Millions of yen			
	2002	2003	2004	Increase (decrease) 2004 vs. 2003
Net cash provided by operating activities	¥12,543	¥11,509	¥13,247	¥1,738
Net cash used in investing activities	(5,012)	(6,540)	(4,240)	(2,300)
Net cash used in financing activities	(4,356)	(10,123)	(7,270)	(2,853)
Cash and cash equivalents at end of year	73,934	68,375	70,112	1,737

Total assets at March 31, 2003 decreased 1.9 percent from a year earlier to ¥626,626 million, primarily reflecting the decrease in current assets through reduction in inventories and trade receivables. Shareholders' equity increased 14.9 percent to ¥128,987 million, reflecting increases in retained earnings

and unrealized gains on certain investment securities. The return on average total shareholders' equity increased to 6.5 percent from 4.5 percent for the previous fiscal year, and the ratio of shareholders' equity to total assets stood at 20.6 percent, compared to 17.6 percent a year earlier.

Total Assets / Total Shareholders' Equity (Billions of yen)



Capital Investment

The Kuraya Sanseido Group's capital investments in the year under review totaled ¥4,974 million. Primary investments were ¥2,645 million for expansion of the Healthcare Higashinippon Distribution Center in the pharmaceutical wholesale business, and ¥2,178 million for investment in software related to the integration of core systems for sales and distributions. The Kuraya Sanseido Group financed the entire amount of capital investment through internal capital.

Pension System

On April 1, 2004, Kuraya Sanseido adopted a new retirement benefit system consisting of a tax-qualified pension plan, which replaced the contract-based plan, and a new defined contribution pension plan and unfunded lump-sum retirement plan.

Outlook for the Fiscal Year Ending March 2005

Trends such as governmental measures to reform the health-care system and the shift of public hospitals to independent administrative agencies are expected to cause significant changes in the operating environment of the pharmaceutical wholesale industry.

On April 1, 2004, ATOL CO., LTD. and EVERLTH Co., Ltd. became wholly owned subsidiaries of Kuraya Sanseido using the share exchange system, and on May 1, 2004, NAKAGAWA SEIKODO CO., LTD. became a wholly owned subsidiary of Kuraya Sanseido by a simple exchange of shares. On October 1, 2004, the present KURAYA SANSEIDO Inc., upon becoming an operating holding company and changing its name to MEDICEO Holdings Co., Ltd., will separate its pharmaceutical wholesale business, which will become the new KURAYA SANSEIDO Inc. As a result of this company separation, the new KURAYA SANSEIDO Inc., ATOL CO., LTD., EVERLTH Co., Ltd. and NAKAGAWA SEIKODO CO., LTD. will all become wholly owned subsidiaries of MEDICEO Holdings Co., Ltd.

Kuraya Sanseido, YONYAKU CO., LTD. (Ehime Prefecture) and NAKAZAWA UJIKE PHARMACEUTICAL CO., LTD. (Kochi) entered into a business alliance covering all of their operations.

Amid predicted changes in the operating environment, the Kuraya Sanseido Group will make full use of its enhanced functions to raise efficiency and increase its corporate value by concentrating management resources, while maintaining its strength of community-based sales activities built up in each sales area. By doing so, the Group will promote the Medium-Term Consolidated Management Plan and work to further improve business results.

As a result, for the fiscal year ending March 31, 2005, Kuraya Sanseido (which will become MEDICEO Holdings Co., Ltd. as of October 1, 2004) projects consolidated net sales of ¥1,689.0 billion (a 31.5 percent increase year-on-year) and consolidated net income of ¥17.7 billion (a 124.6 percent increase year-on-year).

Operating and Other Risks

Risks related to specific legal regulations

Kuraya Sanseido and the Kuraya Sanseido Group handle various types of pharmaceuticals and related products, and conduct sales activities after receiving the necessary authorizations, registrations, designations and licenses from relevant local governments, pursuant to the Pharmaceutical Affairs Law and other laws and regulations. Inability to comply with these laws and regulations may result in restrictions on the Group's business activities.

Drug price standards

Ethical drugs, the primary product handled by the Kuraya Sanseido Group, are subject to National Health Insurance (NHI) drug price standards. The drug price standards stipulate the scope of drugs that can be used in health insurance treatment and the billing prices for the drugs used, and therefore function as an upper limit on selling prices. The drug price standards are, as a general principle, revised once every two years to reflect actual market prices. Because each revision lowers prices, the upper limit on selling prices also declines with each revision of the drug price standards, which has a material affect on net sales.

Revisions of drug price standards during the last five years were as follows:

NHI Drug Price Revisions

Implementation date	Average rate of decrease
April 1, 2000	7.0%
April 1, 2002	6.3%
April 1, 2004	4.2%

Sales discontinuations and product recalls

Business results may be affected in the event of situations such as the discontinuation of sales or recall due to defects, unforeseen side effects or tampering of certain products sold.

System risk

The business of Kuraya Sanseido and the Kuraya Sanseido Group is heavily reliant on computer network systems. Loss of functions due to a natural disaster, accident, infection by a computer virus or other occurrences may result in significant obstacles to product distribution.

Default risk

Business results would be affected in the event that a default occurs due to customer bankruptcy, civil rehabilitation or similar issues in regard to the receivables associated with ongoing transactions between Kuraya Sanseido and the Kuraya Sanseido Group and medical institutions.

Inventory risk

Kuraya Sanseido and the Kuraya Sanseido Group have inventories from suppliers. Business results may be affected in the event that selling prices decline or products become unsaleable due to supplier bankruptcy, civil rehabilitation or similar issues.

Litigation risk

Kuraya Sanseido and the Kuraya Sanseido Group may be a party to litigation related to product liability, the environment, labor or other matters in the course of conducting business activities.

Various other risks also exist, and the risks affecting the Kuraya Sanseido Group are not limited to the risks described above.