Kuraya Sanseido

MAXIMIZING THE VALUE OF MARKET LEADERSHIP

The MEDICEO Group will be the new leader of Japan's pharmaceutical distribution business. Over the next three years, we will continuously increase stakeholder value through our market leadership.

ANNUAL REPORT 2004

Fiscal year ended March 31, 2004

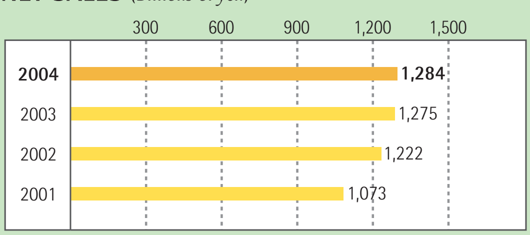
Financial Highlights

Kuraya Sanseido Inc. and its consolidated subsidiaries
Years ended March 31, 2003 and 2004

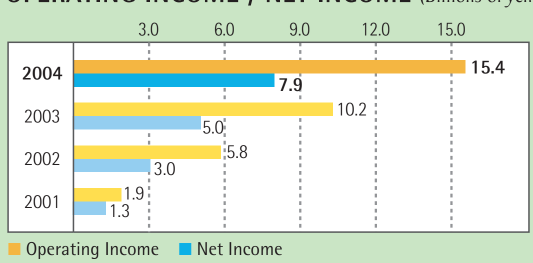
	Millions of yen		Percent change	Thousands of U.S. dollars (Note 1)
	2003	**2004**	2003/**2004**	**2004**
For the Year:				
Net sales	¥1,274,503	**¥1,283,926**	**0.7%**	**$12,112,509**
Operating income	10,160	**15,355**	**51.1**	**144,858**
Net income	5,016	**7,879**	**57.1**	**74,330**
At Year-End:				
Total shareholders' equity	¥ 112,261	**¥ 128,988**	**14.9%**	**$ 1,216,868**
Total assets	638,589	**626,626**	**(1.9)**	**5,911,566**
Per Share (Yen and U.S. dollars):				
Net income (Note 2)	¥ 36.48	**¥ 55.19**	**51.3%**	**$ 0.52**
Diluted net income	31.50	**48.65**	**54.4**	**0.46**
Cash dividends	12.00	**12.00**	**—**	**0.11**
Total shareholders' equity (Note 3)	828.14	**893.84**	**7.9**	**8.43**
Ratios:				
Return on assets (Note 4)	1.6%	**2.4%**		
Return on equity (Note 5)	4.5	**6.5**		

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

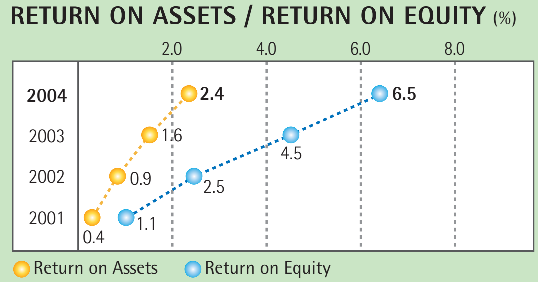
NET SALES (Billions of yen)



OPERATING INCOME / NET INCOME (Billions of yen)



RETURN ON ASSETS / RETURN ON EQUITY (%)



Profile

Kuraya Sanseido Inc. is the largest pharmaceutical wholesaler in Japan, a market that comprises 210,000 medical institutions. Adapting to a changing industry environment, Kuraya Sanseido is now creating the MEDICEO Group of leading wholesalers unified under an operating holding company structure. The MEDICEO Group will have 5,000 marketing specialists throughout Japan to handle the products of more than 2,000 pharmaceutical and medical manufacturers and serve some 131,000 customers. Kuraya Sanseido's strengths in large-scale distribution and the innovative use of information technology to serve customers and suppliers will continue to create a strong competitive advantage for the MEDICEO Group, which we project will have a market share of over 30 percent in both the Tokyo and Osaka areas, Japan's primary economic centers, the top share in each of Japan's six largest markets, and a 23.9 percent share nationwide, As the leader in our industry, we are committed to retaining the trust of our customers, suppliers and shareholders by adhering to the highest standards of ethics and operating efficiency. Our approach to increasing stakeholder value is based on benefiting fully from economies of scale and scope, effective cost management and innovative management of Group resources to add value.

Contents

Forward-Looking Statements

This annual report contains forward-looking statements regarding Kuraya Sanseido's plans, outlook, strategies and results for the future. All forward-looking statements are based on judgements derived from information available about the Company at the time of publication.

Certain risks and uncertainties could cause the Company's actual results to differ materially from any projections presented in this report. These risks and uncertainties include, but are not limited to, the economic circumstances surrounding the Company's business; competitive pressures; related laws and regulations; product development programs; and changes in exchange rates.

>>>To Our SHAREHOLDERS

The fiscal year ended March 31, 2004 was the second year of Kuraya Sanseido's medium-term consolidated management plan. We achieved growth in both sales and earnings for the third consecutive year by shifting toward profit-focused management and fully utilizing our advantages in the areas of purchasing and distribution. On April 1, 2004, Kuraya Sanseido began operations as the MEDICEO Group, a new corporate entity that will provide the framework for further growth.

Overview of Results

In the pharmaceutical industry during the year ended March 31, 2004, an increase in the rate of co-payments by certain patients took effect in April 2003, and demand for influenza and pollen allergy medications decreased. However, expansion due to new products supported moderate growth in the market as a whole.

In this environment, to actively promote cooperation among Kuraya Sanseido Group companies and to 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 that company's wholesale pharmaceutical business in Fukushima Prefecture, and acquired the wholesale over-the-counter drug business of HEISEI YAKUHIN CO., LTD. (Gifu).

IZUTSU PHARMACEUTICAL CO., LTD. (Kyoto) and HEISEI YAKUHIN CO., LTD. were both made wholly owned subsidiaries of the Company through a simple exchange of shares. Kuraya Sanseido also entered into a business alliance with YONYAKU CO., LTD. (Ehime Prefecture) and NAKAZAWA UJIKE PHARMACEUTICAL CO., LTD. (Kochi) covering all of their operations.

In addition to these developments, the Kuraya Sanseido Group continued to work toward the objectives of its medium-term consolidated management plan in its second year. In the ethical drugs segment, we worked to clearly specify final costs and set purchase prices at the beginning of the fiscal year, then to set and maintain selling prices arrived at from selling, general and administrative (SG&A) expenses in the final cost plus a fair profit. This helped us to ensure stable sales by enhancing our relationships of trust with customers.

Measures to strengthen sales included establishing a new operating base in the strategic Tokai region and introducing information terminals for marketing specialists (MSs) to improve their performance. We also worked to build stronger relationships with customers and to upgrade the skills of MSs in order to implement a new business model that combines scheduled deliveries and billing by volume used.

As a result of these factors, consolidated net sales totaled ¥1,283,926 million, an increase of 0.7 percent compared with the previous fiscal year. Gross profit increased 1.6 percent year-on-year to ¥116,805 million, reflecting our ability to maintain selling prices, enabling profit-focused management. Other factors included the advantages of the Company's supply and distribution system based around mega-distribution centers, and expansion of joint sales promotions and bulk purchasing with consolidated subsidiaries in the pharmaceutical wholesale business.

SG&A expenses decreased 3.2 percent year-on-year to ¥101,450 million due to the success of cost reduction measures such as the consolidation of sales branches, the integration of the Group's core systems for sales, distribution and accounting, and the introduction of a new personnel system, as well as an upturn in investment returns on tax-qualified pension plan assets.

Consequently, operating income was ¥15,355 million, a year-on-year increase of 51.1 percent. Net income rose 57.1 percent year-on-year to ¥7,879

million, as a gain on the transfer of the animal health products business offset expenses from special retirement benefits due to the early retirement program and the consolidation of sales branches, and a one-time loss on revision of the retirement benefit system. Cash dividends per share totaled ¥12.00 per share, the same as in the previous fiscal year.

Increasing Group Value

The basic strategy of the medium-term consolidated management plan, scheduled for completion in March 2005, is boosting competitiveness by restructuring resources, operations and functions. The Kuraya Sanseido Group has been working to enhance its operations based on this strategy. We have also taken steps to build a foundation for strengthening and sharing functions throughout the Group in the future. In addition to our efforts to maintain the trust of our customers and reduce costs, other measures during the past fiscal year included introduction of a new personnel system based on job standards and fair evaluation of performance, the integration of core systems in the areas of sales, distribution and accounting, and the establishment of two new distribution centers in Kazo, Saitama Prefecture, that will specialize in handling ethical drugs and healthcare products, respectively. Furthermore, in April 2004, Kuraya Sanseido changed to a retirement benefit system consisting of a tax-qualified pension plan that replaced the former contract-based plan, as well as a newly introduced defined contribution pension plan and an unfunded lump-sum retirement benefit plan.

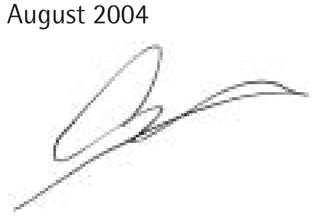
As the pharmaceutical wholesale industry undergoes a period of restructuring, the Kuraya Sanseido Group is working to further solidify its position as the industry leader while continuing to grow and develop. To this end, Kuraya Sanseido will become an operating holding company called MEDICEO Holdings Co., Ltd. on October 1, 2004. At that point, sixteen companies, including ATOL Co., Ltd. (Fukuoka) and EVERLTH Co., Ltd. (Hiroshima), which became consolidated subsidiaries in April 2004, and the new KURAYA SANSEIDO Inc., which will take over the pharmaceutical wholesale business, will commence business as the new MEDICEO Group.

We have formulated a new medium-term consolidated management plan for the three years from April 2004 to March 2007 to ensure a common strategic direction and target figures for the MEDICEO Group, and to establish a corporate structure capable of generating stable earnings.

The operating environment in the pharmaceutical wholesale industry is expected to change dramatically, with government reforms to the healthcare system reforms and the shift to independent administration at public hospitals. Under these conditions, the Kuraya Sanseido Group will increase operating efficiency and improve corporate value by deploying its industry leadership and maintaining its strengths in each of its businesses, while making the most of its enhanced capabilities and consolidating management resources. By doing so, we will carry out the objectives of the medium-term consolidated management plan and further improve results.

The MEDICEO Group has adopted a new management philosophy of "Contributing to people's health and the advancement of society through creation of value in distribution." Accordingly, we aim to increase our corporate value by strengthening our role and function in providing pharmaceutical products to medical institutions and other customers, and ultimately to patients and consumers. We ask for the continued trust and support of our shareholders and investors as we work to fulfill our mission.

August 2004



Sadatake Kumakura
President and Chief Executive Officer

>>>*INTERVIEW WITH PRESIDENT AND CEO*

SADATAKE KUMAKURA

Adapting to changes in the pharmaceutical wholesale industry, in April 2004 Kuraya Sanseido launched a new business group, the MEDICEO Group, to establish a position as a national wholesaler. Starting in October 2004, the MEDICEO Group will consist of 16 consolidated companies, with an operating holding company at the center. In the following interview, President and CEO Sadatake Kumakura explains the purpose of this reorganization, as well as future growth strategies.

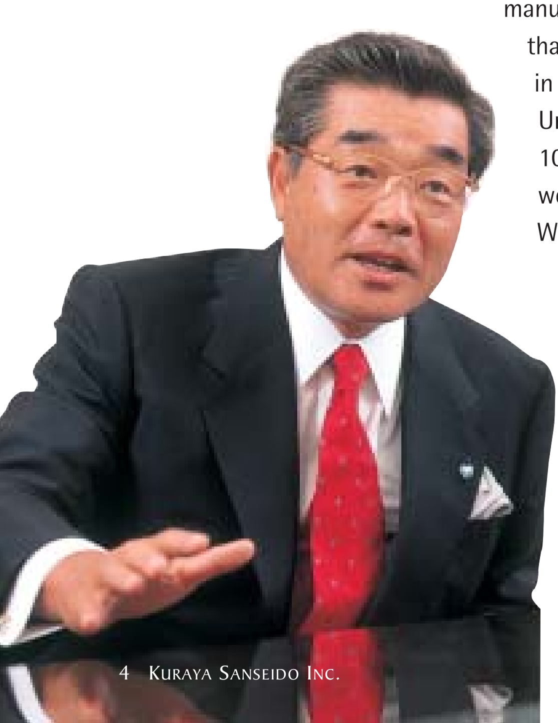
For the year ended March 31, 2004, Kuraya Sanseido posted growth in sales and income for the third consecutive year. What factors contributed to these positive results?

In the past fiscal year, we initiated a policy of establishing a new cost basis in our drive to be number one in our industry both in name and reality. The greatest weakness of our company has been a high level of selling, general and administrative (SG&A) expenses. We overhauled the fundamental structure of SG&A expenses to overcome this weakness. Key components of this effort were the integration of core systems and the introduction of a new personnel system. Because we were able to implement both measures at the beginning of the period, they contributed to results for the fiscal year.

System integration has been an issue since the merger. For more than two years, we worked to build new core systems that would enable efficient wholesale operations, and we completed this successfully. In October 2003, we began the staged integration of Group companies, which is moving ahead on schedule toward its completion in fall 2006. For the new personnel system, in April 2003 we shifted from a seniority-based wage system to one that is based on job standards and performance. This is rapidly bringing our personnel expenses under control, and was a factor in their decrease during the past fiscal year. The ratio of SG&A expenses to net sales has steadily declined for the past three years, and our success in setting up these basic structures will allow us to continue reducing these costs as planned.

Please explain the background to the formation of the MEDICEO Group.

The original impetus for our drive to become a national wholesaler was the entry of foreign manufacturers in the Japanese market. These companies generally have larger new drug pipelines than Japanese manufacturers, so we believed their market share in Japan would inevitably expand. One thing that foreign manufacturers all talked about was the high cost of pharmaceutical distribution in Japan. They pointed out that distribution in Japan costs more than in Europe and the United States, and asked why it costs 4-5 percent in the United States but as much as 9 or 10 percent in Japan. But since bypassing the wholesale system and conducting direct sales would cost even more, foreign manufacturers had no choice but to go through wholesalers. We thought that as long as they had to use a wholesaler, they would prefer an efficient one with nationwide operations, so we set out to become just such a wholesaler.



Subsequently, the division of prescription and dispensing functions took place, and the retail market began to shift from individual local pharmacies to nationwide dispensing pharmacy chains. This has further fueled the need for a national wholesale distributor. Furthermore, with the move to independent administration at public hospitals, medical institutions can now conduct nationwide bulk purchasing. Awareness that wholesale distributors will also need to be able to supply products on a national scale may prompt a wave of industry realignment. We have an advantage

The MEDICEO Group at the Start of Operations (April 1, 2004)

(Business alliance basis)

Number of Customers: 131,000
Manufacturers Handled: 2,000

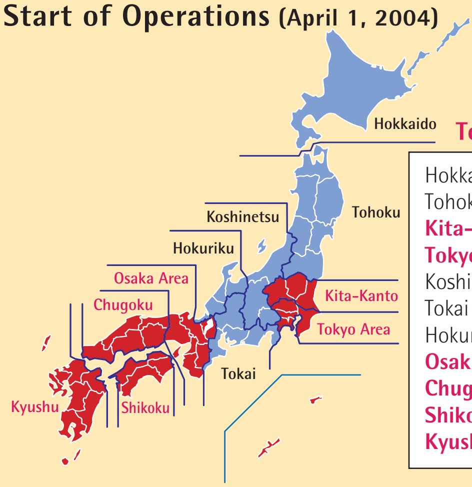
MEDICEO Group Share

(Business alliance basis)

Nationwide Share 23.9%

- Covered by the MEDICEO Group
- Areas where the MEDICEO Group holds the top share

Note: Based on prescription pharmaceutical market data from CRECON Research & Consulting for the year ended March 31, 2003.



Top Share in 6 Areas

Hokkaido	3.2%
Tohoku	13.8%
Kita-Kanto	**33.3%**
Tokyo Area	**30.1%**
Koshinetsu	13.9%
Tokai	11.7%
Hokuriku	14.2%
Osaka Area	**33.0%**
Chugoku	**29.7%**
Shikoku	**33.6%**
Kyushu	**22.3%**

Organization of the MEDICEO Group from October 1, 2004

Operating Holding Company

MEDICEO Holdings Co., Ltd.

Pharmaceutical Wholesale Companies

- SENSHU YAKUHIN CO., LTD.
- USHIODA SANGOKUDO YAKUHIN CO., LTD.
- Chiyaku Co., Ltd.
- KURAYA SANSEIDO Inc.
- YAMAHIRO KURAYA SANSEIDO Inc.
- HEISEI YAKUHIN CO., LTD.
- IZUTSU PHARMACEUTICAL CO., LTD.
- EVERLTH Co., Ltd.
- ATOL Co., Ltd.
- NAKAGAWA SEIKODO CO., LTD.
- HOSSP CORPORATION

Medical-Related Companies

- ORIENTAL PHARMACEUTICAL CO., LTD.
- KURAYA SHOJI, INC.
- KURAYA KASEI, INC.
- ELF Co., Ltd.

because we got an early start in integrating the MEDICEO Group, which has allowed us to establish a pharmaceutical supply network that extends to every prefecture of Japan except Okinawa.

What are the advantages and strengths of the MEDICEO Group?

Wholesalers are beginning to establish an important position in the pharmaceutical industry. As pharmaceutical manufacturers are battling for survival, they must concentrate their capital on research and development and overseas expansion, and are increasingly leaving domestic distribution to strong wholesalers. Another factor is that hospitals, our customers, are now required to report the number of acute and chronic beds, which will lead to a further decrease in the number of hospital beds. In addition, our customers' operating environment is undergoing major changes, such as the implementation of the Diagnosis Procedure Combination and the requirement for public hospitals to have independent administrative bodies. In this changing environment, our customers have a critical need to improve their management operations. They want a wholesaler who will support their management improvement and who can offer business suggestions directly linked to management efficiency.

The MEDICEO Group has several strengths that allow it to respond to these market changes. First, we have already established various infrastructures in the Group, whereas in most cases, companies start doing this after the group is formed. As a result, we already have core systems in place, and we also introduced a personnel system that incorporates performance-based elements first at Kuraya Sanseido, and plan to implement it at other Group companies as well. All the systems have been established, including distribution centers and a system for implementing joint sales promotion plans. Group companies are able to take advantage of this solid infrastructure, which will allow us to quickly and steadily exploit the benefits of management integration.

Our second strength is economies of scale. Starting from October 2004, the MEDICEO Group will be structured with an operating holding company, MEDICEO Holdings Co., Ltd., as the parent company. MEDICEO Holdings will promote business strategies for the entire group and conduct bulk purchasing functions, and will also centralize administrative functions and other general back-office operations for Group companies. The MEDICEO Group will have 5,000 marketing specialists (MSs), who are in charge of sales, and we intend to make full use of this sales force, the largest and most powerful in Japan, to generate the highest level of revenues in our industry.

The third strength is region-based sales. The pharmaceutical wholesalers in the MEDICEO Group are all influential companies in their areas, and currently have the number-one share in six areas — Kita-Kanto, the Tokyo and Osaka areas, Chugoku, Shikoku and Kyushu. By specializing in sales, these companies are able to tailor their business to their respective regions and achieve high productivity. We will use this system to further enhance customer support and our ability to gather and provide information.

These strengths mean that doing business with the MEDICEO Group offers advantages for both manufacturers and customers. Their understanding of these advantages will ultimately be our greatest strength.

The vision of the medium-term consolidated management plan drawn up recently is establishing the MEDICEO brand. What is the MEDICEO brand?

As I mentioned, the MEDICEO Group companies conduct region-oriented sales activities, and retaining their same corporate names and presidents makes it easier for them to join the Group.

Ordinarily, integration of companies takes the form of a merger. Although mergers can quickly bring about the benefits from management integration, one drawback is that they require uniform wages. To preserve regional wage differences while generating the same benefits as a merger, the best method in terms of management efficiency is bringing all systems, logistics and personnel together in a single framework, with an operating holding company at the center. This framework that achieves management efficiency while maintaining regional wage differences is the MEDICEO brand. The companies in the Group can take full advantage of the benefits generated from this shared framework as they work to increase their regional market shares. As a result, I believe the Group as a whole will be able to grow steadily.

What measures are you taking to raise the Group's overall strength by increasing the efficiency of the cost structure in areas such as marketing, distribution and purchasing?

We will continue pursuing a profit-oriented strategy. MEDICEO Holdings will carry out initiatives that affect the entire Group, such as expansion of bulk purchasing and implementation of unified sales promotion plans, and will continue to ensure compliance with our original standard weighted pricing system at Group companies. In workforce reductions, we plan to reduce the number of employees by 715 over three years and 1,200 by the end of the long-term vision in five years. After we complete system integration in autumn 2006, the cost benefits of this should become clear. Firmly establishing the MEDICEO Group framework at Group companies will take time, but we expect this effort to yield steady results.

ADVANTAGES AS THE MARKET LEADER

Sales	More than 5,000 marketing specialists (MSs), the most in the industry; leadership in pharmaceutical and healthcare markets.
Distribution	Nationwide coverage; leadership in the largest, fastest growing areas of Japan, including Tokyo.
Purchasing	Industry-leading purchasing volume reduces costs and supports earnings.
Personnel	Efficiencies from consolidation will support reduction in personnel to achieve sales per employee of ¥200 million.

TOWARD A HIGHLY EFFICIENT COST STRUCTURE

	Year ended March 2004	Year ending March 2007
SG&A	¥101.6 billion (7.9% of net sales)	¥129.0 billion (7.2% of net sales)
Employees	10,063	9,348
Gross Profit	¥114.7 billion (8.9% of net sales)	¥156.0 billion (8.7% of net sales)

Note: Amounts for the year ended March 2004 are estimates from the medium-term consolidated management plan announced on March 12, 2004.

What are your growth strategies in the OTC and medical equipment businesses, two strategic areas outside of the ethical drug business?

OTC Business

Under government policies to improve the finances of the National Health Insurance system, the consumer healthcare market is likely to grow further. Currently, the over-the-counter market accounts for 25 percent of total drug sales in the United States, but only 12 percent in Japan. We foresee the market expanding to twice its present size in the future, and believe we can leverage the successful experience we have accumulated in the ethical drug business in this market, too. If the large number of OTC wholesalers diminishes in the future, as we have seen happen in the ethical drug market, the business environment will change dramatically. In addition, retailers and drugstores, our customers in this area, do business on a national scale, yet there is still no national wholesaler. Because of these factors, there will certainly be a need for national wholesalers in the consumer healthcare field.

Medical Equipment Business

The medical equipment business is similar to the ethical drug business in that our customers are hospitals, clinics and pharmacies, so there is no need to develop new customers. The combination of NAKAGAWA SEIKODO CO., LTD., a medical equipment wholesaler that became a wholly owned subsidiary in May 2004, and Kuraya Sanseido's medical equipment division, together will have the highest sales in the industry.

Currently, the size of the medical equipment market is about ¥2.6 trillion, but there are as many as 300,000 companies registered to handle medical equipment. As the leader in this field, the MEDICEO Group plans to build the medical equipment business into a revenue-generating business. We expect to be able to establish a revenue base in this area earlier than in the consumer healthcare business, and intend to create the structure for this by the next fiscal year.

How do you plan to develop *medks-epi* and the Total Solution Model?

medks-epi

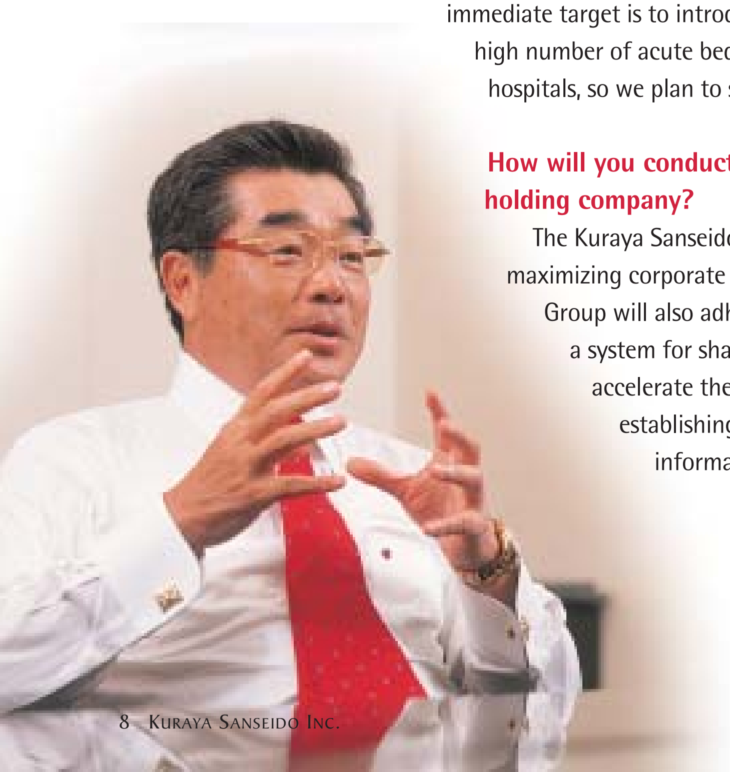
The *medks-epi* system is a contract model for dispensing pharmacies that combines planned deliveries and usage-based payment. Through the end of March 2004, *medks-epi* has been introduced at 1,437 locations. We have not yet reached our target of 3,000 locations, but having the system in place at more than 1,000 locations clearly shows that it has become a well-established model. The original purpose of *medks-epi* was to lower our costs by reducing the frequency of deliveries. But as the system has been implemented, another trend has emerged: the cash flow of customers who have adopted *medks-epi* has improved and their operations run more smoothly. For the year ending March 2005, we will try once again to introduce *medks-epi* at 3,000 locations, and will also seek to improve its quality and phase in its establishment at Group companies.

Total Solution Model

In the cost structure of hospitals, drug purchases account for about 20 percent of costs. Until now pharmaceutical wholesalers have generally not been able to provide support for the other 80 percent, which includes non-medical operations such as linen and food related work and medical coding and billing. By offering comprehensive support, we will reduce the burden of work on hospitals. This will help us to maintain our current share of sales to hospitals and ensure that the MEDICEO Group is on the winning side in non-price and added-value competition, rather than just price competition.

The centerpiece of the Total Solution Model will be recommending brands of pharmaceuticals and diagnostic materials for hospitals. In order to implement Diagnosis Procedure Combination and reduce medical errors, preparing a critical path that combines standardized treatment and pharmaceutical usage plans and procedures is becoming an important issue for hospitals, and we will provide support in that effort. Specifically, we will analyze how pharmaceuticals and other products are used and perform estimates of cost savings to create a list of standard brands of pharmaceutical products and diagnostic materials. By doing so, we can propose brand switches to conform to the budgets of hospitals.

We have been getting very good responses to the Total Solution Model in a one-year pilot project with numerous hospitals, and are now about to enter the phase of seriously implementing and expanding it. Our immediate target is to introduce the model in the current fiscal year at 30 of the 500 hospitals with a high number of acute beds. The Total Solution Model is designed for thorough incorporation into hospitals, so we plan to start out small and gradually expand it.



How will you conduct effective corporate governance under the new operating holding company?

The Kuraya Sanseido Group carries out its business activities based on the policy of maximizing corporate value while ensuring sound, transparent management. The MEDICEO Group will also adhere to the same fundamental policies. Moreover, we will quickly establish a system for sharing Group company information in real time. In particular, we will accelerate the speed of transmitting negative and risk-related information by establishing a crisis management system that facilitates the exchange of information.

Vision of the New Medium-Term Consolidated Management Plan
(April 2004–March 2007)

Establishment of the MEDICEO Brand

By working to reinforce and strengthen sales, purchasing and distribution functions and information systems, and meeting the wide-ranging needs of customers and partners, we will work to raise trust in the MEDICEO Group, further increase corporate value and expand its business domain.

Consolidated Management Targets (Year ending March 2007)

(Figures in parentheses are percentages of net sales)

Net sales	¥1,780 billion	
Operating income	¥27 billion	(1.5%)
Net income	¥23 billion	(1.3%)
Return on assets*	3.0%	
Return on equity**	10.5%	

* Return on assets = Operating income / Average total assets
**Return on equity = Net income / Average total shareholders' equity

MEDICEO Brand Logo

MEDICEO

Use of Human Form for the Letter "I"

> A company deeply involved with human life and health
> Corporate stance of promoting active, full lifestyles

Use of Red

> Symbolizes an energetic corporate group
> A group full of warmth and caring for people

How do you envision the future of the MEDICEO Group? In this regard, what will you do to raise shareholder value?

This year, Kuraya Sanseido for the first time made *Forbes* magazine's list of the World's 2,000 Leading Companies, entering at number 1,417. Among pharmaceutical manufacturers, Pfizer Inc. ranked 24th and Takeda Chemical Industries, Ltd. (currently Takeda Pharmaceutical Company Limited) was 226th. We were extremely pleased to be recognized as one of the world's leading companies.

As we embark on a new start as the MEDICEO Group, we believe we have grown into a socially essential corporate group. As we go forward, I want to build a structure in which we can grow steadily as a company with a valued presence in society. I believe that forming a corporate group that grows continually, one step at a time, rather than sharply, is our responsibility to all our stakeholders, including shareholders, customers, employees, consumers and society.

To live up to the expectations and trust of our shareholders, I believe it is important to expand earnings, pay stable dividends, and maintain or increase our stock price. I pledge to manage the MEDICEO Group so that loyal shareholders who support us and hold our stock for the long term will be rewarded.

Corporate Governance and Compliance

Basic Policies Concerning Corporate Governance

The Kuraya Sanseido Group focuses on ensuring transparent and sound management while maximizing corporate value.

The Board of Directors considers and decides on management policies and matters established by law, as well as other important management-related matters. The Board also supervises the status of overall business execution.

Corporate auditors conduct strict supervision of directors' execution of duties from the standpoints of legality and efficiency.

An Auditing Office reporting directly to the president conducts regular company-wide internal audits, with the aim of appropriate management and improvement spanning all aspects of business operations.

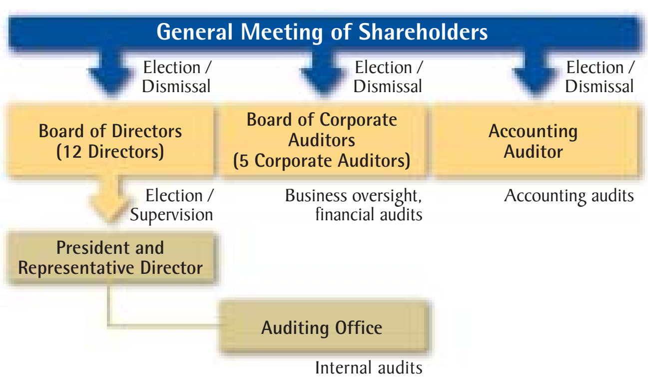
Implementation of Measures Concerning Corporate Governance

The Board of Directors is composed of 12 directors. This represents an increase of two implemented from April 1, 2004 in order to strengthen the management team in preparation for expansion of the Company's business scope by the exchange of shares. Board meetings are held once a month and are attended by corporate auditors. The Company uses the auditor system, and appoints three outside auditors among the five corporate auditors.

The Company has adopted an executive officer system to clearly separate management decision-making and supervision from business execution. In addition, a Management Meeting participated in by directors, executive officers and corporate auditors is held, in principle, once a week to share information on management strategies and consider business solutions.

Moreover, to help shareholders exercise voting rights more quickly and actively, Internet-based exercise of voting rights was implemented starting from the general meeting of shareholders held in June 2002.

Corporate Governance System (Non-Managerial)



Compliance Initiatives

The Company has established an Action Guidelines Committee whose members include the Company's advising attorney. The Committee is drawing up "Action Guidelines" that will form standards for judgment and action in carrying out activities to realize our corporate philosophy. It has also created "Basic Points for Business" as standards for legal compliance and sound business activities.

Currently, the Company is conducting initiatives such as regular meetings with individual divisions aimed at ensuring thorough knowledge and practice of these standards in order to improve corporate ethics.

Management Team

(As of June 29, 2004)

Genichiro Tanabe　Sadatake Kumakura　Osamu Takumiya

President and Chief Executive Officer

Sadatake Kumakura*

Vice Presidents

Osamu Takumiya*
(Executive Director of Sales)

Genichiro Tanabe*
(Management Reform Executive Director)

Directors

Kenichi Murata
(Executive Director of Medical Equipment Division)

Shuichi Watanabe
(Ethical Drug Sales Division Executive Director)

Bunichi Murayama
(Executive Director of Administration Division)

Akihiro Sakamoto
(Health Care Division Director)

Taro Kimura
(Management Planning Department Executive Director)

Taro Shintani
(Executive Director of Distribution Division)

Osamu Watanabe
(President, ATOL Co., Ltd.)

Takashi Saito
(President, EVERLTH Co., Ltd.)

Masahiko Masuyama
(Executive Director of Affiliated Business Division)

Shinichi Matsuo
(Director of Human Resources, Administrative Division)

Kazumi Takahashi
(Executive Director of Tokyo Regional Sales Division)

Yoshihiro Takatori
(Director of Account Department)

Corporate Auditors

Hideki Noguchi
(Statutory Auditor)

Yoshiharu Kataoka
(Statutory Auditor)

Akihiko Tanaka
(Statutory Auditor)

Yoko Sanuki
(Outside Auditor)

Yoshio Okamoto
(Outside Auditor)

*Representative Director

(As of July 1, 2004)

Chief Executive Officers

Kikuo Miki
(Director of Public and Investor Relations Department)

Renzo Konishi
(Executive Vice Director of Medical Equipment Division)

Akiyoshi Ohgane
(Senior Managing Director and Director of Business Supervisory Division, USHIODA SANGOKUDO YAKUHIN CO., LTD.)

Kazuo Misaki
(Information Technology Promotion Department Director)

Hidetaka Hata
(President and Representative Director, HEISEI YAKUHIN CO., LTD.)

Yoshio Imaichi
(Hyogo/Chugoku Regional Sales Division Director, Ethical Drug Sales Division)

Jyuichiro Ichiyama
(President and Representative Director, ORIENTAL PHARMACEUTICAL CO., LTD.)

Akira Moriwaki
(Osaka/Kiwa Regional Sales Division Director)

Senior Executive Officers

Masaaki Matsuishi
(Vice President and Representative Director, Director of Ethical Drug Sales Division, IZUTSU PHARMACEUTICAL CO., LTD.)

Hitoshi Higuchi
(Director of Purchase Planning Department, Ethical Drug Sales Division)

Yuzuru Sato
(President and Representative Director, SENSHU YAKUHIN CO., LTD.)

Takaharu Sako
(Director of Customer Support Center, Ethical Drug Sales Division)

Yoshiro Hasegawa
(Interregional Sales Coordination Department, Ethical Drug Sales Division)

Tsuyoshi Uehara
(Executive Director of System Division)

Executive Officers

Hiroyuki Maruyama
(Director, Ethical Drug Sales Division Deputy Director and Director of Reagents Division, IZUTSU PHARMACEUTICAL CO., LTD)

Kazutoshi Hashimoto
(Director of Reagent Sales, Ethical Drug Sales Division)

Kyujiro Shimomaki
(Distribution Division Executive Vice Director)

Masaaki Kobuchi
(Executive Director of Sales Division, SENSHU YAKUHIN CO., LTD.)

Fuminari Hikita
(Legal Affairs Director, Administrative Division)

Sakae Terauchi
(Hokkaido/Tohoku Regional Sales Division Director, Ethical Drug Sales Division)

Kazuyoshi Kamata
(Tokai Regional Sales Division Director, Ethical Drug Sales Division)

Toshio Hirasawa
(Director of Financial Affairs, Administrative Division)

Yuji Taniguchi
(Director of General Affairs, Administrative Division)

Yukihiro Hirosaka
(Hokuriku Regional Sales Division Director, Ethical Drug Sales Division)

Akio Nishimura
(Minami Kanto Regional Sales Division Director, Ethical Drug Sales Division)

Yasuhiro Choufuku
(Director of Sales Strategy, Ethical Drug Sales Division)

Hideaki Takemura
(Director of Medical Information, Ethical Drug Sales Division)

Kazunori Toyota
(Director of Management Coordination Committee)

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.

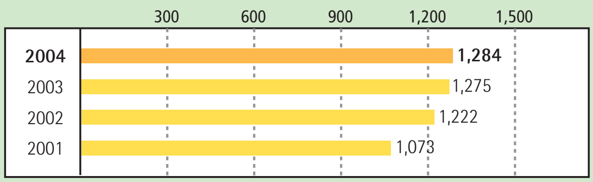
Moreover, to actively promote cooperation among Kuraya Sanseido Group companies and enhance and strengthen its management base, we transferred business related to the wholesale of pharmaceuticals in Ibaraki, Tochigi and Gunma prefectures to USHIODA SANGOKUDO YAKUHIN CO. LTD. (Mito), took over business 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.

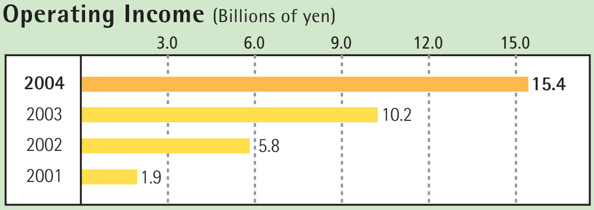
Selling, general and administrative (SG&A) expenses decreased 3.2 percent to ¥101,450 million. The ratio of SG&A expenses to net sales improved to 7.9 percent from 8.2 percent for the previous fiscal year, reflecting efficiencies from integrating systems for sales, distribution and accounting, cost reductions 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)

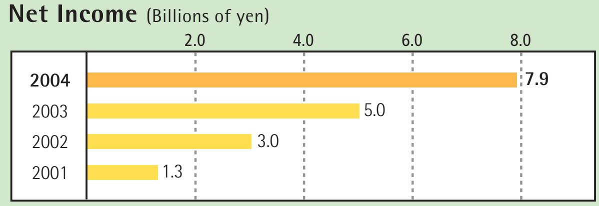
Total other income (expenses) amounted to a net expense of ¥261 million, compared to net other income of ¥1,041 million for the previous fiscal year. The primary factors in the year-on-year change were an increase in restructuring costs to ¥1,477 million and additional retirement benefits for employees 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.

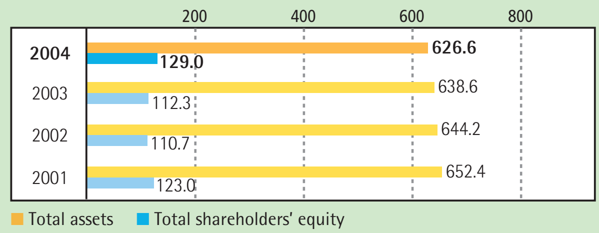
As a result, cash and cash equivalents at the end of the year increased 2.5 percent to ¥70,112 million.

Cash Flow Highlights

	Millions of yen			
Years ended March 31	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 healthcare 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.

CONSOLIDATED BALANCE SHEETS

Kuraya Sanseido Inc. and its consolidated subsidiaries
March 31, 2003 and 2004

	Millions of yen		Thousands of U.S. dollars (Note 1)
ASSETS	2003	**2004**	**2004**
Current assets:			
Cash on hand and in bank (Notes 3 and 8)	¥ 70,153	**¥ 70,646**	**$ 666,472**
Marketable securities (Note 4)	3	**3**	**28**
Notes and accounts receivable:			
Trade	340,233	**338,035**	**3,189,009**
Other	30,186	**23,458**	**221,302**
Allowance for doubtful accounts	(3,944)	**(2,892)**	**(27,283)**
Inventories	55,900	**52,955**	**499,575**
Deferred income taxes (Note 12)	4,126	**3,633**	**34,274**
Other current assets	1,895	**1,808**	**17,057**
Total current assets	498,552	**487,646**	**4,600,434**
Property, plant and equipment (Note 8)**:**			
Land (Note 5)	48,403	**46,805**	**441,557**
Buildings and structures	78,246	**76,591**	**722,557**
Machinery and equipment	6,745	**6,917**	**65,255**
Vehicles, furniture and fixtures	9,053	**9,106**	**85,905**
Construction in progress	54	**2,715**	**25,613**
	142,501	**142,134**	**1,340,887**
Accumulated depreciation	(47,036)	**(48,395)**	**(456,557)**
Net property, plant and equipment	95,465	**93,739**	**884,330**
Investments and other assets:			
Investment securities (Notes 4 and 8)	11,956	**15,004**	**141,547**
Long-term loans receivable	399	**325**	**3,066**
Allowance for doubtful accounts	(5,180)	**(5,790)**	**(54,623)**
Software	1,817	**5,189**	**48,953**
Deferred income taxes (Note 12)	7,679	**6,809**	**64,236**
Deferred income taxes — land revaluation (Note 5)	8,456	**7,975**	**75,236**
Consolidation difference	1,987	**1,156**	**10,906**
Other	17,458	**14,573**	**137,481**
Total investments and other assets	44,572	**45,241**	**426,802**
	¥638,589	**¥626,626**	**$5,911,566**

See accompanying notes.

LIABILITIES AND SHAREHOLDERS' EQUITY	Millions of yen 2003	Millions of yen 2004	Thousands of U.S. dollars (Note 1) 2004
Current liabilities:			
Short-term bank loans (Notes 6 and 8)	¥ 12,299	**¥ 7,339**	**$ 69,236**
Long-term debt due within one year (Notes 6 and 8)	969	**735**	**6,934**
Notes and accounts payable (Note 8):			
Trade	445,652	**433,696**	**4,091,472**
Other	4,550	**6,795**	**64,104**
Accrued expense	10,223	**9,237**	**87,142**
Income taxes payable (Note 12)	5,384	**2,840**	**26,792**
Other current liabilities	2,604	**2,346**	**22,132**
Total current liabilities	481,681	**462,988**	**4,367,812**
Long-term liabilities:			
Long-term debt (Notes 6 and 8)	20,462	**15,201**	**143,406**
Long-term accounts payable	—	**6,062**	**57,189**
Deferred income taxes — land revaluation (Note 5)	252	**234**	**2,208**
Employees' retirement benefits (Note 7)	16,420	**9,956**	**93,924**
Officers' retirement benefits	1,828	**1,854**	**17,490**
Other long-term liabilities	1,258	**651**	**6,141**
Total long-term liabilities	40,220	**33,958**	**320,358**
Minority interests	4,427	**692**	**6,528**
Contingent liabilities (Note 9)	—	**—**	**—**
Shareholders' equity (Note 10)**:**			
Common stock, par value ¥50 per share:			
Authorized – 500,000,000 shares in 2003 and 2004			
Issued – 142,424,946 shares in 2003 and 147,736,054 shares in 2004	12,751	**15,183**	**143,236**
Capital surplus	25,919	**30,064**	**283,623**
Retained earnings	87,875	**93,309**	**880,273**
Revaluation surplus (Note 5)	(12,260)	**(11,462)**	**(108,132)**
Unrealized gains on certain investment securities (Note 4)	2,602	**4,342**	**40,962**
Treasury stock, at cost	(4,626)	**(2,448)**	**(23,094)**
Total shareholders' equity	112,261	**128,988**	**1,216,868**
	¥638,589	**¥626,626**	**$5,911,566**

CONSOLIDATED STATEMENTS OF OPERATIONS

Kuraya Sanseido Inc. and its consolidated subsidiaries
Two years ended March 31, 2004

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	**2004**	**2004**
Net sales	¥1,274,503	**¥1,283,926**	**$12,112,509**
Costs and expenses:			
Cost of sales	1,159,580	**1,167,121**	**11,010,575**
Selling, general and administrative expenses	104,763	**101,450**	**957,076**
Total costs and expenses	1,264,343	**1,268,571**	**11,967,651**
Operating income	10,160	**15,355**	**144,858**
Other income (expenses):			
Research fee income	2,886	**3,201**	**30,198**
Interest and dividend income	261	**217**	**2,047**
Interest expense	(388)	**(306)**	**(2,886)**
Loss on devaluation of investment securities	(313)	**(300)**	**(2,830)**
Other, net (Note 11)	(1,405)	**(3,073)**	**(28,991)**
Total other income (expenses)	1,041	**(261)**	**(2,462)**
Income before income taxes and minority interests	11,201	**15,094**	**142,396**
Income taxes (Note 12)**:**			
Current	7,804	**6,328**	**59,698**
Deferred	(2,131)	**531**	**5,010**
Total income taxes	5,673	**6,859**	**64,708**
Minority interests in net income of consolidated subsidiaries	512	**356**	**3,358**
Net income	¥ 5,016	**¥ 7,879**	**$ 74,330**

	Yen		U.S. dollars (Note 1)
	2003	**2004**	**2004**
Amounts per share of common stock:			
Net income	¥36.48	**¥55.19**	**$0.52**
Diluted net income	31.50	**48.65**	**0.46**
Cash dividends applicable to the period	12.00	**12.00**	**0.11**

See accompanying notes.

Consolidated Statements of Shareholders' Equity

Kuraya Sanseido Inc. and its consolidated subsidiaries
Two years ended March 31, 2004

		Millions of yen		
	Number of shares of common stock issued (Thousands)	Common stock	Capital surplus	Retained earnings
Balance at March 31, 2002	136,706	¥11,153	¥24,321	¥84,537
Increase due to merger	—	—	—	57
Conversion of convertible bond into stock	5,719	1,598	1,598	—
Net income	—	—	—	5,016
Cash dividends paid (¥12.0 per share)	—	—	—	(1,610)
Bonuses to directors and statutory auditors	—	—	—	(17)
Increase due to the increase in consolidated subsidiaries	—	—	—	23
Loss on reverse of revaluation surplus	—	—	—	107
Retirement of treasury stock	—	—	—	(238)
Balance at March 31, 2003	142,425	¥12,751	¥25,919	¥87,875
Conversion of convertible bond into stock	**5,311**	**2,432**	**2,432**	**—**
Retirement of treasury stock, net of the cost	**—**	**—**	**1,713**	**—**
Net income	**—**	**—**	**—**	**7,879**
Cash dividends paid (¥12.0 per share)	**—**	**—**	**—**	**(1,645)**
Bonuses to directors and statutory auditors	**—**	**—**	**—**	**(151)**
Reverse of revaluation surplus	**—**	**—**	**—**	**(649)**
Balance at March 31, 2004	**147,736**	**¥15,183**	**¥30,064**	**¥93,309**

	Thousands of U.S. dollars (Note 1)		
	Common stock	Capital surplus	Retained earnings
Balance at March 31, 2003	$120,293	$244,519	$829,009
Conversion of convertible bond into stock	**22,943**	**22,943**	**—**
Retirement of treasury stock, net of the cost	**—**	**16,161**	**—**
Net income	**—**	**—**	**74,330**
Cash dividends paid (¥12.0 per share)	**—**	**—**	**(15,519)**
Bonuses to directors and statutory auditors	**—**	**—**	**(1,425)**
Reverse of revaluation surplus	**—**	**—**	**(6,122)**
Balance at March 31, 2004	**$143,236**	**$283,623**	**$880,273**

See accompanying notes.

Consolidated Statements of Cash Flows

Kuraya Sanseido Inc. and its consolidated subsidiaries
Two years ended March 31, 2004

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	**2004**	**2004**
Cash flows from operating activities:			
Income before income taxes	¥11,201	**¥15,094**	**$142,396**
Adjustments to reconcile income before income taxes to net cash flows provided by operating activities:			
Depreciation and amortization	5,204	**5,709**	**53,858**
Amortization of consolidation difference	732	**726**	**6,849**
Loss on disposal of property, plant and equipment — net	862	**1,771**	**16,708**
(Increase) decrease in employees' retirement benefits — net	1,811	**(6,464)**	**(60,981)**
Increase (decrease) in officers' retirement benefits	(28)	**26**	**245**
Increase (decrease) in accrued employees' bonuses	818	**(988)**	**(9,321)**
Increase (decrease) in allowance for doubtful accounts	374	**(443)**	**(4,179)**
Increase (decrease) in allowance for returns	29	**(6)**	**(57)**
Interest expenses	388	**306**	**2,887**
Interest and dividend income	(261)	**(217)**	**(2,047)**
Loss on sale and devaluation of securities — net	286	**296**	**2,792**
Loss on sale and devaluation of golf memberships — net	182	**37**	**349**
(Increase) decrease in notes and accounts receivable — trade	(2,872)	**1,464**	**13,811**
(Increase) decrease in inventories	(2,315)	**2,929**	**27,632**
Increase (decrease) in notes and accounts payable	1,496	**(11,956)**	**(112,792)**
Increase (decrease) in accrued consumption taxes	225	**(292)**	**(2,755)**
Decrease in other current assets	1,488	**6,788**	**64,038**
Increase (decrease) in other current liabilities	(1,772)	**7,968**	**75,170**
Payment of officers' bonuses	(22)	**(163)**	**(1,538)**
Interest and dividends received	261	**217**	**2,047**
Cash paid for interest	(386)	**(303)**	**(2,858)**
Cash paid for income taxes	(6,183)	**(8,873)**	**(83,708)**
Gain on sale of businesses	—	**(160)**	**(1,509)**
Others	(9)	**(219)**	**(2,065)**
Net cash provided by operating activities	¥11,509	**¥13,247**	**$124,972**

See accompanying notes.

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2003	**2004**	**2004**
Cash flows from investing activities:			
Payments for time deposits	¥ (1,659)	**¥ (265)**	**$ (2,500)**
Maturity of time deposits	1,990	**1,509**	**14,236**
Payments for purchase of property, plant and equipment — net	(4,954)	**(3,680)**	**(34,717)**
Payments for purchase of investment securities	(452)	**(117)**	**(1,104)**
Proceeds from sale of investment securities	169	**12**	**113**
Decrease in loans receivable — net	(10)	**(218)**	**(2,057)**
Payments for purchase of investment in subsidiary	(230)	**(12)**	**(113)**
Proceeds from sale of businesses	—	**397**	**3,745**
Other, net	(1,394)	**(1,866)**	**(17,603)**
Net cash used in investing activities	(6,540)	**(4,240)**	**(40,000)**
Cash flows from financing activities:			
Decrease in short-term bank loans — net	(3,641)	**(4,960)**	**(46,792)**
Proceeds from long-term debt	800	**400**	**3,774**
Repayment of long-term debt	(1,406)	**(1,030)**	**(9,717)**
Repayment of convertible bonds	(4)	**—**	**—**
Proceeds from issuance of common stock	4	**—**	**—**
Purchase of treasury stock	(4,250)	**(14)**	**(132)**
Cash dividends paid	(1,610)	**(1,645)**	**(15,519)**
Cash dividends paid to minority shareholders	(16)	**(21)**	**(199)**
Net cash used in financing activities	(10,123)	**(7,270)**	**(68,585)**
Effect of exchange rate change on cash and cash equivalents	3	**—**	**—**
Net increase (decrease) in cash and cash equivalents	(5,151)	**1,737**	**16,387**
Cash and cash equivalents at beginning of year	73,934	**68,375**	**645,047**
Cash and cash equivalents in connection with merger of non-consolidated subsidiary	13	**—**	**—**
Cash and cash equivalents in connection with exclusion of consolidation for certain subsidiary	(421)	**—**	**—**
Cash and cash equivalents at end of year	¥68,375	**¥70,112**	**$661,434**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Kuraya Sanseido Inc. and its consolidated subsidiaries
Two years ended March 31, 2004

1. Basis of presenting consolidated financial statements

Kuraya Sanseido Inc. and its consolidated subsidiaries (the "Company") maintain their accounts and records in accordance with the provisions set forth in the Japanese Commercial Code and the Securities and Exchange Law and in conformity with accounting principles and practices generally accepted in Japan, which are different from the accounting and disclosure requirements of International Accounting Standards.

The accompanying consolidated financial statements are a translation of the audited consolidated financial statements of the Company which were prepared in accordance with accounting principles and practices generally accepted in Japan from the accounts and records maintained by the Company and were filed with the Financial Services Agency as required by the Securities and Exchange Law.

In preparing the accompanying consolidated financial statements, certain reclassifications have been made in the consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan.

The translations of the Japanese yen amounts into U.S. dollars are included solely for the convenience of the reader, using the prevailing exchange rate at March 31, 2004, which was ¥106.00 to U.S.$1.00. The convenience translations should not be construed as representations that the Japanese yen amounts have been, could have been, or could in the future be, converted into U.S. dollars at this or any other rate of exchange.

2. Summary of significant accounting policies

Consolidation

Consolidated financial statements included the accounts of Kuraya Sanseido Inc. and ten domestic subsidiaries in 2003 and 2004, which are significant.

All material intercompany transactions and accounts have been eliminated. In the elimination of investments in subsidiaries, the assets and liabilities of the subsidiaries, including the portion attributable to minority shareholders, are recorded using the fair value at the time the Company acquired control of the respective subsidiaries.

Equity method

Investments in non-consolidated subsidiaries and affiliates over which the Company has the ability to exercise significant influence over operating and financial policies of the investees, are accounted for using the equity method.

Investments in other non-consolidated subsidiaries and affiliates are stated at cost, since net income and retained earnings in the aggregate of such companies are not material compared to those on a consolidated basis.

Consolidation difference

Consolidation difference is being amortized over mainly 5 years on a straight-line basis. Immaterial consolidation difference is charged to expense as incurred.

Cash flow statement

In preparing the consolidated statements of cash flows, cash on hand, readily available deposits and short-term highly liquid investments with maturities not exceeding three months at the time of purchase are considered to be cash and cash equivalents.

Marketable securities and investment securities

The Company adopted "Accounting Standards for Financial Instruments" issued by the Ministry of Finance ("MOF") on January 22, 1999. In accordance with the accounting standards, the Company's marketable and investment securities are considered as available-for-sale. Available-for-sale securities represent those securities that do not meet the classification of trading securities and held-to-maturity securities.

Available-for-sale securities are stated at fair value and the unrealized gains and losses are reported as a separate component of stockholders' equity. In cases where substantial impairment of value is recognized compared to fair value, the carrying amount is reduced to the fair value.

Inventories

Inventories are mainly stated at cost determined by the first-in, first-out (FIFO) method.

Property, plant and equipment

Depreciation of property, plant and equipment is computed by the declining-balance method with respect to the Company.

In accordance with revisions of the Corporation Tax Law, buildings acquired after March 31, 1998 are depreciated using the straight-line method.

Finance leases

Finance leases, except leases for which the ownership of the leased assets is considered to be transferred to the lessee, are accounted for in the same manner as operating leases.

Software costs

The Company included software in intangible assets and amortized it using the straight-line method over the estimated useful lives (five years).

Allowance for doubtful accounts

Allowance for doubtful accounts is recorded at an amount necessary to cover for possible losses from doubtful accounts based on the amount estimated to be uncollectable on an individual basis and from other accounts based on historical loss ratios.

Accrued employees' bonuses

At March 31, 2003 and 2004, the Company accrued the employees' bonuses based on estimated amounts to be paid in the subsequent period.

Employees' retirement benefits and pension

The Company adopted "Accounting Standards for Retirement Benefits" pronounced by MOF on June 16, 1998. In accordance with the accounting standards, allowance for employees' retirement benefits is recorded based on the projected benefit obligation less fair value of the pension plan assets. The experience adjustments of actuarial assumptions are amortized at the year incurred over three years using the straight-line method.

Effective April 1, 2004, Kuraya Sanseido Inc. amended its retirement benefit plan. The new plan consists of the defined benefit plan and defined contribution plan instead of tax-qualified pension plan and unfunded retirement plan, respectively. The Company adopted "Accounting for Amendment of Retirement Benefit Plan" pronounced by Financial Accounting Standards Foundation ("FASF").

Officers' retirement benefits

The Company pays retirement benefits to officers in accordance with its internal rules.

The Company provides for lump-sum severance payments for officers in the amount which would be required if all officers retired at each year-end. Such provision is not funded.

Income taxes

Income tax payable is computed based on the pretax income included in the consolidated financial statements. The asset and liability method is used to recognize deferred tax assets and liabilities for the expected future tax consequences of temporary differences.

Foreign currency translation

Monetary assets and liabilities of the Company are translated at the current exchange rates at the balance sheet date. The resulting foreign currency gains or losses are recognized as other income or expenses.

Amounts per share of common stock

The computations of net income per share of common stock are based on the average number of shares outstanding during each year. In accordance with "Accounting Standards for Net Income per Share" pronounced by FASF on September 25, 2002, the net income excludes the bonuses to directors and statutory auditors.

For computing diluted net income per share of common stocks, the average number of shares was increased by the number of shares that would have been outstanding assuming that domestic convertible bonds were converted on the date of issuance (September 11, 1996) at the actual conversion rates in effect during the year. Cash dividends per share represent the actual amounts declared during the respective years.

3. Cash and cash equivalents

Cash and cash equivalents at March 31, 2003 and 2004 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2003	**2004**	**2004**
Cash on hand and in bank	¥70,153	**¥70,646**	**$666,472**
Time deposits over three months	(1,778)	**(534)**	**(5,038)**
Cash and cash equivalents	¥68,375	**¥70,112**	**$661,434**

4. Market value information for securities

(1) Available-for-sale securities with a market value

	Millions of yen		
Year ended March 31, 2004	Carrying value	Estimated fair value	Unrealized gain
Securities whose fair value exceeds their carrying value:			
Equity securities	**¥3,843**	**¥12,303**	**¥8,460**
Government bonds and corporate bonds	**5**	**5**	**—**
Others	**—**	**—**	**—**
	¥3,848	**¥12,308**	**¥8,460**
Securities whose carrying value exceeds their fair value:			
Equity securities	**¥ 478**	**¥ 424**	**¥ (54)**
Government bonds and corporate bonds	**—**	**—**	**—**
Others	**—**	**—**	**—**
	¥ 478	**¥ 424**	**¥ (54)**
Total	**¥4,326**	**¥12,732**	**¥8,406**

	Thousands of U.S. dollars		
Year ended March 31, 2004	Carrying value	Estimated fair value	Unrealized gain
Securities whose fair value exceeds their carrying value:			
Equity securities	**$36,255**	**$116,066**	**$79,811**
Government bonds and corporate bonds	**47**	**47**	**—**
Others	**—**	**—**	**—**
	$36,302	**$116,113**	**$79,811**
Securities whose carrying value exceeds their fair value:			
Equity securities	**$ 4,509**	**$ 4,000**	**$ (509)**
Government bonds and corporate bonds	**—**	**—**	**—**
Others	**—**	**—**	**—**
	$ 4,509	**$ 4,000**	**$ (509)**
Total	**$40,811**	**$120,113**	**$79,302**

	Millions of yen		
Year ended March 31, 2003	Carrying value	Estimated fair value	Unrealized gain
Securities whose fair value exceeds their carrying value:			
Equity securities	¥2,701	¥8,154	¥5,453
Government bonds and corporate bonds	—	—	—
Others	—	—	—
	¥2,701	¥8,154	¥5,453
Securities whose carrying value exceeds their fair value:			
Equity securities	¥1,518	¥1,324	¥ (194)
Government bonds and corporate bonds	5	5	—
Others	—	—	—
	¥1,523	¥1,329	¥ (194)
Total	¥4,224	¥9,483	¥5,259

(2) Available-for-sale securities sold during the year

Two years ended March 31, 2004	Millions of yen 2003	Millions of yen 2004	Thousands of U.S. dollars 2004
Sales value	¥208	**¥15**	**$142**
Profit on sale	34	**4**	**38**
Loss on sale	7	**—**	**—**

(3) Securities without a market value and book value

Two years ended March 31, 2004	Millions of yen 2003	Millions of yen 2004	Thousands of U.S. dollars 2004
Held-to-maturity debt securities	¥ —	**¥ —**	**$ —**
Other securities	1,407	**1,373**	**12,953**

(4) Schedule for redemption of available-for-sale securities with a maturity and held-to-maturity debt securities

	Millions of yen				Thousands of U.S. Dollars	
	2003		**2004**		**2004**	
	Due within one year	Due after one year through five years	Due within one year	Due after one year through five years	Due within one year	Due after one year through five years
Bonds	¥3	¥5	**¥3**	**¥5**	**$28**	**$47**
Others	—	—	**—**	**—**	**—**	**—**
Total	¥3	¥5	**¥3**	**¥5**	**$28**	**$47**

5. Land revaluation

Under the “Law of Land Revaluation,” promulgated on March 31, 1998 and revised on March 31, 2001, the Company elected a one-time revaluation of its own-use land to a value based on real estate appraisal information as of March 31, 2002.

The resulting land revaluation excess represents unrealized appreciation of land and is stated, net of deferred tax assets and liabilities, as revaluation surplus as a component of shareholders’ equity. There is no effect on the statements of operations. Continuous readjustment is not permitted unless the land value subsequently declines significantly such that the amount of the decline in value should be removed from the land revaluation excess account and related deferred tax assets and liabilities. The details of the one-time revaluation as of March 31, 2004 were as follows:

	Millions of yen	Thousands of U.S. dollars
Land before revaluation	¥60,975	$575,236
Land after revaluation	41,658	393,000
Land revaluation excess (Net deferred tax)	11,462	108,132
Estimated fair value	35,366	333,642

6. Short-term bank loans and long-term debt

The Company has credit agreements with 20 banks in order to support effective financing. The lines of credit and bank loans under the credit agreements at March 31, 2003 and 2004 are listed below.

	Millions of yen 2003	Millions of yen 2004	Thousands of U.S. dollars 2004
Lines of credit	¥ 70,200	**¥72,300**	**$682,075**
Balance of bank loans	(10,995)	**(6,615)**	**(62,405)**
Net: Open lines of credit	¥ 59,205	**¥65,685**	**$619,670**

Short-term bank loans including loans under the credit agreement at March 31, 2003 and 2004 were principally bearing annual interest rates of 1.03% and 0.96% per annum, respectively.

Long-term debt at March 31, 2003 and 2004 consisted of the following:

	Millions of yen 2003	Millions of yen 2004	Thousands of U.S. dollars 2004
Unsecured domestic convertible bonds due 2008 at a rate of 0.9%	¥19,324	**¥14,459**	**$136,406**
Loans from banks due serially through 2016 at interest rates of 1.00% to 3.60% per annum - secured	2,107	**1,477**	**13,934**
	21,431	**15,936**	**150,340**
Less amount due within one year	(969)	**(735)**	**(6,934)**
Amount due after one year	¥20,462	**¥15,201**	**$143,406**

Domestic convertible bonds due 2008 provide, among other conditions, for (1) conversion prices of ¥916.0 ($8.60) and (2) convertible period from October 1, 1996 to September 29, 2008.

At the current conversion price, a total of 15,784 thousand shares of common stock were issuable upon full conversion of the domestic bonds outstanding at March 31, 2004.

The annual maturities of long-term debt at March 31, 2004 were as follows:

	Millions of yen	Thousands of U.S. dollars
2005	¥ 735	$ 6,934
2006	403	3,802
2007	194	1,830
2008	28	264
2009	14,474	136,547
Thereafter	102	963

7. Employees’ retirement benefits

(1) Overview of retirement benefit plan

The Company has defined retirement benefit plans covering a contributory trusteed employee pension plan established by the pharmaceutical industry, tax-qualified pension plans and unfunded retirement plans.

Effective April 1, 2004, Kuraya Sanseido Inc. amended its retirement benefit plan. The new plan consists of the defined benefit plan covering the contributory trusteed employee pension plan and new pension plan, instead of the tax-qualified pension plan and the defined contribution plan instead of the unfunded retirement plan.

(2) Retirement benefits

The following table reconciles the net fund status of plan to retirement benefits recorded in the consolidated balance sheets at March 31, 2003 and 2004.

	Millions of yen 2003	Millions of yen 2004	Thousands of U.S. dollars 2004
Projected benefit obligation	¥(35,900)	**¥(30,269)**	**$(285,557)**
Fair value of plan assets	17,107	**19,025**	**179,481**
Plan assets less than projected benefit obligation	(18,793)	**(11,244)**	**(106,075)**
Experience adjustments of actuarial assumptions	2,373	**1,288**	**12,151**
Reserve for retirement benefits	¥(16,420)	**¥ (9,956)**	**$ (93,924)**

Effects of providing the defined contribution plan instead of the unfunded retirement plan were as follows:

	Millions of yen	Thousands of U.S. dollars
Decrease in projected benefit obligation	¥7,811	$73,689
Unamortized experience adjustments of actuarial assumption	376	3,547
Decrease in employees' retirement benefits	¥7,435	$70,142

Loss on amendment to the pension plan amounted to ¥567 million ($5,349 thousand). Assets in the amount of ¥8,002 million ($75,491 thousand) will be contributed to the pension fund over a period of 4 years. The unpaid amount of ¥8,002 million ($75,491 thousand) was recorded in other current liabilities and long-term accounts payable in 2004.

(3) Net pension expense

The components of net pension expense in 2003 and 2004 are listed below.

	Millions of yen		Thousands of U.S. dollars
	2003	**2004**	**2004**
Service costs	¥2,693	**¥2,418**	**$22,811**
Interest cost on projected benefit obligation	1,066	**1,058**	**9,981**
Assumed return on plan assets	(597)	**(433)**	**(4,085)**
Experience adjustments of actuarial assumptions	1,886	**1,795**	**16,934**
Loss on amendment to defined contribution plan	—	**567**	**5,349**
Net pension expense	¥5,048	**¥5,405**	**$50,990**

In addition to the pension expense above, additional retirement benefit on the early retirement plan is recorded in the amount of ¥1,362 million ($12,849 thousand).

(4) Assumptions

Projected benefit obligation is determined on the basis of employees' evaluation, their length of service and certain other factors. Other significant assumptions used in the calculation of projected benefit obligation and pension expense are listed below.

	2003	**2004**
Discount rate	3.0%	**2.5%**
Assumed rate of return on plan assets	3.0%	**2.5%**
Amortization period for experience adjustments of actuarial assumptions	3 years	**3 years**

(5) Contributory trusteed employee pension plan

Assets of the contributory trusteed employee pension plan established by the pharmaceutical industry amount to ¥35,651 million ($336,330 thousand) at March 31, 2004 based on the proportion of the Company's payments to the fund.

8. Pledged assets

The Company pledged the following assets to secure trade payables in the amount of ¥27,866 million ($262,887 thousand) as well as certain bank loans at March 31, 2004.

	Millions of yen	Thousands of U.S. dollars
Land	**¥6,272**	**$59,170**
Buildings and structures at net book value	**2,730**	**25,755**
Investment securities	**959**	**9,047**
Time deposits	**160**	**1,509**

9. Contingent liabilities

Contingent liabilities of the Company at March 31, 2004 were guarantees for loans from banks of unconsolidated subsidiaries, affiliates and others in the amount of ¥143 million ($1,349 thousand).

10. Shareholders' equity

The Japanese Commercial Code, amended effective on October 1, 2001, provides that an amount equal to at least 10% of appropriations paid in cash be appropriated as the legal reserve and capital surplus until an aggregated amount of the legal reserve and capital surplus equals 25% of common stock.

The legal reserve and capital surplus may be used to reduce a deficit by resolution of the shareholders or may be capitalized by resolution of the Board of Directors.

11. Other income (expenses)

Other income (expenses) – "Other, net" in the accompanying consolidated statements of operations for the two years ended March 31, 2004 comprised the following:

	Millions of yen		Thousands of U.S. dollars
	2003	**2004**	**2004**
Gain on sale of investment securities–net	¥ 26	**¥ 4**	**$ 38**
Loss on disposal of property, plant and equipment – net	(862)	**(677)**	**(6,387)**
Loss on devaluation of securities	(313)	**(300)**	**(2,830)**
Loss on devaluation of golf memberships	(132)	**(37)**	**(349)**
Restructuring costs	(45)	**(1,477)**	**(13,934)**
Additional retirement benefit for employees	(1,079)	**(1,362)**	**(12,849)**
Miscellaneous	1,000	**776**	**7,320**
	¥(1,405)	**¥(3,073)**	**$(28,991)**

12. Income taxes

The Company is subject to a number of income taxes, which, in the aggregate, indicate statutory tax rates in Japan of approximately 42.1% for the years ended March 31, 2003 and 2004.

The reconciliation between the statutory tax rate and the effective tax rate of the Company for financial statement purposes for the years ended March 31, 2003 and 2004 is presented as follows:

	2003	**2004**
Statutory tax rate	42.1%	**42.1%**
Non-deductible expenses for tax purposes	3.5	**2.0**
Minimum inhabitant taxes	1.7	**1.1**
Effect of change in tax rate for deferred taxes	2.2	**—**
Tax benefit for information technology (IT) investment	—	**(4.3)**
Others	1.1	**4.5**
Effective tax rate	50.6%	**45.4%**

Significant components of the deferred tax assets and liabilities of the Company as of March 31, 2003 and 2004 are as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	**2004**	**2004**
Deferred tax assets:			
Excess bad debt expenses	¥ 2,652	**¥ 2,279**	**$ 21,500**
Excess bonuses accrued	2,541	**2,453**	**23,142**
Enterprise taxes	659	**266**	**2,509**
Retirement benefits	5,492	**6,787**	**64,028**
Disallowed provision for officers' retirement benefits	749	**756**	**7,132**
Other	3,691	**3,216**	**30,340**
Total deferred tax assets	15,784	**15,757**	**148,651**
Deferred tax liabilities:			
Excess tax depreciation	(1,128)	**(1,196)**	**(11,283)**
Unrealized gain on certain investment securities	(2,152)	**(3,423)**	**(32,292)**
Other	(699)	**(696)**	**(6,567)**
Total deferred tax liabilities	(3,979)	**(5,315)**	**(50,142)**
Net deferred tax assets	¥11,805	**¥10,442**	**$ 98,509**

13. Non-capitalized financial leases

Finance leases which do not transfer ownership to lessees are not capitalized and are accounted for in the same manner as operating leases. Certain information for such non-capitalized finance leases was as follows:

(1) Future minimum lease payments at March 31, 2004 were ¥5,555 million ($52,406 thousand), including ¥1,722 million ($16,245 thousand) due within one year.

(2) Lease payments for fiscal 2003 and 2004 were ¥2,436 million and ¥2,056 million ($19,396 thousand), respectively.

14. Transactions with principal shareholder

The following are transactions between the Company and a principal shareholder of Kuraya Sanseido Inc. which owns more than 10% interest:

	Millions of yen	Thousands of U.S. dollars
Principal shareholder	Takeda Chemical Industries, Ltd.	
Common stock	¥63,540	$599,434
Principal business	Pharmaceutical product manufacturer	
Percentage of total shares	13.93%	
Description of the Company's transactions:		
Purchase amounts from April 2003 to March 2004	¥189,413	$1,786,915
Research fee income amounts from April 2003 to March 2004	520	4,906
Balance of accounts payable-trade, as of March 31, 2004	45,796	432,038
Balance of accounts receivable-other, as of March 31, 2004	3,452	32,566

15. Segment information

The Company is mainly engaged in the sale of pharmaceutical supplies. Sales of such business segment exceeded 90% of consolidated net sales for the two years ended March 31, 2004.

Information by location and overseas sales was not disclosed because domestic sales of Kuraya Sanseido Inc. and its domestic consolidated subsidiaries exceeded 90% of consolidated net sales for the two years ended March 31, 2004.

16. Subsequent events

(1) On June 29, 2004, shareholders of Kuraya Sanseido Inc. approved the payment of a cash dividend of ¥6.00 ($0.06) per share to shareholders of record at March 31, 2004, for a total payment of ¥864 million ($ 8,150 thousand).

(2) Exchange of Kuraya Sanseido Inc. common stock for Atol Co., Ltd. ("Atol") and Everlth Co., Ltd. ("Everlth") common stock.

On April 1, 2004, Kuraya Sanseido Inc. exchanged its common stock for the common stock of Atol and Everlth in order to enhance the efficiency of business activities and increase corporate value by providing business services through a national network and concentrating corporate resources. Atol and Everlth became wholly owned subsidiaries of Kuraya Sanseido Inc. under the exchange.

As a result, Kuraya Sanseido Inc. common shares issued increased by 35,681,868 shares and capital surplus increased by ¥33,684 million ($317,774 thousand).

The increase in capital surplus was accounted for in accordance with the Japanese Institute of Certified Public Accountants (JICPA) Accounting Committee Research Report No. 6, "Consolidation Procedures in Creation of Parent-Subsidiary Relationships by Means of System of Exchange and Transfer of Stocks," issued in February 2001.

The share exchange ratio was 0.93 shares of Kuraya Sanseido Inc. common stock per share of Atol and Everlth common stock, respectively. Common shares were issued to the shareholders of Atol and Everlth based on this exchange ratio. However, the 193,000 shares of Atol and 140,000 shares of Everlth held by Kuraya Sanseido Inc. were not exchanged.

Financial information of Atol

	Millions of yen	Thousands of U.S. dollars
Common stock:	¥3,966	$37,415
Principal business:	Pharmaceutical product wholesaler	
Financial results for the year ended March 31, 2004:		
Sales	¥176,916	$1,669,019
Operating income	2,245	21,179
Net income	1,263	11,915
Total assets, total liabilities and shareholders' equity at March 31, 2004:		
Total assets	¥95,385	$899,858
Total liabilities	59,440	560,755
Total shareholders' equity	35,945	339,104

Financial information of Everlth

	Millions of yen	Thousands of U.S. dollars
Common stock:	¥1,510	$14,245
Principal business:	Pharmaceutical product wholesaler	
Financial results for the year ended March 31, 2004:		
Sales	¥140,263	$1,323,236
Operating income	1,055	9,953
Net income	1,152	10,868
Total assets, total liabilities and shareholders' equity at March 31, 2004:		
Total assets	¥81,859	$772,255
Total liabilities	47,181	445,104
Total shareholders' equity	34,678	327,151

(3) Exchange of Kuraya Sanseido Inc. common stock for Nakagawa Seikodo Co., Ltd. ("Nakagawa Seikodo") common stock

On May 1, 2004, Kuraya Sanseido Inc. exchanged its common stock for the common stock of Nakagawa Seikodo in order to support business activities under its management strategy. Nakagawa Seikodo became a wholly owned subsidiary of Kuraya Sanseido Inc.

As a result, Kuraya Sanseido Inc. common shares issued and outstanding increased by 1,918,059 shares and capital surplus increased by ¥467million ($4,406 thousand).

The increase in capital surplus was accounted for in accordance with JICPA Accounting Committee Research Report No. 6, "Consolidation Procedures in Creation of Parent-Subsidiary Relationships by Means of System of Exchange and Transfer of Stocks," issued in February 2001.

The share exchange ratio was 3.419 shares of Kuraya Sanseido Inc. common stock per share of Nakagawa Seikodo common stock. Common shares were issued to shareholders of Nakagawa Seikodo based on this exchange ratio.

Financial information of Nakagawa Seikodo

	Millions of yen	Thousands of U.S. dollars
Common stock:	¥281	$2,651
Principal business:	Pharmaceutical product wholesaler	
Financial results for the year ended March 31, 2004:		
Sales	¥27,247	$257,047
Operating income	52	491
Net income	195	1,840
Total assets, total liabilities and shareholders' equity at March 31, 2004:		
Total assets	¥14,007	$132,142
Total liabilities	11,944	112,679
Total shareholders' equity	2,063	19,462

Report of Independent Public Accountants

To the Shareholders and the Board of Directors of Kuraya Sanseido Inc.:

We have audited the accompanying consolidated balance sheets of Kuraya Sanseido Inc. and subsidiaries as of March 31, 2003 and 2004, and the related consolidated statements of operations, shareholders' equity and cash flows for the two years ended March 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Kuraya Sanseido Inc. and subsidiaries as of March 31, 2003 and 2004, and the consolidated results of their operations and their cash flows for the two years ended March 31, 2004, in conformity with accounting principles generally accepted in Japan.

As discussed in Note 16 to the consolidated financial statements, Kuraya Sanseido Inc. exchanged its common stock for common stocks of Atol Co., Ltd. and Everlth Co., Ltd. on April 1, 2004 whereby Atol Co., Ltd. and Everlth Co., Ltd. are wholly owned subsidiaries of Kuraya Sanseido Inc.

Also, in our opinion, the U.S. dollar amounts in the accompanying consolidated financial statements have been translated from Japanese yen on the basis set forth in Note 1.

The Shinyo Audit Corporation

Tokyo, Japan
June 29, 2004

Statement on Accounting Principles and Auditing Standards
See Note 1 to the consolidated financial statements which explains the basis of presentation of the consolidated financial statements of Kuraya Sanseido Inc. and its consolidated subsidiaries under Japanese accounting principles and practices.

SUBSIDIARIES AND AFFILIATED COMPANIES

(As of June 29, 2004)

PHARMACEUTICAL WHOLESALE COMPANIES

SENSHU YAKUHIN CO., LTD.
4-9-5, Oroshi-cho, Akita-shi, Akita 010-8511
Phone: 81-18-885-0131
Fax: 81-18-823-5509
Established: February, 2001
Lines of business: Wholesale of medical-use pharmaceuticals
Homepage: http://www.senshu.co.jp/

USHIODA SANGOKUDO YAKUHIN CO., LTD.
1852-4, Otsuka-cho, Mito-shi, Ibaraki 311-4192
Phone: 81-29-251-5151
Fax: 81-29-251-4425
Established: May, 1949
Lines of business: Wholesale distribution of pharmaceutical products
Homepage: http://www.ushiodasangokudou.jp/

Chiyaku Co., Ltd.
3-2, Tonya-cho, Chuo-ku, Chiba-shi, Chiba 260-0025
Phone: 81-43-248-1001
Fax: 81-43-242-0469
Established: July, 1953
Lines of business: Wholesale distribution of pharmaceutical products
Homepage: http://www.chiyaku.co.jp/

YAMAHIRO KURAYA SANSEIDO Inc.
2, Ryutsudanchi Kita, Yamanokami, Tatomi-cho, Nakakoma-gun, Yamanashi 409-3845
Phone: 81-55-273-8911
Fax: 81-55-273-0079
Established: January, 1950
Lines of business: Sales of pharmaceutical products
Homepage: http://www.yamahiroks.jp/

HEISEI YAKUHIN CO., LTD.
1-1, Motomachi, Gifu-shi, Gifu 500-8185
Phone: 81-58-265-8886
Fax: 81-58-265-8488
Established: January, 1929
Lines of business: Wholesale distribution of pharmaceutical products
Homepage: http://www.heiseiyakuhin.co.jp/

IZUTSU PHARMACEUTICAL CO., LTD.
5, Nioumon-cho, Karasuma Higashi Iru, Nijyodori, Nakagyo-ku, Kyoto 604-0854
Phone: 81-75-211-5151
Fax: 81-75-211-7951
Established: October, 1950
Lines of business: Wholesale distribution of pharmaceutical products
Homepage: http://www.izutsu.co.jp/

EVERLTH Co., Ltd.
Hiroshimahaibiru 21, 3-1 Ginyamachyo, Naka-ku, Hiroshima-shi, Hiroshima 730-0022
Phone: 81-82-544-8301
Fax: 81-82-544-8350
Established: April, 1950
Lines of business: Wholesale distribution of pharmaceutical products
Homepage: http://www.everlth.co.jp/

ATOL Co., Ltd.
2-2-51, Handobashi, Hakata-ku, Fukuoka-shi, Fukuoka 816-8552
Phone: 81-92-451-8771
Fax: 81-92-451-8754
Established: January, 1947
Lines of business: Wholesale of medical-use pharmaceuticals
Homepage: http://www.atol-com.co.jp/

NAKAGAWA SEIKODO CO., LTD.
18-15, Hongo 3-chome, Bunkyo-ku, Tokyo 113-8445
Phone: 81-3-3816-5646
Fax: 81-3-3816-1395
Established: April 1947
Lines of business: Sales of medical equipment and laboratory instruments
Homepage: http://www.e-truth.co.jp/

HOSSP CORPORATION
1-12-27, Nobidome, Niiza-shi, Saitama 352-0011
Phone: 81-48-480-2880
Fax: 81-48-477-6292
Established: April, 1999
Lines of business: Sales of medical equipment, instruments, and examination materials

MEDICAL-RELATED COMPANIES

ORIENTAL PHARMACEUTICAL CO., LTD.
1452-3, Aza Yakushihara Minami, Ohaza Takasen, Tendo-shi, Yamagata 994-0068
Phone: 81-236-55-4335
Fax: 81-236-55-4360
Established: August, 1946
Lines of business: Manufacturing and sales of pharmaceuticals and food additives

KURAYA SHOJI, INC.
4-25-12, Ishihara, Sumida-ku, Tokyo 130-0011
Phone: 81-3-3626-6555
Fax: 81-3-3626-6551
Established: September, 1971
Lines of business: Sales of general-use pharmaceuticals, medical apparatus, health machines and equipment

KURAYA KASEI, INC.
917, Oaza Inaba, Nagano-shi, Nagano 380-0911
Phone: 81-26-221-2005
Fax: 81-26-222-3665
Established: January, 1998
Lines of business: Sales of chemical industrial items and food additives

ELF Co., Ltd.
Sanon Bldg., 5-17-30, Fukushima, Fukushima-ku, Osaka-shi, Osaka 553-0003
Phone: 81-6-6453-5001
Fax: 81-6453-4621
Established: August, 1985
Lines of business: Providing home care services and home helper training programs
Homepage: http://elf-nishikobe.hoops.ne.jp/

M.I.C. (Medical Information College), INC.
Tokimo Yushima Bldg. 4F, 3-26-7, Yushima Bunkyo-ku, Tokyo, 113-0034
Phone: 81-3-3832-6181
Fax: 81-3-3832-6182
Established: August, 1984
Lines of business: Training and supplying medical office workers, providing medical office work services on a contract basis, and consulting on medical management

BUTSURYU 24, INC.
Tokimo Yushima Bldg. 4F, 3-26-7, Yushima Bunkyo-ku, Tokyo 113-0034
Phone: 81-3-5846-4821
Fax: 81-3-3837-1825
Established: June, 1998
Lines of business: Management and operation of distribution center, collection and processing of information relating to distribution, and distribution of freight goods

BIGEO Inc.
1-7-35, Horinouchi, Suginami-ku, Tokyo 166-0013
Phone: 81-3-3318-5661
Fax: 81-3-3318-5680
Established: January, 2001
Lines of business: Cleaning and leasing service of medical uniforms and bedclothes

Kuraya (USA) Corporation
3625, Del Amo Blvd., Suite #150, Torrance, CA 90503, U.S.A.
Phone: 1-310-542-4245
Fax: 1-310-542-4175
Established: July, 1997
Lines of business: Supplying overseas disposable medical goods and sales of medical items
Homepage: http//www.kurayausa.com

HONGOH YAKUHIN, INC.
1-7-35, Horinouchi, Suginami-ku, Tokyo, 166-0013,
Phone: 81-3-5305-3851
Fax: 81-3-3314-1261
Established: July, 1988
Lines of business: Management consultancy of pharmacies and sales of pharmacy computers and equipment
Homepage: http://www.nona.dti.ne.jp/~hongoh/

INVESTOR INFORMATION

(As of March 29, 2004)

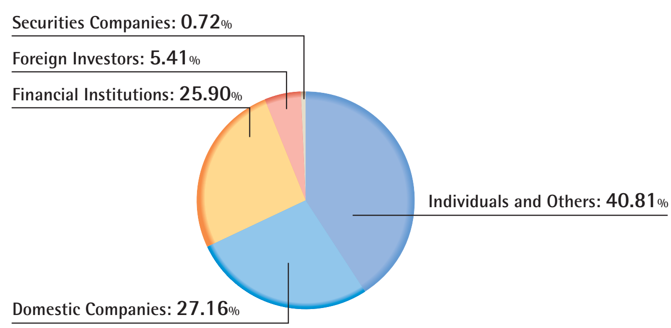
Corporate Name	KURAYA SANSEIDO Inc.
Head Office	7-15, Yaesu 2-chome, Chuo-ku, Tokyo 104-8464, Japan Tel: 81-3-3517-5050 Fax: 81-3-3517-5011 http://www.kurayasanseido.co.jp
Founded	October 1898
Established	May 1923
Number of Employees	7,468 (Consolidated basis) 5,427 (Parent company)
Paid-in Capital	¥15,183 million
Number of Outstanding Shares	147,736,054
Stock Listings	Tokyo
Ticker Code	7459
Trading Unit	100 shares
Transfer Agent for Common Stock	Sumitomo Trust & Banking Co., Ltd.
General Meeting of Shareholders	The Ordinary General Annual Meeting of Shareholders is held annually in June.
Further Information	Investor Relations Department Tel : 81-3-3517-5171

Principal Shareholders

	Number of Shares Held (thousand)	Percentage of Total Shares
Takeda Chemical Industries, Ltd.	18,816	12.74%
Japan Trustee Services Bank, Ltd.	11,754	7.96
Employees Shareholders' Association	11,488	7.78
The Master Trust Bank of Japan, Ltd.	5,856	3.96
Trust and Custody Services Bank, Ltd.	5,259	3.56
Sadatake Kumakura	3,421	2.32
Yamanouchi Pharmaceutical Co., Ltd.	2,861	1.94
Osamu Takumiya	2,371	1.61
Shizue Kumakura	1,924	1.30
Fujisawa Pharmaceutical Co., Ltd.	1,869	1.27

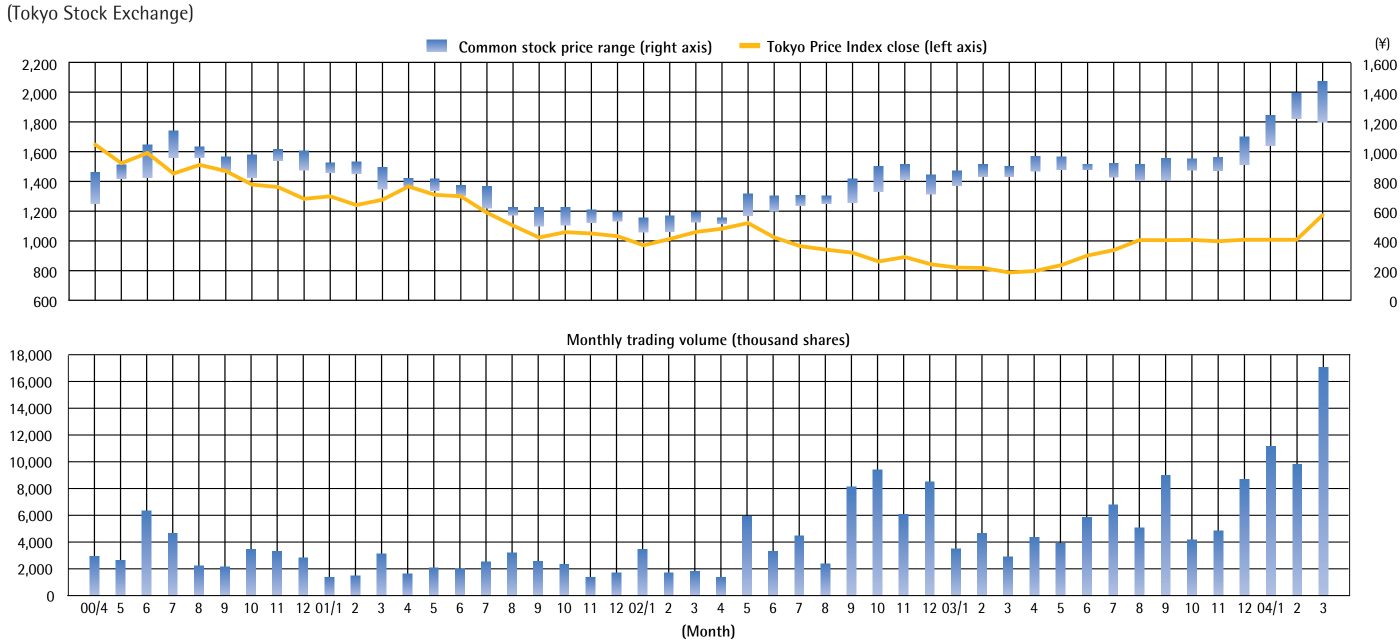
Notes:
1. Takeda Chemical Industries, Ltd. changed its corporate name to Takeda Pharmaceutical Company Limited on June 29, 2004.
2. Shares held by Japan Trustee Services Bank, Ltd., The Master Trust Bank of Japan Ltd. and Trust and Custody Services Bank, Ltd. are held by trust accounts of the respective banks.
3. "Principal Shareholders" and "Distribution of Shareholders" do not include 3,721 thousand shares of treasury stock held by the Company.

Distribution of Shareholders



Monthly Stock Price Range & Trading Volume

(Tokyo Stock Exchange)



Kuraya Sanseido

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