MANAGEMENT'S DISCUSSION AND ANALYSIS

Six-Year Summary

Mediceo Paltac Holdings Co., Ltd. and its consolidated subsidiaries
Years ended March 31

	Millions of yen						Thousands of U.S. dollars (Note 1)
	2002	2003	2004	2005	2006	**2007**	**2007**
For the Year:							
Net sales	¥1,222,222	¥1,274,503	¥1,283,926	¥1,665,816	¥1,921,714	**¥2,166,763**	**$18,362,398**
Gross profit	106,644	114,923	116,805	137,806	161,603	**188,235**	**1,595,212**
Selling, general and administrative expenses	100,863	104,763	101,450	126,819	140,995	**160,459**	**1,359,822**
Operating income	5,781	10,160	15,355	10,987	20,608	**27,776**	**235,390**
Net income	2,951	5,016	7,879	8,730	20,843	**19,106**	**161,915**
Depreciation and amortization	4,866	5,204	5,709	7,625	9,126	**9,663**	**81,890**
Capital expenditures (cash base)	5,663	6,206	4,974	7,812	9,064	**12,236**	**103,695**
At Year-End:							
Total assets	¥ 644,248	¥ 638,589	¥ 626,626	¥ 848,416	¥ 993,491	**¥1,032,931**	**$ 8,753,653**
Interest-bearing debt	41,177	33,730	23,275	15,660	38,400	**42,058**	**356,424**
Total net assets	110,650	112,261	128,988	168,104	242,413	**261,112**	**2,212,814**
Per Share (Yen and U.S. Dollars):							
Net income (Note 2)	¥ 21.67	¥ 36.48	¥ 55.19	¥ 45.90	¥ 97.64	**¥ 82.86**	**$ 0.70**
Diluted net income	18.92	31.50	48.65	43.52	94.22	**82.29**	**0.70**
Total net assets (Note 3)	823.75	828.14	893.84	904.59	1,051.97	**1,128.39**	**9.56**
Cash dividends	12.00	12.00	12.00	12.00	15.00	**15.00**	**0.13**
Ratios:							
Return on assets (Note 4)	0.9%	1.6%	2.4%	1.4%	2.2%	**2.7%**	
Return on equity (Note 5)	2.5	4.5	6.5	5.9	10.2	**7.6**	
Number of employees	7,780	7,741	7,468	9,496	11,078	**10,664**	

Notes: 1. The U.S. dollar amounts in this report represent translations of Japanese yen, for convenience only, at the rate of ¥118.00 to U.S. $1.00, the approximate exchange rate on March 31, 2007.
2. Net income per share = (Net income – Officers' bonuses) / (Average shares outstanding during the year - Average treasury stock during the year)
3. Total net assets per share = (Total net assets - Officers' bonuses) / (Shares outstanding at end of year - Treasury stock)
4. Return on assets = (Operating income + interest and dividend income) / Total assets at end of period
5. Return on equity = Net income / Average total net assets

Scope of Consolidation

The Mediceo Paltac Group (the "Group") consists of 37 subsidiaries and 8 affiliates, with Mediceo Paltac Holdings Co., Ltd. (the "Company") as the core. Eleven Group subsidiaries are consolidated, unchanged from the previous fiscal year. Group companies are primarily engaged in wholesale distribution of pharmaceuticals, cosmetics, daily necessities and other products, and providing services. On April 1, 2006, USHIODA SANGOKUDO YAKUHIN CO., LTD. changed its name to USHIODA KURAYA SANSEIDO Inc., and IZUTSU PHARMACEUTICAL CO., LTD. changed its name to IZUTSU KURAYA SANSEIDO Inc.

Overview of Results

During the year ended March 31, 2007, the Japanese economy recovered. Despite weakness in production in certain sectors, consumer spending trended upward, capital investment increased, and employment conditions improved.

The Group launched the Business Innovation Committee (BIC) on April 1, 2006 with the aim of structuring a new business model, primarily for the prescription pharmaceutical business, in order to realize stable long-term growth.

In addition, the Company acquired 34.0 percent of the common stock of Nihon Hospital Service Co., Ltd., which was a wholly owned subsidiary of Mitsubishi Corporation. By combining the functions and know-how of the Group and Nihon Hospital Service in supply processing and distribution (SPD), the Company intends to develop a sophisticated, high-value-added SPD business that handles a complete range of products from pharmaceuticals to medical materials.

In addition, to promote more efficient, enhanced sales activities, on April 1, 2006 KURAYA SANSEIDO Inc., a wholly owned subsidiary of the Company, transferred its prescription pharmaceutical wholesale business in Toyama, Ishikawa and Fukui prefectures to IZUTSU KURAYA SANSEIDO Inc. (formerly IZUTSU PHARMACEUTICAL CO., LTD.), a wholly owned subsidiary of the Company, and a portion of its medical equipment business in Osaka, Hyogo and Nara prefectures to MEDICEO MEDICAL CO., LTD., a wholly owned subsidiary of the Company.

On October 1, 2006, the OTC pharmaceutical wholesale businesses of wholly owned subsidiaries KURAYA SANSEIDO Inc. and EVERLTH Co., Ltd. were consolidated at wholly owned subsidiary PALTAC CORPORATION. By doing so, the Group aims to further strengthen and enhance customer service and has worked to reduce costs by making its business foundation stronger and more efficient.

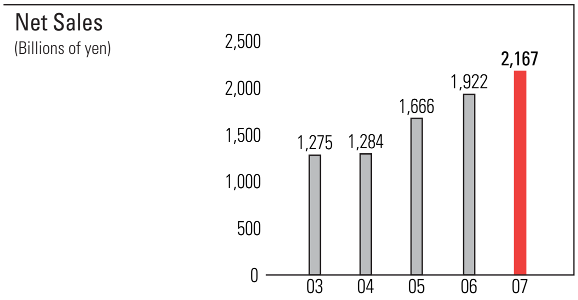
The Group offered early retirement to employees of prescription pharmaceutical wholesale business companies (excluding MEDICEO MEDICAL CO., LTD.). As of September 30, 2006, 305 employees retired under this program.

As a result, consolidated net sales for the year ended March 31, 2007 increased 12.8 percent compared with the previous fiscal year to ¥2,166,763 million, operating income increased 34.8 percent to ¥27,776 million, and net income decreased 8.3 percent to ¥19,106 million.

Sales and Income

Net Sales

Consolidated net sales increased 12.8 percent, or ¥245,049 million, year-on-year to ¥2,166,763 million. The increase in net sales was significantly higher than the overall growth of the market because of the full-year contribution of PALTAC CORPORATION to consolidated results.



Sales by Business Segment

Change in Business Classification

The Group changed its business segment classifications in connection with the management integration of the healthcare business into PALTAC CORPORATION in stages from April 1, 2006. As of the fiscal year ended March 31, 2007, the former Pharmaceutical Wholesale Business, Cosmetics and Daily Necessities Wholesale Business and Medical-Related Business have been changed to the Prescription Pharmaceutical Wholesale Business, the Cosmetics, Daily Necessities and OTC Pharmaceutical Wholesale Business, and Related Business, respectively. Prior-year data have been restated to allow year-on-year comparison.

The following segment information excludes intersegment sales and transfers.

Prescription Pharmaceutical Wholesale Business

The prescription pharmaceutical market was weak due to the effects of an average 6.7 percent reduction in National Health Insurance (NHI) drug price standards on April 1, 2006. The Group adjusted its selling prices to reflect the reduction, and conducted persistent negotiations with an emphasis on securing reasonable profits. Despite delays in reaching pricing agreements with some medical institutions and dispensing pharmacies, the Group increased the contract rate by March 31, 2007 and continued to work to maintain selling prices. In addition, the Group conducted detailed community-based sales activities, including providing a stable supply of products for early prevalence of pollen allergy and for an outbreak of influenza, which was concentrated near the end of the period. As a result, sales of the Prescription Pharmaceutical Wholesale Business increased 0.2 percent compared with the previous fiscal year to ¥1,646,047 million. Segment operating income increased 37.4 percent year-on-year to ¥23,281 million.

Prescription Pharmaceutical Wholesale Business

(Millions of yen)

Years ended March 31	2006	2007	Change (%)
Sales	¥1,642,108	¥1,646,047	0.2%
Operating income	16,942	23,281	37.4
Assets	837,005	835,236	(0.2)
Depreciation	7,224	6,923	(4.2)
Capital expenditures	7,096	5,172	(27.1)

Cosmetics, Daily Necessities and OTC Pharmaceutical Wholesale Business

Sales of cosmetics and daily necessities continued to increase steadily, primarily at drugstores. Sales of OTC pharmaceuticals were lackluster due to weak demand resulting from slumping sales of seasonal products and other items.

In order to provide high-quality, efficient distribution functions, PALTAC CORPORATION, which handles this business, completed construction of a large-scale, high-tech distribution center in Asaminami-ku, Hiroshima (RDC Chugoku) in December 2006.

On December 20, 2006, the Company and PALTAC CORPORATION agreed with Kobayashi Pharmaceutical Co., Ltd. and its consolidated subsidiary KOBASHOU CO., LTD. to begin discussions on a management integration between PALTAC CORPORATION and KOBASHOU CO., LTD.

As a result, sales of the Cosmetics, Daily Necessities and OTC Pharmaceutical Wholesale Business increased 91.5 percent compared with the previous fiscal year to ¥514,753 million. Segment operating income increased 295.1 percent year-on-year to ¥3,939 million.

Cosmetics, Daily Necessities and OTC Pharmaceutical Wholesale Business

(Millions of yen)

Years ended March 31	2006	2007	Change (%)
Sales	¥268,806	¥514,753	91.5%
Operating income	997	3,939	295.1
Assets	165,815	195,400	17.8
Depreciation	1,819	2,740	50.6
Capital expenditures	3,289	8,711	164.9

Related Business

Sales of industrial chemicals to the semiconductor and automobile industries were steady. On the other hand, food additive-related sales were weak due to unseasonable weather and other factors. As a result, sales of the Related Business decreased 44.8 percent compared with the previous fiscal year to ¥5,963 million. Segment operating income decreased 75.2 percent year-on-year to ¥64 million

Related Business

(Millions of yen)

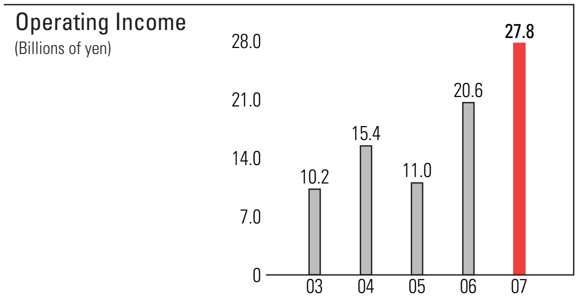
Years ended March 31	2006	2007	Change (%)
Sales	¥10,798	¥5,963	(44.8)%
Operating income	258	64	(75.2)
Assets	2,324	2,800	20.5
Depreciation	82	0	(100.0)
Capital expenditures	24	2	(91.7)

Operating Income

Gross profit increased 16.5 percent, or ¥26,632 million, year-on-year to ¥188,235 million, and the gross profit margin improved to 8.7 percent from 8.4 percent for the previous fiscal year. The Group compensated for the impact of the reduction of NHI drug price standards on April 1, 2006 by adjusting selling prices in tandem with the reduction and by conducting persistent negotiations with an emphasis on securing reasonable profits. The full-year contribution of PALTAC CORPORATION also supported consolidated results.

Selling, general and administrative (SG&A) expenses increased 13.8 percent year-on-year, or ¥19,464 million, to ¥160,459 million, and the ratio of SG&A expenses to net sales increased to 7.4 percent from 7.3 percent for the previous fiscal year. The Group worked to raise efficiency and reduce costs through the integration in stages of the Group's healthcare business within PALTAC CORPORATION from April 1, 2006. At the same time, SG&A expenses reflected the addition of the full-year expenses of PALTAC CORPORATION to consolidated results.

As a result, operating income increased 34.8 percent, or ¥7,168 million, year-on-year to ¥27,776 million, and the operating margin increased to 1.3 percent from 1.1 percent for the previous fiscal year.



Other Income (Expenses)

Total other income (expenses) amounted to net other income of ¥6,564 million, a decrease of 30.9 percent compared to net other income of ¥9,501 million for the previous fiscal year. Amortization of negative goodwill was ¥6,068 million, which offset additional retirement benefits for employees totaling ¥5,750 million incurred as a result of the voluntary early retirement program offered to employees of prescription pharmaceutical wholesale business companies discussed above.

As a result, income before income taxes and minority interests increased 14.1 percent, or ¥4,231 million, year-on-year to ¥34,340 million.

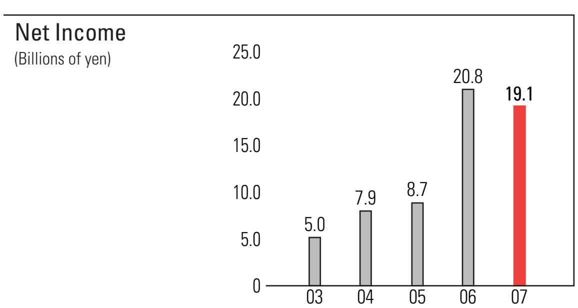
Costs, Expenses and Income as a Percentage of Net Sales

Years ended March 31	2005	2006	2007	Increase (decrease) 2007/2006
Cost of sales	91.7%	91.6%	**91.3%**	**12.8**
Gross profit	8.3	8.4	**8.7**	**12.4**
SG&A expenses	7.6	7.3	**7.4**	**16.4**
Operating income	0.7	1.1	**1.3**	**34.8**
Income before income taxes and minority interests	1.2	1.6	**1.6**	**14.0**
Net income	0.5	1.1	**0.9**	**(8.3)**

Net Income

Income taxes increased 64.4 percent, or ¥5,968 million, year-on-year to ¥15,234 million. Consequently, net income decreased 8.3 percent, or ¥1,737 million, year-on-year to ¥19,106 million.

Net income per share decreased to ¥82.86 from ¥97.64 for the previous fiscal year. Fully diluted net income per share decreased to ¥82.29 from ¥94.22 for the previous fiscal year.



Dividends

The Company considers returns to shareholders to be one of its highest management priorities. The Company's basic policy is to provide stable dividends while giving consideration to increasing internal reserves needed to strengthen its financial position and aggressively develop its business.

The Company also pays dividends from retained earnings twice yearly, with the distribution of retained earnings subject to a resolution of the Board of Directors.

Cash dividends applicable to the fiscal year ended March 31, 2007 totaled ¥15.00 per share, and consisted of an interim dividend of ¥7.50 and a year-end dividend of ¥7.50. As a result, the payout ratio was 18.1 percent.

Financial Strategy

The financial strategy of the Group centers on creating sufficient liquidity and capital for operating needs and a sound balance sheet. Capital investment in property, plant and equipment is carried out according to clearly defined plans.

Cash Flow

Net Cash Provided by Operating Activities

Net cash provided by operating activities decreased ¥21,959 million compared with the previous fiscal year to ¥19,837 million. The main components of cash from operating activities were income before income taxes and minority interests of ¥34,340 million (a year-on-year increase of 14.1 percent), depreciation and amortization of ¥9,663 million, loss on impairment of fixed assets of ¥2,768 million, increase in notes and accounts payable of ¥8,974 million, amortization of negative goodwill of ¥3,451 million, and increase in inventories of ¥8,771 million. Total decrease in allowances was ¥7,756 million, and cash paid for income taxes was ¥13,431 million.

Cash Flow Highlights

(Millions of yen)

Years ended March 31	2005	2006	2007	Increase (decrease) 2007/2006
Net cash provided by operating activities	¥26,302	¥41,796	**¥19,837**	**¥(21,959)**
Net cash provided by (used in) investing activities	31,279	4,366	**(20,138)**	**(24,504)**
Net cash used in financing activities	(8,516)	(22,375)	**(1,691)**	**20,684**
Cash and cash equivalents at end of year	119,121	142,908	**142,439**	**(469)**

Net Cash Used in Investing Activities

Net cash used in investing activities totaled ¥20,138 million. In the previous fiscal year, investing activities provided net cash totaling ¥4,366 million. While proceeds from sale of property and equipment were ¥3,194 million, payments for purchase of property and equipment including RDC Chugoku totaled ¥12,236 million. Payments for purchase of investment securities were ¥4,151 million and payment for acquisition of investment in subsidiaries was ¥3,976 million. Proceeds from acquisition of investment in subsidiaries due to change in the scope of consolidation totaling ¥10,628 million in the previous fiscal year did not recur.

Net Cash Used in Financing Activities

Net cash used in financing activities was ¥1,691 million, compared to ¥22,375 million in the previous fiscal year. The main components were a ¥3,615 million net increase in short-term bank loans, proceeds from long-term debt of ¥5,000 million, repayment of long-term debt totaling ¥6,370 million, and ¥3,798 million in payments for cash dividends to shareholders. Purchase of treasury stock totaled ¥138 million, compared to ¥16,873 million in the previous fiscal year.

In addition to the above, increase in cash and cash equivalents due to change in the scope of consolidation totaled ¥1,523 million. Consequently, cash and cash equivalents at the end of the period decreased ¥469 million (0.3 percent) from the end of the previous fiscal year to ¥142,439 million.

Assets and Liabilities

Total assets at March 31, 2007 increased 4.0 percent from a year earlier to ¥1,032,931 million.

Total current assets increased 2.8 percent from a year earlier to ¥795,808 million. Factors included a ¥3,406 million increase in cash, a ¥9,543 million increase in inventories and a ¥3,996 million increase in accounts receivable, other.

Net property and equipment as of March 31, 2007 increased 0.2 percent from a year earlier to ¥151,520 million. Buildings and structures increased ¥1,940 million from a year earlier, while land decreased ¥1,858 million from a year earlier.

Total intangible assets increased 119.8 percent from a year earlier to ¥13,494 million due to goodwill totaling ¥8,567 million.

Investments and other non-current assets increased 16.3 percent from a year earlier to ¥72,109 million. Factors included an increase of ¥9,001 million from a year earlier in investment securities.

Total current liabilities increased 2.1 percent from a year earlier to ¥716,061 million. This mainly consisted of a ¥15,044 million increase in notes and accounts payable and a ¥5,415 million increase in short-term bank loans.

Working capital increased 9.5 percent compared to the end of the previous fiscal year to ¥79,747 million. The current ratio was 1.11 times, compared to 1.10 times a year earlier.

Total long-term liabilities increased 11.9 percent from a year earlier to ¥55,758 million. While convertible bonds decreased ¥527 million and long-term debt decreased ¥1,168 million, deferred income taxes increased ¥6,020 million and negative goodwill totaled ¥13,978, up from consolidated adjustment account, which formerly presented goodwill, totaling ¥11,749 million a year earlier. Total interest-bearing debt as of March 31, 2007 increased 9.5 percent from a year earlier to ¥42,058 million.

Net assets as of March 31, 2007 increased 7.7 percent from a year earlier to ¥261,112 million. Factors included an increase of ¥13,813 million in retained earnings and an increase of ¥1,781 million in unrealized gains on securities. The net worth ratio increased to 25.3 percent from 24.4 percent a year earlier. Return on equity decreased to 7.6 percent from 10.2 percent for the previous fiscal year.

Capital Expenditures

Capital expenditures in the year ended March 31, 2007 totaled ¥12,236 million on a cash basis. The purpose of the investments was to further strengthen and enhance the efficiency of distribution functions, primarily in the Prescription Pharmaceutical Wholesale Business and the Cosmetics, Daily Necessities and OTC Pharmaceutical Wholesale Business. Software investment was ¥1,423 million. The Company funded capital expenditures using internal capital resources and external borrowings.

Capital expenditures by business segment are as follows. In the Prescription Pharmaceutical Wholesale Business, the Company made investments of ¥3,598 million in construction of the Kuraya Sanseido Chiba Building and other projects. In addition, the Company invested ¥1,385 million in software to integrate core systems for sales, distribution and other operations.

In the Cosmetics, Daily Necessities and OTC Pharmaceutical Wholesale Business, the Company invested ¥8,634 million in projects including the construction of PALTAC CORPORATION's RDC Chugoku, a distribution center in Hiroshima.

In the Related Business, the Company invested ¥2 million.

Outlook for the Fiscal Year Ending March 2008

The Group's Business Innovation Committee is vigorously promoting innovation in the core areas of competitive strategy, value strategy and information technology (IT) strategy with the aim of structuring a new customer-oriented business model. Other initiatives to deploy collective Group strengths in business development include aggressively continuing to reduce costs and capturing the synergies of the integration of PALTAC CORPORATION. Moreover, during the year ending March 2008 the Group will promote new businesses that respond to the needs of healthcare institutions and social change based on the comprehensive alliance in the medical business with Mitsubishi Corporation.

In the Prescription Pharmaceutical Wholesale Business, the Group will continue to negotiate selling prices with the aim of securing reasonable profits. We will anticipate the changes in the operating environment of core customer segments including healthcare institutions and dispensing pharmacies and work to provide added value that addresses these changes.

In the Cosmetics, Daily Necessities and OTC Pharmaceutical Wholesale Business, the Group has integrated OTC pharmaceutical operations with the cosmetics and daily necessities operations of PALTAC CORPORATION in working to further raise customer satisfaction by establishing the foundation for enhancing the Group's functions and services as a wholesaler in these areas.

As a result, for the year ending March 31, 2008, the Company projects consolidated net sales of ¥2,175.0 billion (a year-on-year increase of 3.8 percent), consolidated operating income of ¥30.7 billion (a year-on-year increase of 10.5 percent) and consolidated net income of ¥24.3 billion (a year-on-year increase of 27.2 percent).

Risk Information

Among the business, management and other issues presented in this report, risks that may exert a significant influence on investor decisions include, but are not limited to, the following. Forward-looking statements in the following text are based on the judgment of the Group as of March 31, 2007.

Specific Regulations and Other Legal Issues

The Group handles various types of pharmaceuticals and related products. Therefore, it conduct sales activities after receiving the necessary authorizations, registrations, designations and licenses from the local governments where business sites are located, pursuant to the Pharmaceutical Affairs Law and other laws.

Medical System Reform

In Japan, fiscal reconstruction is an urgent issue, and includes the implementation of medical system reforms. The content of these reforms may affect the business results of the Prescription Pharmaceutical Wholesale Business and the Related Business.

Drug Price Standards

The prescription pharmaceuticals handled by the Group's Prescription Pharmaceutical Wholesale Business are subject to National Health Insurance (NHI) drug price standards. The NHI drug price standards stipulate the range of pharmaceuticals that can be used under health insurance coverage and their billing prices. Accordingly, these standards function as an upper limit on selling prices. Revisions of NHI drug prices during the last five years were as follows.

Implementation Date	Average Rate of Decrease
April 1, 2002	6.3%
April 1, 2004	4.2%
April 1, 2006	6.7%

Investment Cost and Unit Selling Prices

The Group is expanding its competitive scale and scope by merging with other wholesalers. Increased investment costs associated with improvement and expansion of distribution and information systems to handle these expansions or a larger-than-expected decrease in unit selling prices may affect business results.

Sales Discontinuations, Product Recalls and Other Issues

Situations including the discontinuation of sales or recall of certain products due to defects, unforeseen side effects or tampering with certain products sold may affect business results.

System Problems

The Group's business operations rely heavily on computer network systems. Network interruptions due to natural disasters, accidents, computer viruses or other incidents may result in significant obstacles to product sales and distribution.

Default Risk

The Group generates receivables through its ongoing transactions with customers. Default due to issues including bankruptcy or civil rehabilitation among customers could affect business results.

Product Inventory Risk

Issues including bankruptcy or civil rehabilitation among suppliers could cause Group product inventory to decline in value or become unsaleable, which could affect business results.

Litigation Risk

The Group's operations may be subject to litigation seeking monetary damages.