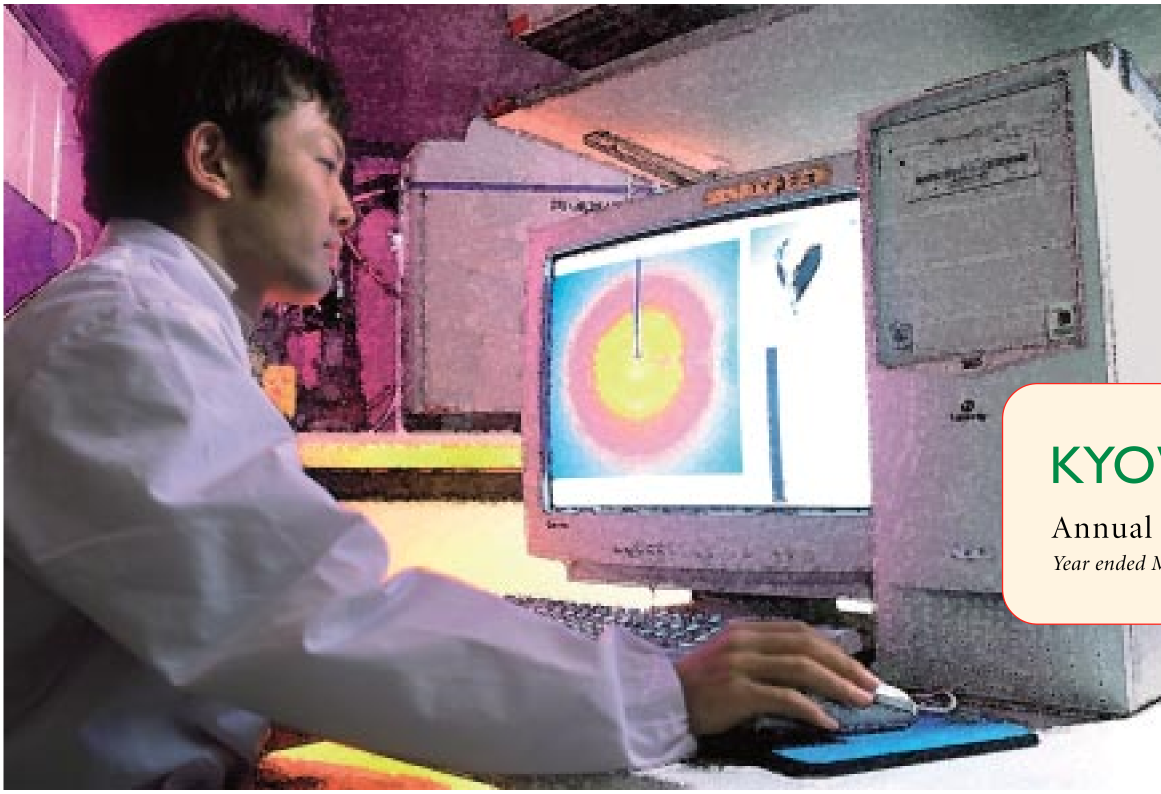
KYOWA HAKKO KOGYO CO., LTD. Annual Report 2004

KYOWA



KYOWA HAKKO

Annual Report 2004

Year ended March 31, 2004

BIOTECHNOLOGY:

BUILDING ON OUR STRENGTHS

Kyowa Hakko Kogyo Co., Ltd., is a research-based company with special strengths in biotechnology. The Company is dedicated to the creation of new value in the life sciences, especially pharmaceuticals and bio-chemicals, and strives to contribute to the health and well-being of people around the world.

Following its founding, Kyowa Hakko contributed to the eradication of tuberculosis in Japan by producing streptomycin. The Company subsequently developed anticancer agent Mitomycin C, which is now a leading chemotherapy agent in markets around the world. In addition to anticancer agents, Kyowa Hakko is actively engaged in the R&D, production, and sale of pharmaceuticals that address a wide range of other medical needs, including hypertension and allergies. Kyowa Hakko's Pharmaceuticals operations are now one of the Company's core business fields.

Kyowa Hakko is focusing its R&D resources on treatments for allergies and cancer as well as antibody and other key technologies. At the same time, the Company is bolstering drug development activities in Europe and the United States and promoting its operations in overseas markets.

The Company has worked to apply its biotechnology capabilities to the mass production of such products as amino acids. Kyowa Hakko also applies these capabilities to its Bio-Chemicals and Food operations. Along with Pharmaceuticals, Bio-Chemicals operations are the Company's other core business field, and Kyowa Hakko is a global leader in the supply of fermented bulk products, such as amino acids and nucleic acids.

In Food operations, the Company uses its fermentation and other original technologies to differentiate itself from competitors in the development of food products, especially natural seasonings.

The Company's Chemicals operations grew out of its original acetone and butyl alcohol fermentation operations. In addition to basic chemicals, such as plasticizers and solvents, Kyowa Hakko is working to expand its lineup of specialty chemicals that contribute to environmental conservation.

Note to Performance Forecasts

Forecasts contained in the *Annual Report 2004* represent judgments based on information available as of June 29, 2004. It should be noted that there is a possibility that actual results could differ significantly due to such factors as exchange rate fluctuations.

C O N T E N T S

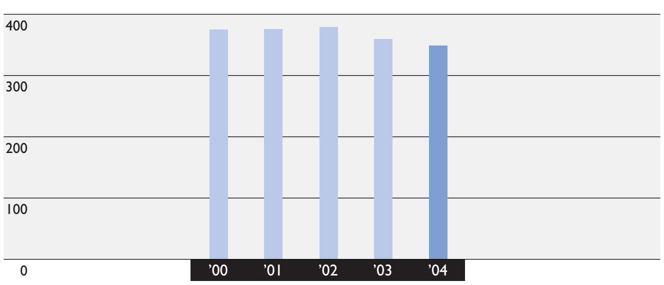
FINANCIAL HIGHLIGHTS

KYOWA HAKKO KOGYO CO., LTD. and Its Consolidated Subsidiaries
For the years ended March 31, 2004, 2003 and 2002

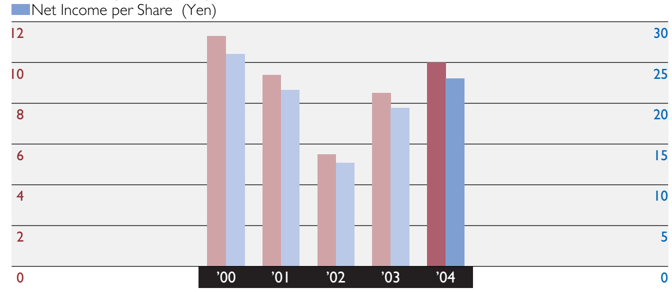
	Millions of Yen			Thousands of U.S. Dollars (Note 1)
	2004	2003	2002	**2004**
For the Year:				
Net sales	**¥348,838**	¥359,285	¥378,668	**$3,300,577**
Operating income	**26,836**	16,089	20,357	**253,912**
Net income	**10,017**	8,485	5,535	**94,777**
Capital expenditures	**9,041**	11,791	11,454	**85,543**
Depreciation and amortization	**11,358**	14,768	17,819	**107,465**
R&D expenses	**29,206**	31,438	29,294	**276,336**
At Year-End:				
Total assets	**361,096**	368,772	430,113	**3,416,558**
Interest-bearing debt	**13,358**	51,969	74,354	**126,388**
Total shareholders' equity	**225,042**	219,047	211,652	**2,129,265**
	Yen			U.S. Dollars (Note 1)
Per Share Data:				
Net income—basic (Note 2)	**¥ 23.0**	¥19.4	¥ 12.7	**$0.218**
Total shareholders' equity	**522.6**	505.4	487.5	**4.945**
Cash dividends	**7.5**	7.5	7.5	**0.071**
	%			
Ratios:				
Return on assets	**2.74**	2.12	1.28	
Return on equity	**4.51**	3.94	2.72	

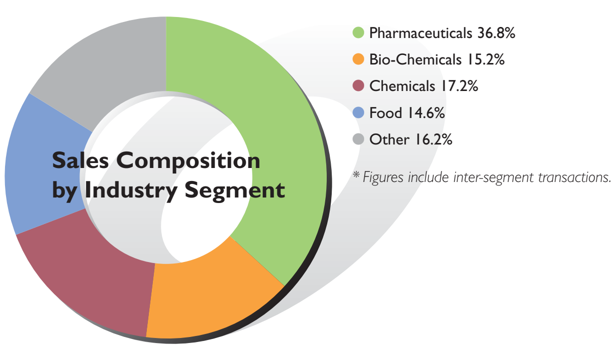
Notes: 1. U.S. dollar amounts are translated from Japanese yen, for convenience only, at the rate of ¥105.69=US$1, the approximate exchange rate at March 31, 2004.
2. Net income per share of common stock is based upon the weighted average number of shares of common stock outstanding during each year, appropriately adjusted for subsequent free distributions of common stock.

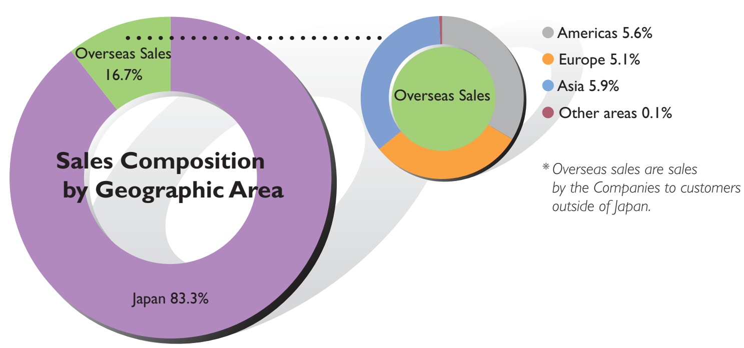
Net Sales
(Billions of Yen)



Net Income / Net Income per Share
Net Income (Billions of Yen)
Net Income per Share (Yen)





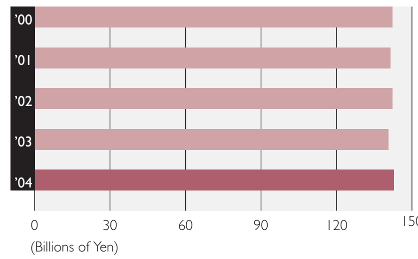


AT A GLANCE

Segment | **Profile** | **Segment Sales** (Including inter-segment transactions)

Pharmaceuticals

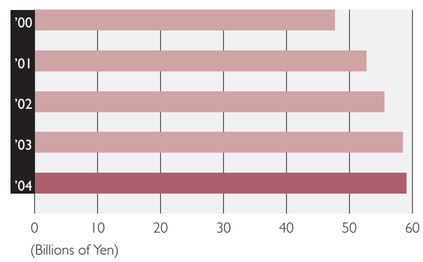
The Pharmaceuticals Segment conducts R&D, production, and sales of ethical pharmaceuticals, principally in the fields of cancer, allergies, and hypertension, and of diagnostic reagents. In ethical pharmaceuticals, targeting growth in overseas markets, in Europe and North America we are moving ahead with the clinical development of new drugs and biopharmaceuticals based on our original strong-acting antibody technology.



Fiscal 2004
Net sales: ¥142.9 billion (36.8%)*
Operating income: ¥11.9 billion (44.0%)
** Figures in parentheses indicate percent of consolidated total*

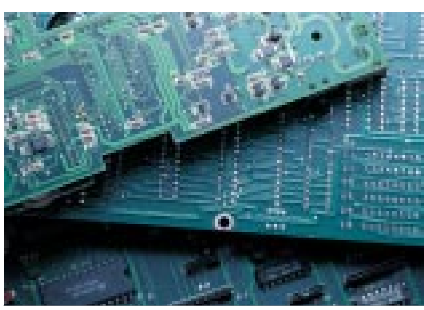
Bio-Chemicals

In Japan and overseas, the Bio-Chemicals Segment produces and markets fermented bulk products, such as amino acids, nucleic acids, and related compounds. These products are used as raw materials for pharmaceuticals, health foods and dietary supplements, cosmetics, and pharmaceutical intermediates. The Company decided to withdraw from feed-grade amino acid operations, such as feed-grade lysine. The Bio-Chemicals Segment also supplies agrochemicals and animal health products to the livestock and fisheries industries.

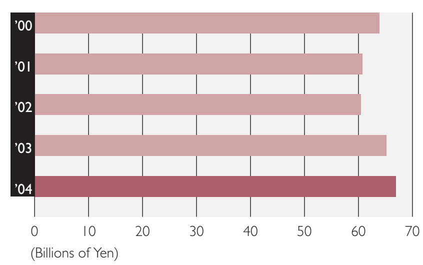


Fiscal 2004
Net sales: ¥59.0 billion (15.2%)*
Operating income: ¥8.5 billion (31.4%)
** Figures in parentheses indicate percent of consolidated total*

Chemicals



The Chemicals Segment produces and markets basic chemicals, which include solvents used in dyes and inks, plasticizers used as additives in PVC products, and raw materials for plasticizers; and specialty chemicals, which include environmentally friendly products and products used in advanced technologies.

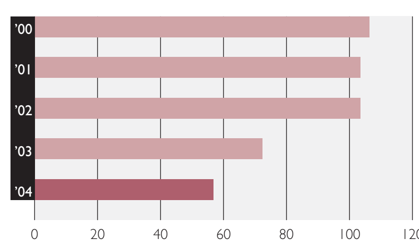


Fiscal 2004
Net sales: ¥66.9 billion (17.2%)*
Operating income: ¥2.9 billion (10.7%)
** Figures in parentheses indicate percent of consolidated total*

Food*

The Food Segment develops, produces, and markets seasonings, principally natural seasonings made from meat, vegetables, and fish; and bakery products and ingredients, such as yeast and bread improvers.

** Accompanying the September 2002 transfer of alcoholic beverage operations, the name of the segment was changed as of April 2004.*



Fiscal 2004
Net sales: ¥56.7 billion (14.6%)*
Operating income: ¥2.0 billion (7.4%)
** Figures in parentheses indicate percent of consolidated total*

Topics	Main Products
• Subsidiary Kyowa Medex Co., Ltd., began sales of highly sensitive brain natriuretic peptide (BNP) diagnostic reagents for use in diagnosing heart disease (April 2003). • Sales of antiallergic agent Allelock® began in South Korea (August 2003). • A joint promotional campaign began with Kyorin Pharmaceutical Co., Ltd., for antiallergic agent Allelock® (October 2003). • Adenosine A1 receptor antagonist KW-3902 licensed to NovaCardia, Inc., of the United States (October 2003). • Clinical trials for anti-Parkinson's disease agent KW-6002, which had been stopped temporarily, restarted (April 2004). • GRAPES, a global document management system that is compatible with NDA formats in Japan, the United States, and Europe, built (May 2004). • U.S. biopharmaceutical business subsidiary BioWa, Inc., licensed Potelligent™ strong-acting monoclonal antibody technology to four companies, including Medarex, Inc., and Biogen Idec Inc., of the United States (as of June 2004).	**Ethical Drugs** • Coniel® (Hypertension and angina pectoris) • Celtect® (Antiallergic agent) • Allelock® (Antiallergic agent) • Depakene® (Antiepileptic agent) • 5-FU (Anticancer agent) • Durotep® Patch (Transdermal analgesic agent) **Diagnostic Reagents** • Determiner® series (clinical chemistry diagnostic reagents)
• Domestically, demand expanded, especially for beverages containing amino acids, and sales of amino acids in fiscal 2004 increased. • Sold feed-grade amino acid production subsidiary Fermex, of Mexico (December 2003), and agreed to sell feed-grade amino acid production subsidiary Agroferm, of Hungary (May 2004). • Agreed to increase investment in joint venture Shanghai Guan Sheng Yuan Kyowa Amino Acid Co., Ltd., to make it a subsidiary, and to raise its production capacity through the construction of a new plant (April 2004).	**Fine Chemicals** • Amino acids, nucleic acids, related compounds **Agrochemicals** • Plant growth regulators **Animal Health Products**
• Sales of specialty chemicals in fiscal 2004 surpassed ¥10.0 billion for the first time. • Succeeded in first commercial production of a new polyol: TOE-2000H (August 2003). • Japan Ethyl Acetate Co., Ltd., an ethyl acetate joint venture with Showa Denko K.K., began production (April 2004). • Kyowa Yuka Co., Ltd., a production subsidiary of Kyowa Hakko, took over Kyowa Hakko's Chemicals operations and made a new start as Kyowa Hakko Chemical Co., Ltd. (April 2004).	**Solvents** • Butyl alcohol, ethyl acetate, butyl acetate **Raw Materials for Plasticizers** • Di-2-ethylhexyl alcohol, Oxocol® 900 **Environmentally Friendly Products** • Polyvinyl ether, 2-ethyl hexanoic acid, isononanoic acid (refrigeration lubricant raw materials used as CFC substitutes) **Products for Advanced Technologies** • Squaric acid and its derivatives (raw materials for recording media)
• CSPHP, a soy protein/phospholipid complex system that is used as a cholesterol lowering food ingredient, was added by the U.S. FDA to the list of products generally recognized as safe (GRAS) (March 2004). • Health foods operations and raw material alcohol operations transferred to the Bio-Chemicals Company (April 2004). • *Kokumi* seasoning MP-300 launched for use by processed food manufacturers (May 2004). • Second plant put into operation at Wuxi Xiehe Food Co., Ltd., a natural seasoning production and sales subsidiary in China (May 2004). • New liquid seasoning plant in Japan put into operation (May 2004).	**Seasonings** • Natural seasonings **Bakery Products and Ingredients** • Baker's yeast, premixes, baking improvers **Freeze-Dried Products** • Instant egg-drop soup **Health Food Products** • Vitamins, minerals, carotenoids, peptides, Remake series **Raw Material Alcohol** • For use in refined sake • For use in food preservatives and disinfectants

MESSAGE TO SHAREHOLDERS

Tadashi Hirata (*seated*), Chairman and Chief Executive Officer, and **Yuzuru Matsuda**, President and Chief Operating Officer

Operating Environment

In fiscal 2004, ended March 31, 2004, Kyowa Hakko faced intensified competition in its Pharmaceuticals operations. The acceleration of overseas development and the establishment of a presence in overseas pharmaceutical markets are becoming increasingly important. In Bio-Chemicals, amino acids for beverages and other health foods enjoyed strong demand, as did pharmaceutical ingredients. In Chemicals, sales of functional chemical products increased due to the public's concern with environmental conservation and to the advance of the information society. In Food, conditions remained difficult due to the ongoing market trends of sluggish consumption and lower prices.

Higher Revenues and Profits on Existing-Operations Basis in Year under Review

In this operating environment, in accordance with the Company's Eighth Medium-Term Management Plan, Kyowa Bio-Innovator, which covers the three-year period ending March 2005, Kyowa Hakko worked to steadily implement operational restructuring measures and to improve its financial position. At the same time, we endeavored to enhance our profitability through aggressive sales promotions and cost-cutting measures and to develop new products. Consolidated net sales in the year under review were down 2.9%, to ¥348.8 billion. However, excluding a decline of ¥14.3 billion in sales that was attributable to the transfer of alcoholic beverage operations in September 2002, sales increased on an existing-operations basis. Operating income grew 66.8%, to ¥26.8 billion, and net income was up 18.1%, to ¥10.0 billion. Cash dividends per share were unchanged at ¥7.5, comprising interim and year-end per-share dividends of ¥3.75 each.

Outlook for Fiscal Year Ending March 2005

The Kyowa Hakko Group's core Pharmaceuticals operations will be significantly affected by the April 2004 drug price revisions. We will continue to implement aggressive sales promotions and cost-cutting measures. Accompanying a decline in the number of consolidated subsidiaries, net sales in the year ending March 2005 are forecast to decrease 4.0%, to ¥335.0 billion, with operating income edging up 0.6%, to ¥27.0 billion, and net income rising 49.7%, to ¥15.0 billion.

Enhancing Enterprise Value

Guided by our corporate philosophy of "contributing to the health and well-being of people worldwide by creating new value with the pursuit of advancements of life science and technology," we strive to develop our operations on a global scale as an R&D-based company with a strong foundation of original, innovative research and technology.

In April 2005, we plan to complete the transition from the current in-house company system to a holding company system. As a "Bio-Innovator," with biotechnology as its core technology, Kyowa Hakko will become a holding company with two business pillars—Pharmaceuticals and Bio-Chemicals. At the same time, Chemicals and Food operations will be wholly owned subsidiaries. In this way, the Company will put in place a system that can meet customer needs more closely and rapidly, enhance the competitiveness and growth potential of the Kyowa Hakko Group, and further raise enterprise value.

In addition, as we work to improve our performance we will fulfill our social responsibilities—such as corporate ethics, quality assurance, and environmental safety—from the viewpoint of the customer. We will endeavor to be a company that is trusted by society.

We would like to ask our shareholders for their continued support in the years ahead.

June 2004

Tadashi Hirata
Chairman and Chief Executive Officer

Yuzuru Matsuda
President and Chief Operating Officer

Becoming the Number One Biotechnology Company in the World on a Foundation of Fermentation Technology

In the fiscal year ended March 2004, Kyowa Hakko achieved a significant increase in operating income. However, there still remains a substantial gap between the Company's actual performance and the goals spelled out in the Eighth Medium-Term Management Plan. In the following interview, President Matsuda, in his second year as president, discusses the strategies that Kyowa Hakko will follow.

Q How would you evaluate the fiscal year ended March 2004?

A In the past year, our results reflected our commitment to meeting our targets. Although net sales were down from the previous year, excluding the influence of the transfer of our alcoholic beverage operations, sales from existing operations were actually higher. As for profits, the operational restructuring measures that we have been implementing over the past several years began to show results, and in comparison with the previous fiscal year we achieved a significant increase in operating income. And our financial position has also improved rapidly.

However, we cannot celebrate. We did not reach the targets set out in the Eighth Medium-Term Management Plan. And in the current year, it will also be extremely difficult for us to achieve the plan's goals. We will closely analyze the gap between the targets set out in the plan and our actual performance and incorporate the results of that analysis into our future strategies.

In the past year, we implemented the principles of selection and concentration as we pursued growth in our stronger businesses and withdrew from unprofitable ones. At the same time, we decided to separate our Chemicals and Food operations into wholly owned subsidiaries that will compete in their own industries as independent businesses. Not all of our operational activities will take place under the Kyowa Hakko umbrella.

Q The past year was the second year of the Company's Eighth Medium-Term Management Plan. How would you evaluate the results to date?

A Before we began to implement the Eighth Medium-Term Management Plan, other than Pharmaceuticals, our Bio-Chemicals, Chemicals, Food, and Alcoholic Beverages operations were not profitable. They were supported by our core Pharmaceuticals operations. However, over the past two years of the plan, our Bio-Chemicals, Chemicals, and Food operations have all become profitable. This achievement of profitability in all segments is the largest success of the plan to date.

This performance is the result of progress in structural reforms in all of our fields of business. In Bio-Chemicals, we decided to withdraw from feed-grade amino acids, which are highly susceptible to market fluctuations, and to focus on high-value-added products that use our technologies, such as amino acids for pharmaceuticals, food, and industrial applications. In Chemicals, in the field of bulk products, we determined that it was important to expand the scale of our operations and boost our competitiveness, and accordingly we followed a strategy of aggressively entering alliances with other companies. In April 2000, our plasticizer joint venture with Mitsubishi Chemical Corporation commenced operations, and in April 2004 operations began at Japan Ethyl Acetate Co., Ltd., a joint venture with Showa Denko K.K. for ethyl acetate production. We have also achieved success in our efforts to expand our business in high-value-added specialty chemicals, such as environmentally friendly and IT-related products. In Food, we are focusing on high profitability fields, such as natural seasonings. We worked to expand our production capacity in Japan and China and to develop and build sales of new products that draw on our original technologies, such as *Kokumi* seasonings.

As a result of those efforts, over the past two years of our medium-term management plan, our non-pharmaceuticals operations have begun to record significant improvements in profitability.

In our core Pharmaceuticals operations, we made progress in clinical development in Europe and the United States, with consideration for overseas markets. For example, the clinical trials for anti-Parkinson's agent KW-6002 were stopped temporarily, but it has now completed phase IIb clinical trials and preparations are under way for phase III clinical trials in the U.S. and Europe.

We have positioned therapeutic antibodies as a key driver of future growth, and we have already reached agreements with three companies, including Medarex, Inc., to license our Potelligent™ strong-acting monoclonal antibody technology. In June 2004, we agreed to license Potelligent™ technology to Biogen Idec Inc., one of the world's most well-known biotechnology companies. We are making steady progress with initiatives targeting the growth and development of our Pharmaceuticals operations.

In regard to our short-term performance, the targets set out in our medium-term management plan were too high in certain aspects, which has resulted in the gap between our performance and the plan's targets.

First, our growth forecasts for core products Coniel®, an agent for treating hypertension and angina pectoris, and Allelock®, an antiallergic agent, were too high. Second, we planned to license-in new drugs in late development stages, but our progress did not meet expectations.

In non-pharmaceuticals operations, our forecasts for operating income in the year ending March 2005 are in line with the targets for the final year of the Eighth Medium-Term Management Plan. However, the plan's operating income target for Pharmaceuticals operations is ¥20.0 billion, while our forecast is ¥13.5 billion. This difference in Pharmaceuticals operations will be a significant factor in the gap between Kyowa Hakko's prospects and the targets of the Eighth Medium-Term Management Plan.

Q What strategies will Kyowa Hakko follow in the year ending March 2005?

A In non-pharmaceuticals operations, we will follow the principles of selection and concentration as we implement structural reforms. These clear principles provide an indication of the direction we will need to take. In Bio-Chemicals, we will use our technologies in the field of health care, centered on fermented bulk products, in which we boast world-class capabilities. In Chemicals, we will focus on functional chemical products, and in Food we will emphasize natural seasonings.

In our core Pharmaceuticals operations, the issue is how we will handle the gap between our performance and the targets of the Eighth Medium-Term Management Plan. This will also be a key point in the formulation of the Ninth Medium-Term Management Plan.

To resolve this issue, we will first strengthen our domestic marketing capabilities. We have added 100 MRs, reaching a total of 900. Also, we have implemented measures to bolster our marketing activities for such core products as Coniel® and Allelock®. These measures include the SMART (Sales and Marketing Transformation) Project. The results of such initiatives are steadily becoming apparent.

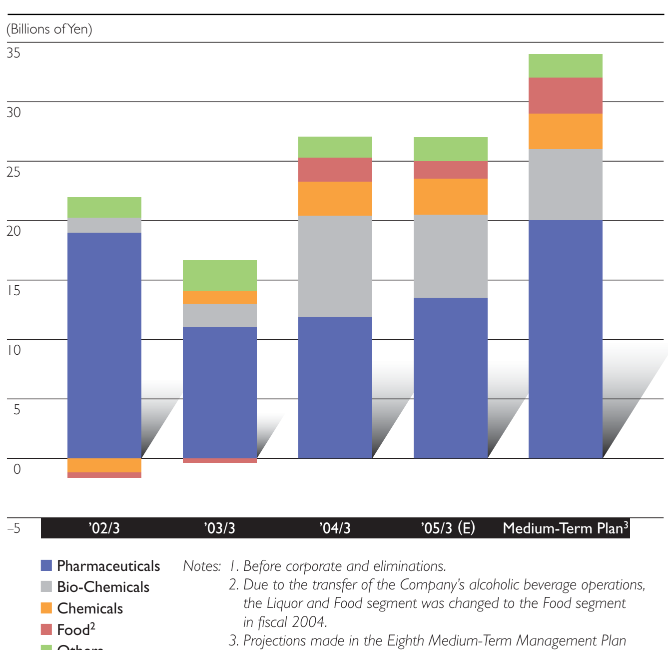
Next, using alliances, we will aggressively promote our strategy of product licensing, both to and from other companies. To that end, we have changed our organization and strengthened the licensing division.

We will also promote the POC (proof-of-concept) Fast strategy. In consideration of the scale of Kyowa Hakko's operations, there is no point in our imitating large, specialized global pharmaceutical companies. To launch products as rapidly as possible, we will conduct R&D with a special emphasis on speed from discovery to proof of concept, which is proof that a drug works as desired in humans. Once proof of concept is obtained, we have a broad range of choices, which will be made in accordance with the theme. We can continue in-house development overseas or we can elect to pursue joint development with the objective of buying time and a higher rate of success. We can also license a product to the most appropriate partner and, in turn, introduce a product that can be marketed in Japan.

The strengths of our Pharmaceuticals operations include our domestic discovery capabilities and the overseas development capabilities of Kyowa Pharmaceutical, Inc. (KPI), in the United States and Kyowa Hakko U.K., Ltd., in the United Kingdom. To promote the POC Fast strategy, we integrated our research and development organizations and removed the barrier between them. Moreover, with the goal of ensuring smooth interaction between domestic discovery capabilities and overseas development capabilities, we have appointed the executive vice president responsible for development at KPI, who has a superior development record in Europe and the United States, a member of the International Portfolio Committee, which meets in Japan. By incorporating his opinions from the early stage of development, we will speed up decision making, such as whether to continue, stop, or give priority to the development of a product. In this way, we will endeavor to increase development speed.

Also, with the achievement of profitability in all of our fields of business, the profits from each segment can be used as funding for aggressive initiatives in original R&D. This is

Operating Income (Loss) by Industry Segment



Notes: 1. Before corporate and eliminations.
2. Due to the transfer of the Company's alcoholic beverage operations, the Liquor and Food segment was changed to the Food segment in fiscal 2004.
3. Projections made in the Eighth Medium-Term Management Plan announced in April 2002.

a very important point. In each business segment, investment will be focused on priority fields. And in this way, Kyowa Hakko is moving forward into a period of growth and development.

Q How will the Company proceed with the process of converting in-house companies into subsidiaries?

A Regarding this process, we have two goals for our Chemicals and Food operations—independence and rapid management.

As independent companies, they will only survive if they cut unprofitable operations and implement rapid management. We have transferred authority to those segments to make them self-reliant business entities, making it possible for them to make decisions quickly. The Chemicals operations, which already started as Kyowa Hakko Chemical Co., Ltd., in April 2004, are doing very well, and we expect the same performance from Food operations, which are scheduled to be separated into a new subsidiary in April 2005.

On the other hand, in Bio-Chemicals, we have changed our initial plan, which was to separate these operations into a wholly owned subsidiary, and decided to manage them under the holding company, as a core operation along with Pharmaceuticals. The reason is that we expect that Pharmaceuticals and Bio-Chemicals will move closer together in the years ahead. In Bio-Chemicals, we are making pharmaceutical raw materials, and, as I will explain shortly, we are building original health care operations through the use of the infrastructure in Pharmaceuticals. Accordingly, it is necessary for our Bio-Chemicals operations to work closely with Pharmaceuticals.

Also, as we move ahead with this process, such matters as corporate ethics, quality assurance, and environmental safety are Groupwide risk management issues, and therefore responsibility for them must be assumed on a Groupwide basis. That is why we established the Corporate Compliance Division in April 2004 and assigned a full-time director.

Q Kyowa Hakko has strengthened its financial position considerably. Would you elaborate?

A In the year ended March 2004, we redeemed bonds prior to maturity, and, accompanying the dissolution of the retirement benefit trust, we recorded as an expense the entire amount of the unrecognized actuarial differences from the trust. Now, we effectively have no borrowing, and our equity ratio has reached 62.3%. Our balance sheet has improved considerably.

However, if a certain investment is necessary for the Kyowa Hakko Group to continue to grow and develop in the future, then we will make that investment even if we have to increase borrowing temporarily. The future focus of our investment activities will be the strengthening of existing operations where we have an established customer base and market position. In existing operations, we want to achieve further increases in sales and profits.

We are using operating return on assets to evaluate the performance of each of our operational segments. In the year ended March 2004, operating return on assets for the Company as a whole was 7.4%, approaching the 8% target in the Eighth Medium-Term Management Plan.

Q What are your thoughts on the social mission of companies?

A My definition of the social responsibility of a company is "to become an integral part of the social framework and to offer products and services that work in social cycles without any resistance." Without companies that act in this way, the social framework will not function, so this is probably the number one social mission for a company.

I do not believe that any other company can boast of fulfilling its social responsibilities to the extent that Kyowa Hakko has. After World War II, we were devoted to eliminating tuberculosis from Japan, and we invested a huge sum of money to introduce streptomycin from Merck & Co., Inc., of the United States. To build up the physiques of Japanese, we wanted to provide high-quality protein at a low price, and we achieved a world first with the successful industrial production of amino acids using fermentation. These activities were not driven by the desire to make a profit; rather, they were performed as a social mission. I think we should recognize the spirit that Kyowa Hakko had at the time of its founding.

Returning to Kyowa Hakko's starting point as a company that accepts challenges, in April 2004 we established the BioFrontier Laboratories, which are under my direct control and are dedicated to boldly taking on the challenges of new research fields. We will provide facilities for researchers to explore themes in which they are interested and will accept the challenge of creating new fields of business suitable for Kyowa Hakko.

Q Would you tell us about the direction Kyowa Hakko will take in the future?

A As a holding company, Kyowa Hakko will move forward with two business pillars—Pharmaceuticals and Bio-Chemicals. There will be no other company in the world like this. This is a unique framework, and we will build a competitive edge with a distinctive presence.

One specific example is health care. Because Kyowa Hakko is involved in pharmaceuticals, it has accumulated infrastructure, such as drug formulation, genome, and pharmacological evaluation technologies. For example, our pharmaceutical technologies enable the reliable delivery to the liver of ingested substances. At our Healthcare Research Laboratories*, we can provide data that scientifically backs up the beneficial functioning in the body of health care related substances. And with our strengths in fermentation, we have production technologies that other companies cannot match. We focused all of our resources on the start-up of health care operations in our Bio-Chemicals operations, and we believe that health care is a field in which we will see synergies between Pharmaceuticals and Bio-Chemicals operations.

One goal that Kyowa Hakko is pursuing is to be the world's number one biotechnology company based on fermentation technology. In Pharmaceuticals, we aim to discover innovative drugs that contribute to progress in medicine, such as therapeutic antibodies. In Bio-Chemicals, we aim to provide fermented bulk products, including health care products, to global markets. And what these two fields have in common is biotechnology. By moving ahead with operational development that is distinctively original and draws on our special technological strengths, we will work to further raise the enterprise value of the Kyowa Hakko Group.

*In April 2004, the name of Tsukuba Research Laboratories was changed to Healthcare Research Laboratories.

CORPORATE GOVERNANCE

Fundamental Approach

Kyowa Hakko conducts its operational activities in accordance with its corporate philosophy of "contributing to the health and well-being of people worldwide by creating new value with the pursuit of advancements of life science and technology." Our fundamental approach to corporate governance is to establish the management organization and framework and implement the policies that are necessary to realize this philosophy.

Kyowa Hakko's system of basic management institutions comprises the corporate institutions stipulated by the Commercial Law Act—a board of directors and a board of auditors. The board of directors, which has eight members as of June 29, 2004, makes decisions about important issues, such as management policies, and supervises the work of the directors. As of June 29, 2004, the board of auditors has four members, of whom three are outside auditors. In accordance with auditing policies determined by the board of auditors, the auditors attend important meetings, such as meetings of the board of directors, conduct investigations of operations and assets, and audit the work of the directors.

A management meeting was established as a decision-making body that would make accurate and effective management decisions from a strategic viewpoint for all important issues related to management.

In 1999, to clarify operational responsibility, we introduced the in-house company system and transferred authority. Also, to ensure rapid management decision making and administrative execution, Kyowa Hakko introduced a corporate executive officer system.

Progress in Initiatives

In July 2003, Kyowa Hakko established an advisory board to provide outside management viewpoints, to strengthen the management constitution, and to increase the transparency and soundness of management in regard to management issues faced by Kyowa Hakko and the Kyowa Hakko Group. To respond to various risks inherent to management issues, we established a number of in-house committees, such as the Corporate Ethics Committee, the Environmental Safety Committee, the Quality Assurance Committee, the Information Disclosure Committee, and the Financial Management Committee.

On April 1, 2004, to strengthen internal control in such areas as corporate ethics, quality assurance, and environmental safety and to enhance corporate social responsibility activities, we established the Corporate Compliance Division. From April 2005, we plan to give more authority to each operational area and move to a holding company system to achieve rapid operational administration stemming from quicker decision making and the clarification of operational responsibility.

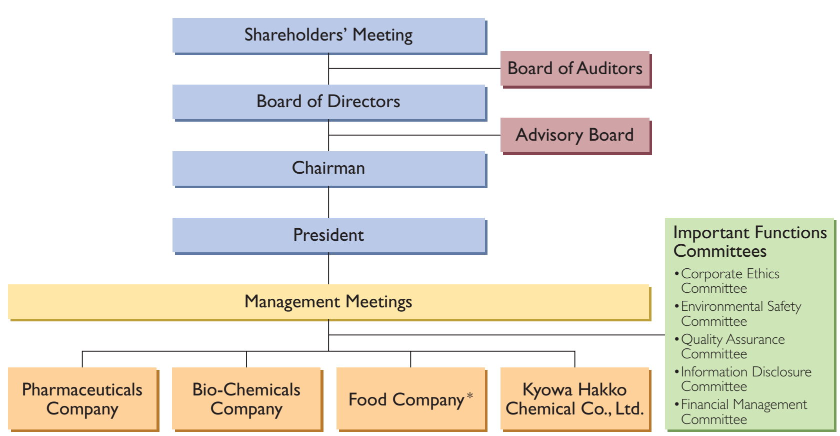
Increasing Management Transparency

Kyowa Hakko aims to be a company that is relied upon by all of its stakeholders, including shareholders, customers, and local communities. By using a variety of opportunities and methods, such as the timely disclosure of the Kyowa Hakko Group's management information and an enhanced web site, we are working to raise management transparency through appropriate information release and disclosure.

Corporate Ethics

We have established Kyowa Hakko ethics principles and employee ethics action standards that form the basis of the activities of all employees at Kyowa Hakko Group companies. Also, we have established the Corporate Ethics Department and are working to provide employees with ongoing education and to raise their awareness of issues related to ethics.

Corporate Governance Organization



** Scheduled to become a wholly owned subsidiary in April 2005.*

R&D PIPELINE

(As of June 2004)

Category Code Name *Generic Name*	In-house/Licensed From *Indication*	Stage in Japan	Stage Overseas (Country)	Remarks
Anticancer				
KW-2307* *Vinorelbine ditartrate*	Pierre Fabre *Breast cancer*	Filed [June 2000]		Product name: Navelbine® Original indication: Non-small-cell lung cancer
KW-2401 (UCN-01)	In-house *Malignant tumor*	Phase I [completed]	Phase I/II (U.S.)	Sponsored by the National Cancer Institute, of the U. S.
KW-2871	In-house *Malignant melanoma*		Phase I/IIa (U.S.)	Chimeric monoclonal antibody
KW-2246 *Fentanyl citrate*	Orexo *Cancer pain*	Phase I		
Central Nervous System				
KW-6485 *Topiramate*	Cilag *Antiepileptic*	Phase III		
KW-6002 *Istradefylline*	In-house *Parkinson's disease*	Phase I	Phase IIb (U.S. & Canada) [completed]	
Cardiovascular, Urology				
KW-3049 *Benidipine hydrochloride*	In-house *Hypertension*		Approved (China) [March 2004]	Product name: Coniel® (Launched in Japan)
GMK-527* *Alteplase*	Genentech *Acute ischemic stroke*	Filed [April 2004]		Jointly developed with Mitsubishi Pharma Original indication: Acute myocardial infarction Product name: Activacin®
KW-7158	In-house *Urinary incontinence*	Phase I	Phase IIa (U.S. & Europe)	
Other				
MM-Q01	Meiji Dairies *Contrast medium for MRI*	Filed [March 2003]		Jointly developed with Meiji Dairies

** For additional indication*

On a base of fermentation technology, the Kyowa Hakko Group has developed distinctive operations in Pharmaceuticals and a range of other fields. In our core Pharmaceuticals operations, we are developing highly effective drugs in fields in which we have special strengths, such as cancer and allergies. And in amino acids, which are the focus of growing attention, we boast some of the world's most advanced technologies. Kyowa Hakko will draw on its strengths in biotechnology, based on fermentation, as it strives for continued growth in its Pharmaceuticals and Bio-Chemicals operations.

In this section, we introduce the keys to our future—global pharmaceutical development, antibody technologies, and progress in Bio-Chemicals operations—and outline the factors that will support our growth in the years ahead.

BIOTECHNOLOGY:
Building on Our Strengths

Kyowa Pharmaceutical, Inc., and Kyowa Hakko U.K. Ltd. will play central roles in overseas drug development. With consideration for global markets, we are moving forward with clinical development targeting the quickest possible launches of highly effective drugs, such as anti-Parkinson's disease agent KW-6002.

(*From left:* Kazuyoshi Tachibana, President and CEO; Dr. Philip Chaikin, Executive Vice President, Kyowa Hakko International Development Head; and Dr. April Teitelbaum, Vice President, Clinical Research, of Kyowa Pharmaceutical, Inc.)

Global Development in Pharmaceuticals

For its original drug pipeline, the Pharmaceuticals Company follows a policy of conducting development overseas first in accordance with its company vision. We generally handle the development on our own up to phase IIa, where efficacy is confirmed. In phase IIb and thereafter, we must decide whether to file an NDA based on our own development, to license out the drug, or to conduct joint development with another company. In making that decision, we emphasize maximizing value based on our portfolio analysis for the entire development pipeline.

In line with this policy, we have established two clinical development subsidiaries: Kyowa Pharmaceutical, Inc., which is located in Princeton, New Jersey, in the United States, and Kyowa Hakko U.K. Ltd., which is situated in Slough, Berkshire, near London, in the United Kingdom. In our three-part development system—centered on Japan, Europe, and the United States—we have completed the preparation of infrastructure, such as safety information and document management systems, which are now operating smoothly. Our development pipeline includes drugs that will soon enter into late stage clinical trials, and accordingly we are working to increase our overseas development workforce.

Progress with Key Development Drugs

For Parkinson's Disease: KW-6002

KW-6002, the world's first selective adenosine A2A receptor antagonist, is under development as a treatment for Parkinson's disease. Its effectiveness in improving the "wearing-off" effect has been confirmed, and we are now preparing for the start of phase III large-scale clinical trials in the United States and Europe in the third quarter of 2004. We are in the process of determining the best way to promote this drug and maximize its value.

For Urinary Incontinence: KW-7158

KW-7158 is a non-cholinergic compound with a tricyclic structure. It differs from existing anticholinergic drugs in that it is effective on the peripheral sensory nerves in the bladder. Indications are expected to include urinary frequency, urinary incontinence, and sense of urgency caused by overactive bladder contractions. In Europe and the United States, phase IIa trials have been completed. The market for this drug is large and includes competing products from global companies; therefore, our overseas development and operations will likely be based on alliances.

For Cancer: KW-2871

KW-2871, an anticancer agent for malignant melanoma, is a monoclonal antibody that binds specifically to the GD3 cell surface antigen, which is expressed in about 90% of melanoma cells. Phase I trials have been completed in Australia, and KW-2871 is now in phase I/IIa trials in the United States.

Cancer is one of our core fields and is an area in which we will continue to develop our overseas operations. We are already marketing products overseas, principally anticancer agent Mitomycin C, through subsidiaries in the United Kingdom; Italy; Singapore, which is our base in Asia; Malaysia; and Thailand. In China, we are developing our operations through Kyowa Pharmaceutical (H.K.) Co., Ltd. In the future, while effectively utilizing the development and sales capabilities that we are establishing overseas, we will choose the optimal method for development and sales in accordance with the scale of the potential market and the competitive situation.

Operations in China

In March 2004, Coniel®, an agent for treating hypertension, was approved as an imported drug by China's State Food and Drug Administration (SFDA), and we are now preparing to begin sales. In addition, the IND for antiallergic agent Allelock® was submitted in July 2003, and clinical trials are expected to commence in the third quarter of 2004.

Products for which Development Has Been Stopped

From a business perspective, Kyowa Hakko has stopped the development of anticancer agent KW-2170 and antiasthmatic KW-4490 because the results of the phase IIa clinical trials did not demonstrate sufficient efficacy. Kyowa Hakko will continue to position cancer and allergies as core fields and will focus its discovery and development activities on original candidate compounds in these fields.

(As of June 2004)

Principal Candidate Dewgs				Development Schedule					
Category	Code Name	Indication	Target Sales Scale at Peak*	2004	2005	2006	2007	2008	2009
Central Nervous System	KW-6002	Parkinson's Disease	Large	Phase IIb [completed] (U.S. & Canada)		NDA Filing			
Urology	KW-7158	Urinary Incontinence	Large	Phase IIa (U.S. & Europe)					NDA Filing
Anticancer	KW-2871	Malignant Melanoma	Medium	Phase I/IIa (U.S.)					NDA Filing

** Medium: over ¥10 billion / Large: over ¥30 billion*

Potelligent™ technology facilitates remarkable results in the development of biopharmaceuticals. U.S. subsidiary BioWa, Inc., which markets Potelligent™ technology, is emphasizing its dramatic effectiveness and ease of use through such activities as conference sponsorship and is working to establish alliances with other companies, centered on licensing.

(*From left:* Dr. Patrick J. Kocks, Associate General Counsel; Dr. Nobuo Hanai, President and CEO; and Martina Molsbergen, Director of Business Development, of BioWa, Inc.)

Operational Development in Antibody Technologies

More than a year has passed since U.S. subsidiary BioWa, Inc., was founded in Princeton, New Jersey, in April 2003 with capital of $5 million. Led by President and CEO Nobuo Hanai, the company has worked with a range of partners and participated in numerous conferences and meetings. BioWa's business activities have centered on the licensing of Potelligent™ technology, which dramatically increases antibody-dependent cellular cytotoxicity (ADCC) activity. Aggressive public relations activities have ensured that the BioWa name is widely known in the European and U.S. biotech industries. In 2004, BioWa has been a sponsor of such conferences as BioPartnering North America (February, Vancouver), BIO-Windhover (April, Washington D.C.), BIO 2004 (June, San Francisco), and Antibody World Summit (July, Philadelphia). In January 2004, the company took a key step toward underpinning its future growth when Martina Molsbergen joined BioWa as Director of Business Development.

In licensing Potelligent™ technology, in addition to U.S. biopharmaceutical company Medarex, Inc., licensing contracts have been concluded with several other biotechnology companies in Europe and the United States that are conducting antibody development. In June 2004, we agreed to license our Potelligent™ technology to Biogen Idec Inc., one of the world's most well-known biotechnology companies. We anticipate strong growth in Potelligent™ technology licensing contracts, and accordingly we are working to support the expansion of our operations by providing partners with antibody research and development capabilities and aggressively conducting the joint development of antibodies with enhanced ADCC activity.

There has been great progress in the development of Potelligent™ technology at Kyowa Hakko. We succeeded in generating antibodies with less or no fucose by cells capable of high productivity. BioWa has set up this cell bank in companies with GMP-compliant facilities in the United States, rapidly provided cells to partners, and built a system to initiate R&D. In addition, papers related to Potelligent™ technology have been published in some of the world's leading journals in such fields as biochemistry, molecular biology, and oncology. The heightened evaluation of Potelligent™ by scientists has led to increased contacts with leading companies.

BioWa's Revolutionary Antibody Technology

Potelligent™ technology allows the production of antibodies with a 100-fold or greater enhancement in ADCC, which results in significant improvement in the lysis of low-antigen cells and can provide effective treatment for the majority of patients who are currently resistant to the approved antibodies. This efficacy has been demonstrated in animal models. The revolutionary Potelligent™ technology is compatible with ADCC antibody manufacturing processes developed by partners. Also, by using BioWa's stable Potelligent™ cells, high ADCC antibodies can be produced with the same manufacturing processes utilized previously. The cell line used to generate antibodies does not add fucose, but in respect to other antibody properties it is no different from other production cell lines.

Selected POTELLIGENT™ Articles

- **Shinkawa T et al.:** *The Absence of Fucose but Not the Presence of Galactose or Bisecting N-Acetylglucosamine of Human IgG1 Complex-Type Oligosaccharides Shows the Critical Role of Enhancing Antibody-Dependent Cellular Cytotoxicity. J. Biol. Chem., Vol. 278, Issue 5, 3466–3473, 2003*
- **Niwa R et al.:** *Defucosylated Chimeric Anti-CC Chemokine Receptor 4 IgG1 with Enhanced Antibody-Dependent Cellular Cytotoxicity Shows Potent Therapeutic Activity to T-Cell Leukemia and Lymphoma. CANCER RESEARCH 64, 2127–2133, 2004*
- **Okazaki A et al.:** *Fucose Depletion from Human IgG1 Oligosaccharide Enhances Binding Enthalpy and Association Rate between IgG1 and FcgRIIIa. J. Mol. Biol. (2004) 336, 1239–1249*

Antibody Pipeline

Category	Code Name	Target	Indications	Stage
Anticancer	KW-2871[1]	Ganglioside GD3	Malignant melanoma	Phase I/IIa
	KM2550[1]	VEGF-R/FLT-1	Breast and colon cancers	Preclinical
	Undisclosed	FGF8	Prostate, breast, and ovary cancers	Preclinical
	Undisclosed	Cytokine	Solid tumor	Preclinical
	Undisclosed[1]	Tumor antigen	Hematolologic and solid tumors	Preclinical
	Potelligent™-GM2[1, 2]	Ganglioside GM2	Lung cancer, glioblastoma	Preclinical
	Potelligent™-GD2[1, 2]	Ganglioside GD2	Solid tumor	Preclinical
Antiallergic	Potelligent™-IL5R[1]	IL-5 Receptor	Asthma	Preclinical
	Potelligent™-T Cell[1]	T-Cell	Asthma	Preclinical

Notes: 1. Potelligent™ technology applied
2. Product rights transferred to BioWa

Amino acids are the focus of attention in such fields as beverages and other health foods. Centered on amino acids and other fermented bulk products, we are working to provide a stable supply of high-quality products, to develop new applications for these products, and to aggressively expand global business operations.

(*From left:* Dr. Akio Ozaki, General Manager of Development Department; Toshifumi Asada, Executive Officer, Vice President; and Dr. Toshikazu Kamiya, Head of the Healthcare Research Laboratories, of Bio-Chemicals Company, Kyowa Hakko)

OUTLOOK FOR BIO-CHEMICALS OPERATIONS

The Bio-Chemicals Company's core business is the production and marketing of fermented bulk products, such as amino acids, nucleic acids, and related compounds. Fermentation has been one of Kyowa Hakko's key technologies since the Company was founded, and in 1956 Kyowa Hakko achieved a world first with the successful industrial production of amino acids through the use of fermentation. The Bio-Chemicals Company's goal is to provide high-quality fermented bulk products, such as amino acids, to customers in such fields as pharmaceuticals, pharmaceutical intermediates, food products, dietary supplements, and cosmetics, thereby helping them to raise their corporate value.

Amino acids are widely used in a range of health care and related fields, from pharmaceuticals to cosmetics. The fields that are currently drawing the most attention are beverages and dietary supplements. Since amino acids became an established part of the U.S. market for dietary supplements, demand for them has expanded in the United States. In recent years, beverages containing amino acids have become bestsellers in Japan as well, and demand for amino acids has grown dramatically. Demand for dietary supplements is also expected to rise in the years ahead as a result of growing concerns about health amid pressure to reduce medical expenditures.

To further strengthen our operations in these health care fields, the health foods operations of the Food Company have been integrated into the Bio-Chemicals Company. As a result, Kyowa Hakko's health care business, which had been developed separately in the Food and Bio-Chemicals companies, has now been unified. The Bio-Chemicals Company has a diverse array of amino acids and other fermented products and has developed a wide range of operations in this field, not only in Japan but also in the United States, Europe, and China. The Food Company's health foods operations, which were principally oriented toward the domestic market and based on a business model somewhat different from that of the Bio-Chemicals Company, have successfully cultivated original business know-how and customer information extending from research to sales. At the same time, the Food Company built an original product lineup that includes CSPHP, a soy protein/phospholipid complex system. Through the integration of the Bio-Chemicals Company, with its wealth of experience in overseas operational development, and the health foods operations of the Food Company, with its original business model centered on the domestic market, Kyowa Hakko has laid the foundation for broader, more active expansion of its original business activities in health care fields.

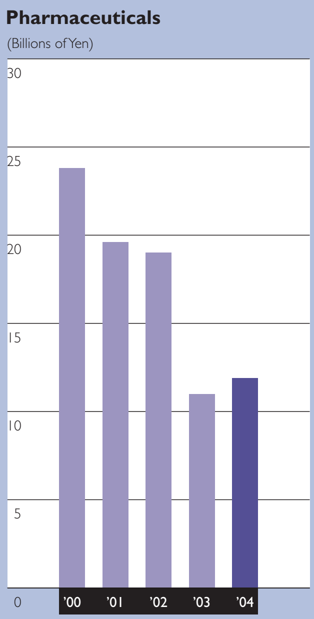
To provide support for the creation of synergies stemming from the integration of these operations, we have expanded and strengthened the Healthcare Research Laboratories*, which is now equipped to handle a range of functions. These functions include the discovery of new substances; the development of new products and applications through the testing of the characteristics and functions of amino acids and other materials; the development of secondary processing technologies, such as tableting and taste improvement; the proposal of new formulations; and marketing support.

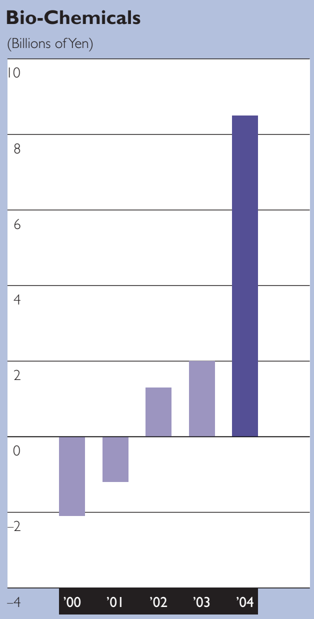
In the markets for amino acids and other fermented bulk products, competition is intensifying as manufacturers in South Korea and China expand their operations. To maintain our position as a leading company in this highly competitive environment, we must allocate our management resources effectively and selectively. To that end, we decided to withdraw from feed-grade amino acids, which had become a commodity, and to concentrate on high-value-added fermented bulk products, centered on health care.

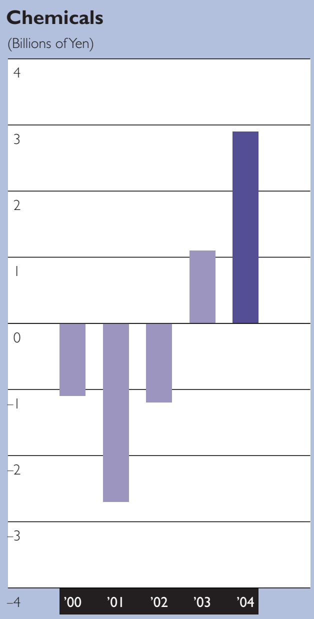
In production technology, we will focus our research resources on the creation of new fermented products that have the potential to become mainstay businesses and on the development of fermentation technologies targeting thorough cost reductions. Also, to optimize our production bases, we decided to increase our investment in our joint venture in Shanghai, make it a subsidiary, and raise its production capacity. As a result, we have strengthened our production system, centered on Japan, the United States, and China. In the future, we will work to maintain and enhance our competitiveness and further expand our fermented bulk products operations on a global scale.

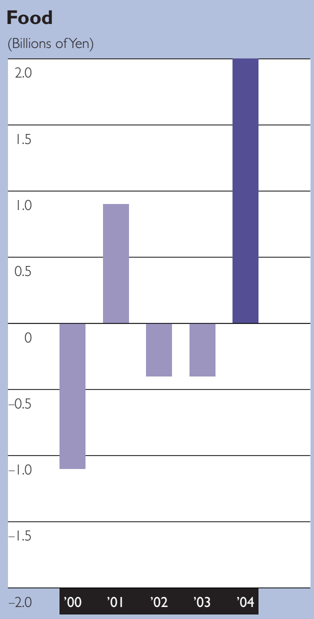
* In April 2004, the name of Tsukuba Research Laboratories was changed to Healthcare Research Laboratories.

Segment Operating Income (Loss)







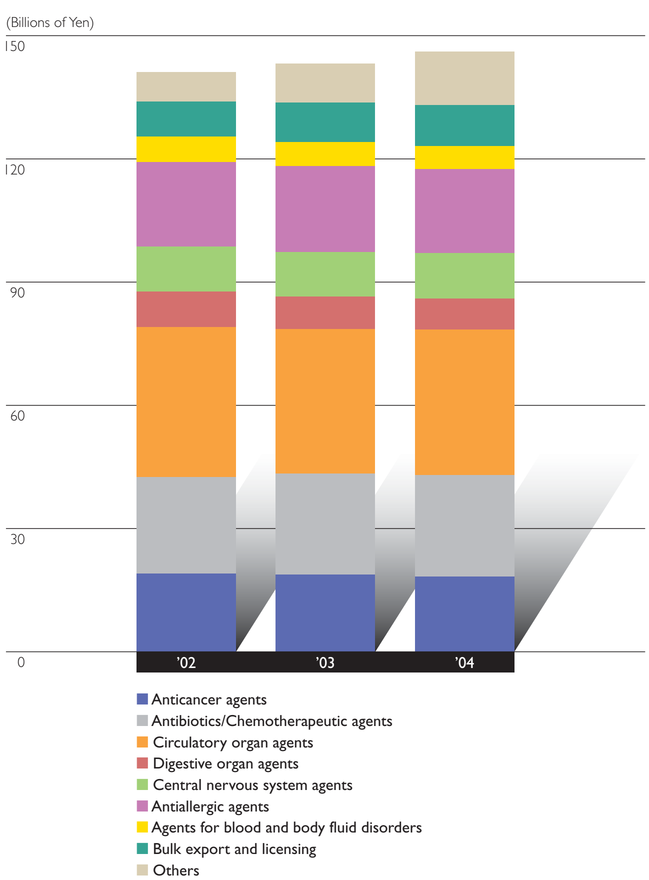


REVIEW OF OPERATIONS

Company President
Yoshito Imai
Senior Managing Director

PHARMACEUTICALS

Fiscal 2004 Sales Breakdown
(Nonconsolidated basis)



INDUSTRY OUTLOOK

Against a background of swift trends toward fewer children per family and an aging population, sluggish economic conditions, and changing public thinking about health care, Japan's health care system is undergoing a fundamental reevaluation and moving toward patient-centered medicine, with an emphasis on facilitating the provision of medical information, enhancing quality and efficiency, and promoting standardization. Moreover, the pharmaceutical industry is undergoing significant reform, with the reorganization of pharmaceutical companies in Japan and overseas proceeding on a large scale.

In this operating environment, Kyowa Hakko will focus its research resources on the fields of cancer and allergies and on core technologies, such as antibodies. We will strive to develop drugs that meet medical needs and, at the same time, to contribute to evidence-based medicine through the provision of high-quality medical information. As always, we will work to be a company that is trusted by its customers—patients and health care workers.

OPERATIONAL STRATEGY

The key strategic objectives for the Pharmaceuticals Company are the generation of cash flow through the strengthening of domestic marketing capabilities for ethical drugs and the use of a portion of those funds to drive the aggressive development of overseas operations.

In Japan, to enhance the provision of information about the distinctive characteristics of Allelock®, our core antiallergic agent, and to increase its market penetration, in October 2003 we began a joint promotional campaign with Kyorin Pharmaceutical Co., Ltd., which boasts special strengths in practicing physicians in internal medicine and otorhinology. We expect this alliance to help us to maximize the value of Allelock®.

In April 2004, with the goal of increasing the speed and efficiency of R&D, we implemented an organizational integration of our R&D system. The person responsible for clinical development at our U.S. subsidiary Kyowa Pharmaceutical, Inc., now participates in decision making, and the new system aims to obtain proof-of-concept as rapidly as possible. With the completion of these changes to our R&D system, we believe that we have established the foundation to support growth over the medium to long term.

Overseas, we are implementing an operational development project under which we will strive to rapidly launch products in development and maximize their value, centered on KW-6002, an anti-Parkinson's disease agent; KW-7158, a treatment for urinary incontinence; and KW-2871, an anticancer agent. In China, where the development of Coniel® has been under way, approval has been received and we are preparing to begin sales. To aggressively promote operational development using our original Potelligent™ strong-acting monoclonal antibody technology, in 2003 we established BioWa, Inc., in the United States, and BioWa has already signed contracts with several companies, such as Medarex, Inc.

OVERVIEW

In fiscal 2004, the Pharmaceuticals Company faced intensified competition, due in part to the advances of overseas pharmaceutical companies. Net sales rose 1.6%, to ¥142.9 billion, with support from higher sales of core products, such as antiallergic agent Allelock® and analgesic for persistent cancer pain Durotep® Patch. Operating income was up 8.1%, to ¥11.9 billion, primarily because of higher sales and lower SG&A expenses.

Ethical Drugs

In ethical drugs, measures to control health care spending and intensified competition led to continued difficult conditions, but sales increased from the previous year.

Sales of core product Coniel®, an agent for treating hypertension and angina pectoris, were level with the previous year due to intense competition in the market for calcium antagonists. Higher sales were recorded by Allelock® (olopatadine hydrochloride), an antiallergic agent, despite lower than normal levels of pollen. In October 2003, we began joint sales promotions with Kyorin Pharmaceutical to achieve greater market penetration.

Allelock®, an antiallergic agent

Coniel®, an agent for hypertension and angina pectoris

Desmopressin Spray 10 Kyowa, a treatment for nocturnal enuresis

Durotep® Patch, an analgesic for persistent cancer pain, recorded significant sales growth and became the top brand in its field.

In June 2003, we began sales of Desmopressin Spray 10 Kyowa, a treatment for nocturnal enuresis, and in July we launched Mevastan, a treatment for hyperlipidemia, and Fluconamerck, a treatment for deep mycosis.

In bulk exports and technology out-licensing, sales increased. Higher sales were recorded by olopatadine hydrochloride, an antiallergic agent licensed out to Alcon Laboratories, Inc., of the United States. In August 2003, we began the first overseas marketing of Allelock®, in South Korea, and sales have been favorable.

HM-JACK plus Fecal Occult Blood Test Analyzer

In Japan, the Company has filed applications for additional indications for Activacin®, a thrombolytic agent, and for Navelbine®, for cancer, as well as an NDA for MM-Q01, an MRI contrast medium for the gastrointestinal tract. Moreover, we are preparing to file an NDA for antiepileptic KW-6485. Clinical trials are under way for KW-2246, an analgesic for cancer pain.

Overseas, we filed an NDA for Coniel® in China in September 2003 and received approval for Coniel® as an imported drug in March 2004. We are moving ahead with the development of the anti-Parkinson's disease drug KW-6002 and the urinary incontinence treatment KW-7158 in Europe and the United States, and biopharmaceutical KW-2871 is under development in the United States for the treatment of malignant melanoma.

Principal Drug Sales (Nonconsolidated basis)

	Billions of Yen		
	2004	2003	2002
Coniel	**¥28.9**	¥28.8	¥29.9
Allelock	**13.3**	11.8	8.7
Celtect	**7.0**	8.9	11.8
Itrizole	**23.4**	23.2	22.0
Depakene	**9.8**	9.6	9.6
Adriacin + Farmorubicin	**8.9**	7.9	7.1
Nauzelin	**7.1**	7.5	8.2
5-FU	**4.4**	5.2	5.9
Neu-up	**4.8**	5.0	5.2
Durotep	**8.8**	4.7	0.1
Bulk export and licensing	**10.0**	9.6	8.4

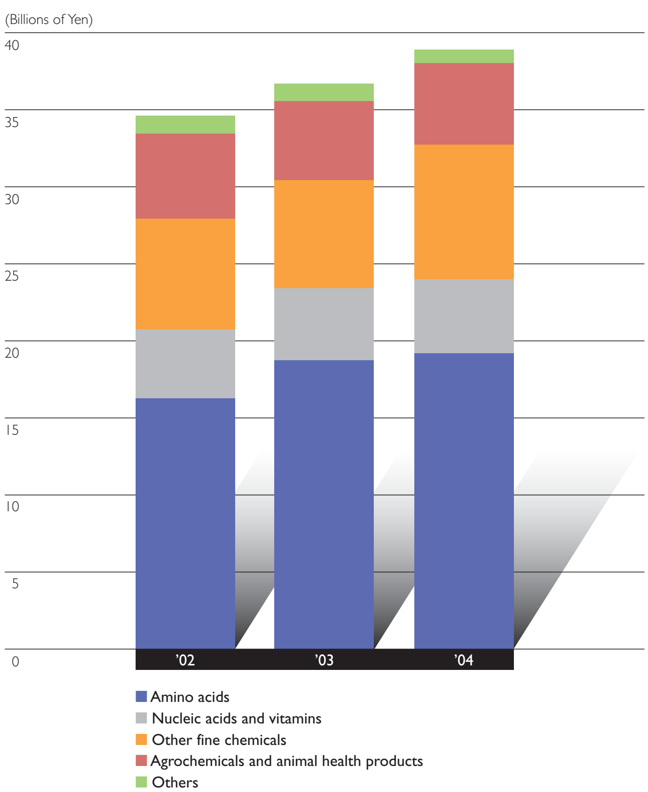
Diagnostic Reagents

Kyowa Medex Co., Ltd., a subsidiary handling the manufacture and sale of diagnostic reagents, recorded higher sales. Sales of clinical chemistry diagnostic reagents declined due to greater competition. However, sales of immunological reagents were supported by favorable performances by such products as Determiner® HbA1c, a diabetes reagent.

Company President
Tomonori Yuji
Managing Director

BIO-CHEMICALS

Fiscal 2004 Sales Breakdown
(Nonconsolidated basis)



INDUSTRY OUTLOOK

In Japan and overseas, demand continues to increase for amino acids for use in food, such as best-selling beverages containing amino acids in Japan and other health foods and dietary supplements. In particular, with concern for health maintenance and promotion heightening around the world and growing pressure to contain medical expenditures, demand for health care related products is expected to expand in the years ahead. In addition, pharmaceuticals that contain amino acids as a fundamental structure have become an established part of the market, and demand for amino acids for use as pharmaceutical intermediates, and as pharmaceutical ingredients for parenteral and enteral nutrition preparations, is strong.

On the other hand, following the BSE and SARS outbreaks, requirements for quality assurance are increasing in a range of fields. The capabilities to provide a stable supply of high-quality products and the maintenance and improvement of the quality assurance system that supports those capabilities are essential.

OPERATIONAL STRATEGY

The Bio-Chemicals Company's core business is the production and marketing of fermented bulk products, such as amino acids, nucleic acids, and related compounds. As the industry leader, the Bio-Chemicals Company supplies these products to customers around the world. Applications for amino acids include raw materials for pharmaceuticals, such as infusions and anti-ulcer agents; health foods and dietary supplements; pharmaceutical intermediates; and cosmetics. In all of these areas, customers require a stable supply of high-quality, competitively priced products, and accordingly the Bio-Chemicals Company is strengthening its production and quality assurance systems to meet market needs. We have built a production system with manufacturing bases in Japan, the United States, and China. As one facet of our efforts to strengthen that system, we agreed to increase our investment in Shanghai-based joint venture Shanghai Guan Sheng Yuan Kyowa Amino Acid Co., Ltd., and to make it a subsidiary. At the same time, we decided to change the company's name to Shanghai Kyowa Amino Acid Company, Ltd., and to raise its production capacity through the construction of a new plant. In addition, the Food Company's health foods operations have been integrated into the Bio-Chemicals Company. This step will help us to achieve further expansion of

our health care business, in which demand has been growing in recent years. Moreover, in accordance with our decision to withdraw from feed-grade amino acid operations, which had been in a restructuring phase, we will focus our management resources on our core operations.

OVERVIEW

Sales of fermented bulk products, such as amino acids, nucleic acids, and related compounds, were supported by the launch of new products and by higher sales in the domestic market of amino acids used in beverages and other health foods. The Bio-Chemicals Company's net sales rose 0.8%, to ¥59.0 billion. Operating income was up 330.0%, to ¥8.5 billion, due to the increase in sales and to improved profitability at overseas subsidiaries, such as Biokyowa Inc., of the United States, which began reorganizing its operations in the previous fiscal year.

Fine Chemicals

Sales of fermented bulk products increased, mainly due to strong domestic sales. In Japan, sales of amino acids for beverages continued to rise, and a contribution was made by the launch of new pharmaceutical ingredients.

Despite lower sales of other bulk products, overseas sales also increased, because of the transfer of production and sales of amino acids to overseas subsidiaries.

In R&D, in addition to ongoing technical development, we conducted fermentation-based production technology development targeting thorough cost reductions. In health foods, we continued to aggressively develop applications for our products, and we have had success in the areas of tableting technologies and flavor improvement of amino acids. We have also developed new pharmaceutical ingredients.

Agrochemicals and Animal Health Products

Sales of agrochemicals declined slightly, reflecting lower exports to Asia. Sales of products for the livestock industry also decreased marginally, due to sluggish markets stemming from a cool summer and the outbreak of avian influenza. Sales of products for the fisheries industry increased significantly thanks to efforts to expand sales of marine feed.

Feed-Grade Amino Acids

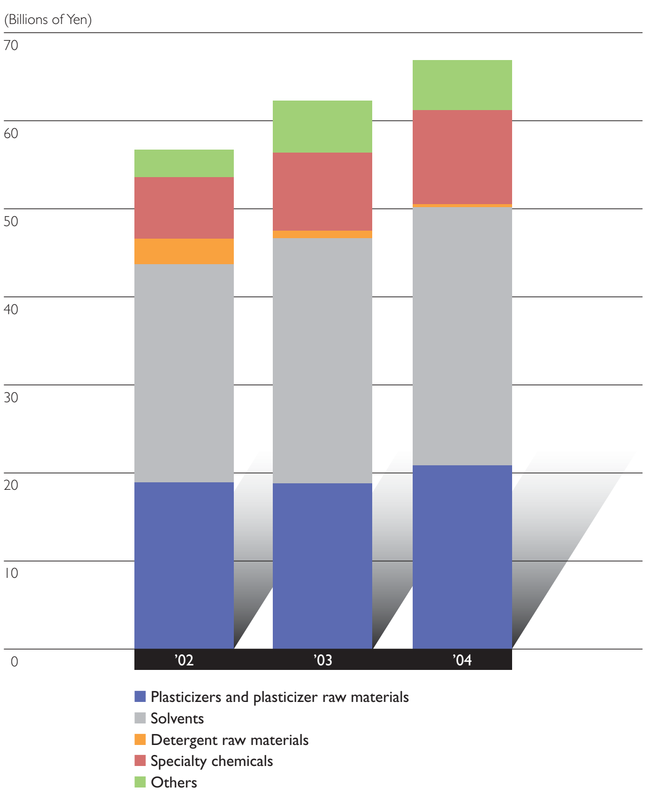
In feed-grade amino acids, the profitability of overseas subsidiaries improved due to better market conditions and increased sales volume. However, Kyowa Hakko decided to withdraw from the markets for feed-grade amino acids. In December 2003, we sold Fermentaciones Mexicanas, S.A. de C.V. (Fermex), of Mexico, to food company Safmex, of Mexico. And in May 2004, we concluded an agreement to sell Agroferm Hungarian-Japanese Fermentation Ltd. (Agroferm), of Hungary, to German chemical company Degussa AG.

Biokyowa Inc., located in Missouri, in the United States

Company President
Shoji Hari*
Executive Officer

C H E M I C A L S

Fiscal 2004 Sales Breakdown
(Nonconsolidated basis)



INDUSTRY OUTLOOK

The year under review began with a number of factors that made the operating environment unstable, such as the war in Iraq and the outbreak of SARS. However, in the end the effect of SARS was comparatively light, and overseas economies turned toward recovery, centered on China and the United States. As a result, conditions in the petrochemical industry were favorable overall. In particular, petrochemical companies in Japan operated at generally high levels due to expansion in exports, which were supported by continued economic growth in China, and to increased demand from the IT industry, where conditions were favorable. Currently, the petrochemical industry enjoys a firm product supply environment. In the future, highly competitive large-scale manufacturing facilities for ethylene and its derivative products will come on stream in the Middle and Near East as well as in China. As a result, the supply structure is expected to change significantly, and global competition to intensify further.

OPERATIONAL STRATEGY

In April 2004, Kyowa Yuka Co., Ltd., a production subsidiary of Kyowa Hakko, took over Kyowa Hakko's chemical operations and made a new start under the name of Kyowa Hakko Chemical Co., Ltd. Based on an integrated system—spanning research, development, production, and sales—that targets flexible operational development and market-cultivation-oriented sales, we will work to strengthen existing bulk operations and to expand our business in high-value-added functional products, such as environmentally friendly and IT-related products. We have steadily strengthened our business structure. In 2000, we integrated our plasticizer operations with those of Mitsubishi Chemical Corporation. Subsequently, we established Japan Ethyl Acetate Co., Ltd., an ethyl acetate production joint venture with Showa Denko K.K. that started operations in April 2004. Also, we are taking steps to reinforce our market position, such as further boosting sales of functional chemical products and new products. In China, where the market is growing rapidly, we established a representative office in Shanghai in March 2004, and in the future we will aggressively expand our operations in that market.

* *As of April 2004, Shoji Hari became the President and Chief Executive Officer of Kyowa Hakko Chemical Co., Ltd.*

China Coat Exhibition in Shanghai

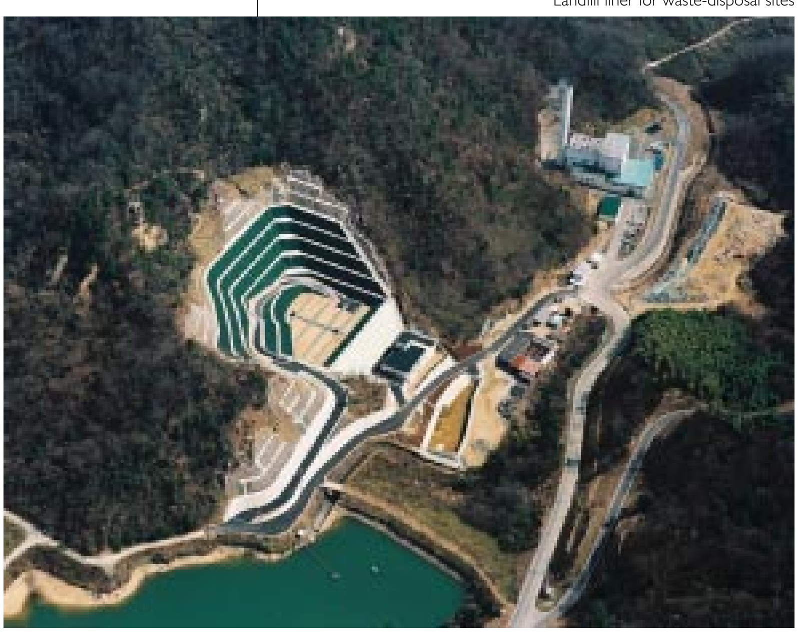
OVERVIEW

The Chemicals Company's net sales rose 2.7%, to ¥66.9 billion, due to growth in sales of solvents, which are basic chemicals, and functional chemical products. Operating income was up 163.0%, to ¥2.9 billion.

Basic Chemicals

In Japan, the sales volume of bulk products, principally solvents, increased. In addition, we revised prices of all products in line with higher raw materials costs. As a result, sales volume and value both rose. We worked to expand exports following the favorable conditions in overseas markets, but lower plant utilization rates stemming from raw material supply-side problems had a significant influence, and sales volume and value both declined.

Landfill liner for waste-disposal sites



To improve profitability and expand production capacity for ethyl acetate, a common solvent used in the ink and paint industries, we established Japan Ethyl Acetate, a joint venture with Showa Denko in August 2003. The company began operations in April 2004.

Specialty Chemicals

Higher sales of raw materials used in CFC substitutes and of refrigerator lubricant oil, which contribute to global environmental protection, and of squaric acid derivatives, which are raw materials for recording media, resulted in gains in sales of specialty chemicals in both volume and value.

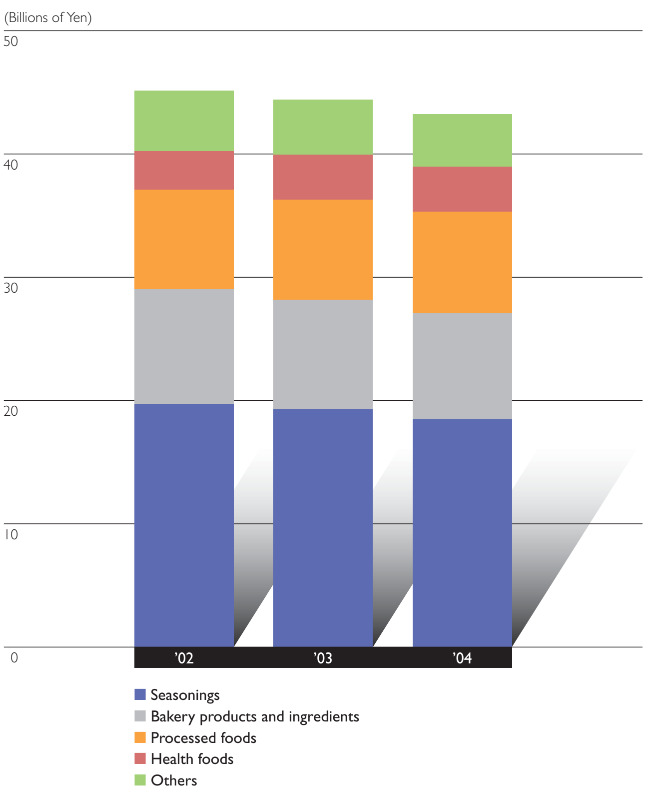
Distillation tower at the Yokkaichi Plant

High-purity solvents for the IT industry

Company President
Fumio Norimatsu
Executive Officer

FOOD*

Fiscal 2004 Sales Breakdown
(Nonconsolidated basis)



* *Following the transfer of alcoholic beverage operations in the previous term, the name of the Liquor and Food segment was changed to the Food segment from fiscal 2004.*

INDUSTRY OUTLOOK

In addition to the slump in consumer spending, food-related issues, such as BSE and the outbreak of avian influenza, have adversely affected the domestic processed food and food service industries. Except for convenience stores and growth companies, demand for seasonings and bakery products and ingredients has been flat.

Over the medium to long term, we expect steady growth in the processed food, take-out food, and food service industries. We also anticipate that demand for seasonings and bakery products and ingredients will focus not only on flavor but also increasingly on safety and price. The development of new products and the establishment of quality assurance systems are important issues for every food company.

OPERATIONAL STRATEGY

The Food Company considers its mission to be the provision of safe, high-quality products that contribute to improving the health and diets of consumers. We are developing food materials that will earn distinctive market positions by using our fermentation and other original technologies.

In the fields of natural seasonings and supplements and bakery products and ingredients, the Food Company will establish a new marketing system that unifies R&D and sales activities and strengthen its quality assurance system. On that basis, the Food Company will apply solution-based marketing to develop the markets for distinctive new products.

Overseas, we operate plants for the manufacture of natural seasonings and freeze-dried food materials in China. In addition to these production bases, we will bolster our marketing capabilities in China and other Asian countries and work to develop new markets.

OVERVIEW

Operating conditions remained challenging in the year under review, due to sluggish consumer spending as well as such problems as BSE and the outbreak of avian influenza, which especially affected food-related industries. In this setting, the Food Company worked to expand sales of core products and to launch new products; however, net sales declined 21.6% from the previous year, to ¥56.7 billion. This decrease was principally attributable to the sale of our alcoholic beverage operations to Asahi

Breweries, Ltd., in September 2002, and to the discontinuance of unprofitable products. Operating performance improved significantly, with operating income of ¥2.0 billion in the year under review, compared with an operating loss of ¥0.4 billion in the previous year.

Instant egg-drop freeze-dried soup

Remake GABA health food products

Sauces for Chinese foods with natural seasonings

Seasonings

In natural seasonings, sales of *Kokumi* seasonings and such newer products as Asep.-chicken increased. However, sales of certain other products were down, and total sales declined from the previous year. Sales volume of *Umami* seasonings decreased following the implementation of a strategy to improve profitability.

Bakery Products and Ingredients

Although sales of bread improvers and flavor enhancers increased, sales of yeast products and premixes decreased. Overall, sales of bakery products and ingredients were down from the previous year.

Processed Foods

Sales of freeze-dried soups were about level with the previous year, but sales of private-brand products increased. Overall sales of processed foods rose from the previous year.

Health Foods*

Sales of existing OEM products declined, and sales in this category were down from the previous year.

CSPHP, a soy protein/phospholipid complex system that is used as a cholesterol lowering food ingredient, was added by the U.S. FDA to the list of products generally recognized as safe (GRAS).

Raw Material Alcohol Division*

Sales of alcohol for the refined sake industry declined due to continued sluggish consumption of refined sake and to a trend toward the consumption of *shochu*. Sales of alcohol for *shochu* production and sales of industrial alcohol increased, and as a result the division recorded higher sales.

**Starting from the year ending March 2005, Health Foods and the Raw Material Alcohol operations have been transferred to the Bio-Chemicals segment.*

Newly completed second plant at Wuxi Xiehe Food in Wuxi, China

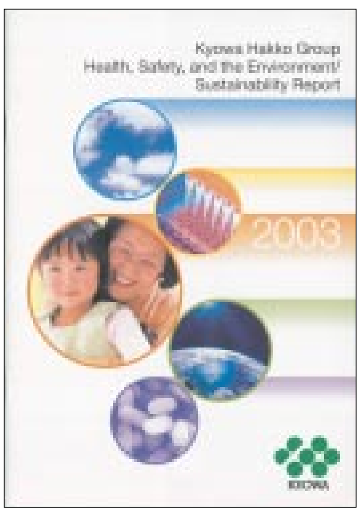
CORPORATE SOCIAL RESPONSIBILITIES

Environmental and Safety Issues

As outlined in its management policies, the Kyowa Hakko Group considers the environment, safety, and health to be among its most important management issues. The leadership of top management provides an example that is followed by everyone at Kyowa Hakko as they participate in responsible care (RC) practices, which encompass a wide range of environmental and safety-related activities.

Environment and Safety Management System

The Group's environment and safety management system, which incorporates the ISO 14001 management system and the Occupational Safety and Health Management System (OSHMS), utilizes the Plan, Do, Check, and Act (PDCA) cycle. We are aiming to steadily extend the application of this system to all our consolidated subsidiaries in the year ahead.



The 2004 version of this report will be available in September 2004.

Compliance

In environmental and safety-related activities, we strictly follow all relevant standards, including not only those set by national and municipal governments but also our own stricter standards. Compliance with these standards is monitored by Kyowa Hakko's Head Office. The Company is working to enhance accountability. Environment and safety information is included in our *Health, Safety, and the Environment/Sustainability Report,* and information from work sites is available on our web site.

However, in the previous fiscal year, subsidiary Kyowa Yuka Co., Ltd. (now, Kyowa Hakko Chemical), failed to meet the government standards for handling high-pressure gas, and as a result the operation of related facilities was temporarily halted. A range of measures to prevent a recurrence of such an incident have been implemented, and we are doing our utmost to restore trust as soon as possible.

Performance

In the fiscal year under review, we worked to reduce the environmental burden of our operations through Companywide activities, principally targeting reduced energy consumption, reduced resource use, and zero emissions. Due to measures to control the generation of industrial waste and waste recycling activities, the volume of waste disposal at landfill sites was down 50% from the previous year, and half of our plants achieved zero emissions. We have brought forward our 2007 target for Companywide zero emissions. Also, through energy-saving initiatives, we reduced energy consumption by the equivalent of 116,000 kiloliters of crude oil. Combined with measures to reduce resource usage, this had an economic effect of about ¥0.65 billion.

We worked to improve water quality by improving production processes and wastewater processing facilities, and we achieved a significant 39% reduction in the pollution burden. We also continue to implement detailed control and reduction measures for emissions of chemical substances.

Further, we are promoting green purchasing in our supply chain throughout the Group. In addition to green office plan activities, centered on administrative departments, we have introduced such evaluation methods as life cycle impact assessment, aiming to improve the quality of our activities.

In safety, we have maintained a top rank in the industry, with an accident rate* of 0.15 at Kyowa Hakko, Kyowa Yuka, and Kyowa Medex Co., Ltd. We also had no incidents of fires or leaks in the year under review.

**The number of occupational injury accidents resulting in worker absences and injuries per million man-hours of labor.*

Assessment

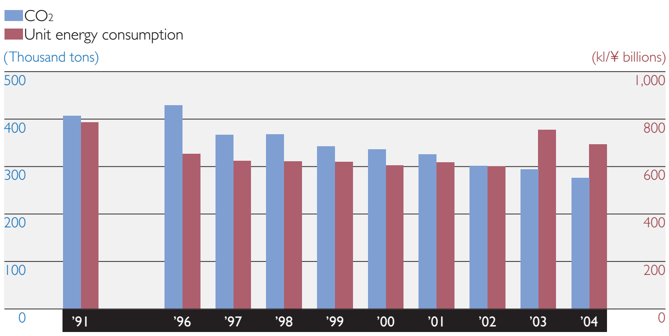
We are steadily implementing risk management. In new product and new technology development, we are taking steps to effectively use our safety and environmental assessment system.

R&D for Environmentally Friendly Products and Technologies

We are aggressively developing environmentally friendly products and technologies, including energy-saving technologies. In particular, we have achieved improvements in productivity through the development of bioprocesses that utilize

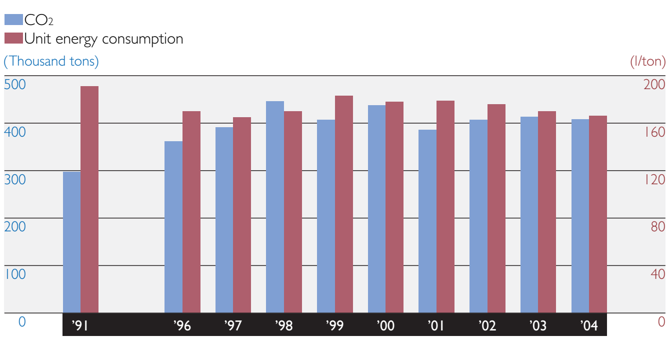
Yearly Changes in Unit Energy Consumption

*Kyowa Hakko, Kyowa Medex, Riken Kagaku, Kyowa F.D. Foods, Kyowa HiFoods, Ohland Foods, and Asahi Foods Products**



Yearly Changes in Unit Energy Consumption

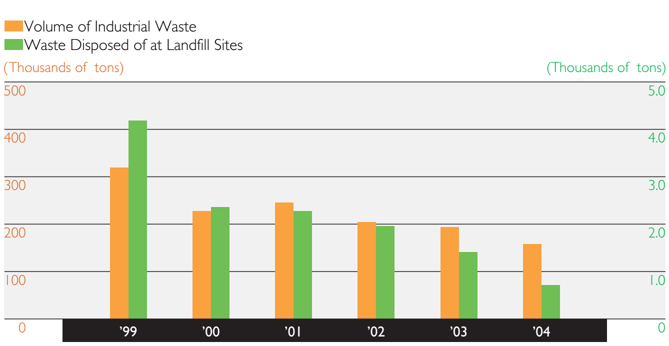
*Kyowa Yuka**



* *Energy consumption per unit of production is expressed on a crude-oil-conversion basis. It is not possible to make a uniform comparison of the amount of basic energy units used by Kyowa Hakko, Kyowa Medex, Riken Kagaku, Kyowa F.D. Foods, Kyowa HiFoods, Ohland Foods, and Asahi Foods Products, which engage in the small-volume production of pharmaceuticals and other products, and Kyowa Yuka, or Kyowa Hakko Chemical as of April 2004, which is involved in the production of chemical products. Therefore, the amounts of unit energy consumption by Kyowa Hakko, Kyowa Medex, Riken Kagaku, Kyowa F.D. Foods, Kyowa HiFoods, Ohland Foods, and Asahi Foods Products and by Kyowa Yuka are presented separately. Because the energy consumption of the alcoholic beverage operations was lower than the average energy consumption for the Company as a whole, the transfer had the effect of worsening the Company's energy consumption numbers.*

Yearly Changes in Volume of Industrial Waste

Kyowa Hakko, Kyowa Yuka, Kyowa Medex, Riken Kagaku, Kyowa F.D. Foods, Kyowa HiFoods, Ohland Foods, and Asahi Foods Products



microorganism genome information. We will continue to emphasize the development of manufacturing methods with low environmental burdens. We are working to make the results of our research available; for example, we disclose microoganism genome information on our web site. We are also implementing ISO 14001-based management in R&D divisions as one facet of our commitment to addressing environmental and safety-related issues from the R&D stage.

On a base of these activities, to increase the transparency of environmental and safety-related activities, including those of consolidated subsidiaries and affiliates, we will continue working to raise the quality of information disclosure.

Quality Assurance

Kyowa Hakko aims not only to provide products and services with quality superior to those from other companies but also to earn the satisfaction and trust of its customers. To raise customer satisfaction, we are working to build a framework extending across all departments—from R&D to production, distribution, and sales—that will enable us to more accurately understand customer needs and problems, to share and utilize customer information with related divisions in the Company, and to engage the entire Company in providing a rapid response to customers.

In regard to product safety, for pharmaceuticals, we conduct strict safety tests in accordance with the Pharmaceutical Affairs Law. For other products, we implement rigorous quality investigations at new product development meetings. In addition, when raw materials or production methods are changed, we confirm quality by conducting stringent product quality assessments.

Moreover, to further enhance quality assurance in products and services, we continue to improve our international standard quality assurance systems, such as GMP, ISO 9000s, and HACCP, at all plants in accordance with product attributes. We will also continue striving to bolster production control and quality control systems. We have already received ISO 9000s certification at the Hofu and Ube plants as well as at Kyowa Yuka's Chiba and Yokkaichi plants and at Kyowa Medex's Fuji Plant. And we are making progress toward the acquisition of ISO 9001 certification (2000 version).

Nonetheless, subsidiary Asahi Foods Products Co., Ltd., implemented a recall of a product in fiscal 2004. Measures to prevent a reoccurrence of this situation have been implemented, and preventive measures are being extended to other subsidiaries as well. In the future, we will continue working to further improve quality assurance throughout the Kyowa Hakko Group.

Corporate Citizenship

As a fundamental management policy, Kyowa Hakko takes measures to ensure that its management is open to society and to aggressively introduce international standards into its management practices. We work to communicate with local communities and, through corporate citizenship activities, to earn society's understanding and trust. To those ends, we implement a wide range of activities.

"Science for a Happier 21st Century" Essay Competition

In recent years, young people in Japan have grown increasingly distanced from science, and in response Kyowa Hakko has introduced a national science essay competition designed to encourage young people—who will play key roles in society in the 21st century—to think about and develop an interest in science.

For junior and senior high school students, the competition is based on the theme of "Science for a Happier 21st Century." The sixth annual competition will be held in 2004. Other sponsors and supporters include the Mainichi Newspapers Co. and the Ministry of Education, Culture, Sports, Science and Technology.

Mobile Science Experiment Classroom —BioAdventure

Kyowa Hakko offers a mobile science experiment classroom that supports science education, with the Company's researchers serving as instructors. Staff at the Tokyo Research Laboratories have installed microscopes and other experimental equipment onto a vehicle—BioAdventure—that is taken to elementary, junior high, and senior high schools. In addition, during school spring vacations we offer science laboratory classrooms at the Pharmaceutical Research Institute for local elementary school students and, during summer vacations, science classrooms at the Ube Plant for elementary and junior high school students.

Asahi Young Session

Every year since 1987, the Company has sponsored the Asahi Young Session, a lecture series that provides an opportunity for leaders from various fields to deliver inspirational messages to young people about the importance of having future directions, dreams, and hopes. Mr. Ken Sakamura, the University of Tokyo professor who created Japan's original TRON operating system, was invited for the 16th session in 2003. For those who were unable to attend the lecture, Mr. Sakamura's address is available in printed form. Other sponsors and supporters of the lecture series include Asahi Shimbun and the Ministry of Education, Culture, Sports, Science and Technology.

Kato Memorial Bioscience Foundation

The Kato Memorial Bioscience Foundation, established by Kyowa Hakko in honor of the Company's founder, Dr. Benzaburo Kato, provides financial support for researchers for innovative work in the basic fields of bioscience. The foundation also sponsors an annual public symposium.

CONTENTS

FINANCIAL SECTION

ELEVEN-YEAR SELECTED FINANCIAL DATA

KYOWA HAKKO KOGYO CO., LTD. and Its Consolidated Subsidiaries
For the years ended March 31, 2004, 2003, 2002, 2001, 2000, 1999, 1998 and 1997; the three-month period ended March 31, 1996; and the years ended December 31, 1995 and 1994

	2004	2003	2002	2001
For the Year:				
Net sales	**¥348,838**	¥359,285	¥378,668	¥375,610
Gross profit	**129,507**	126,328	128,744	123,945
Selling, general and administrative expenses	**102,671**	110,239	108,387	106,233
Operating income	**26,836**	16,089	20,357	17,712
Net income	**10,017**	8,485	5,535	9,395
Capital expenditures	**9,041**	11,791	11,454	17,092
Depreciation and amortization	**11,358**	14,768	17,819	18,502
R&D expenses	**29,206**	31,438	29,294	28,921
Cash Flows:				
Net cash provided by operating activities	**34,264**	18,193	16,955	28,789
Net cash provided by/(used in) investing activities	**10,477**	2,586	8,377	(1,991)
Net cash used in financing activities	**(44,226)**	(38,748)	(16,843)	(20,871)
Cash and cash equivalents at the end of the year	**24,911**	24,588	41,908	32,600
At Year-End:				
Current assets	**194,062**	195,878	244,410	237,852
Total assets	**361,096**	368,772	430,113	431,410
Current liabilities	**98,914**	95,046	162,508	169,821
Interest-bearing debt	**13,358**	51,969	74,354	87,624
Total shareholders' equity	**225,042**	219,047	211,652	194,692
Number of employees	**6,294**	6,749	7,299	7,766
Per Share Data:				
Net income—basic (Note 2)	**¥ 23.0**	¥ 19.4	¥ 12.7	¥ 21.6
Total shareholders' equity	**522.6**	505.4	487.5	448.3
Cash dividends	**7.5**	7.5	7.5	7.5
Common Stock Price Range (Per share)**:**				
High	**719**	780	899	1,225
Low	**495**	411	587	701
Stock Information (Thousands of shares)**:**				
Number of common stock issued	**434,244**	434,244	434,244	434,244
Weighted average number of common stock issued	**431,497**	433,748	434,244	434,244
Financial Ratios:				
Return on assets	**2.74**	2.12	1.28	2.17
Operating return on assets	**7.35**	4.03	4.73	4.09
Return on equity	**4.51**	3.94	2.72	4.82
Equity ratio	**62.32**	59.40	49.21	45.13
Debt/equity ratio	**5.94**	23.73	35.13	45.01

Notes: 1. U.S. dollar amounts are translated from Japanese yen, for convenience only, at the rate of ¥105.69=US$1, the approximate exchange rate at March 31, 2004.
2. Net income per share of common stock is based upon the weighted average number of shares of common stock outstanding during each year, appropriately adjusted for subsequent free distributions of common stock.
3. As a result of a change in the Company's fiscal year-end from December 31 to March 31, fiscal 1996 was the three-month period ended March 31, 1996.
4. Only nonconsolidated figures are available.

	Millions of Yen						Thousands of U.S. Dollars (Note 1)
2000	1999	1998	1997	1996 (Note 3)	1995	1994	**2004**
¥374,910	¥384,671	¥397,361	¥397,629	¥82,990	¥374,978	¥341,545	**$3,300,577**
126,872	127,864	144,191	144,248	31,645	149,050	130,853	**1,225,348**
105,216	104,407	109,448	110,320	24,959	105,425	98,302	**971,436**
21,656	23,457	34,743	33,928	6,686	43,625	32,551	**253,912**
11,274	6,143	13,528	12,339	1,296	15,615	10,646	**94,777**
21,053	24,408	24,555	19,132	4,317	11,428 (Note 4)	9,416 (Note 4)	**85,543**
19,153	17,673	17,113	16,701	3,926	10,341 (Note 4)	10,532 (Note 4)	**107,465**
25,888	24,083	25,358	22,882	5,026	20,658	18,949	**276,336**
32,737	—	—	—	—	—	—	**324,193**
23,422	—	—	—	—	—	—	**99,130**
(50,077)	—	—	—	—	—	—	**(418,450)**
26,215	—	—	—	—	—	—	**235,699**
223,353	270,499	235,697	236,337	228,298	241,871	230,148	**1,836,143**
433,958	477,729	437,271	431,774	418,956	432,500	408,977	**3,416,558**
158,542	211,376	181,554	182,648	175,389	186,209	178,734	**935,888**
102,870	151,489	98,282	97,786	98,195	99,656	102,924	**126,388**
195,039	185,766	188,645	180,391	174,294	174,943	158,857	**2,129,265**
7,866	5,044 (Note 4)	5,134 (Note 4)	5,174 (Note 4)	5,172 (Note 4)	5,298 (Note 4)	5,361 (Note 4)	
	Yen						U.S. Dollars (Note 1)
¥ 26.0	¥ 13.9	¥ 30.3	¥ 27.6	¥ 2.9	¥ 35.0	¥ 23.9	**$0.218**
449.1	427.8	422.6	404.2	390.5	391.9	355.9	**4.945**
10.0	7.5	7.5	7.5	1.9	7.5	7.0	**0.071**
1,581	694	888	1,080	1,030	1,010	1,050	**6.803**
610	485	492	720	914	799	905	**4.684**
434,244	434,244	446,343	446,343	446,343	446,343	446,343	
434,244	441,906	446,343	446,343	446,343	446,343	446,343	
	%						
2.47	1.34	3.11	2.90	0.30	3.71	2.64	
4.75	5.13	8.00	7.98	1.57	10.37	8.07	
5.92	3.28	7.33	6.96	0.74	9.36	6.86	
44.94	38.89	43.14	41.78	41.60	40.45	38.84	
52.74	81.55	52.10	54.21	56.34	56.96	64.79	

MANAGEMENT'S DISCUSSION AND ANALYSIS

Operating Environment and Business Performance

In fiscal 2004, ended March 31, 2004, there were signs of an economic recovery in Japan, centered on the corporate sector. However, there was also cause for concern, such as trends in the U.S. economy and exchange rate fluctuations, and the domestic economy did not completely break out of its lengthy deflationary phase.

Kyowa Hakko faced intensifying competition in its Pharmaceuticals operations, making the acceleration of overseas development activities and the cultivation of overseas markets increasingly important. In Bio-Chemicals operations, amino acids for beverages and other health foods and pharmaceutical ingredients enjoyed strong demand. In Chemicals operations, increased sales were recorded by functional chemical products due to the trend toward environmental conservation and the progress of the information society. Food operations benefited from growing concern with food safety and greater health consciousness, but conditions remained difficult, with consumption sluggish throughout the food products industry and prices trending downward.

In this business environment, the Kyowa Hakko Group worked to improve profitability through aggressive sales promotions and cost reduction measures and to develop new products. At the same time, we took steps to reform our operational structure. As a result, we recorded a gain in net income on a marginal decline in net sales.

Analysis of Profit and Loss

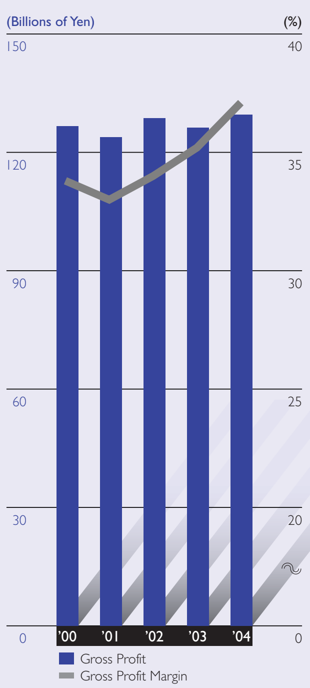
Sales

In the year under review, the Company's consolidated net sales declined 2.9%, to ¥348.8 billion. Higher sales were recorded in the Pharmaceuticals operations, where sales of Allelock®, an antiallergic agent, and Durotep® Patch, an analgesic for persistent cancer pain, increased. Sales growth was also registered in Chemicals operations, where demand was favorable for solvents and functional chemical products, principally in the domestic market. However, the September 2002 transfer of alcoholic beverage operations had a substantial effect on sales in the year under review.

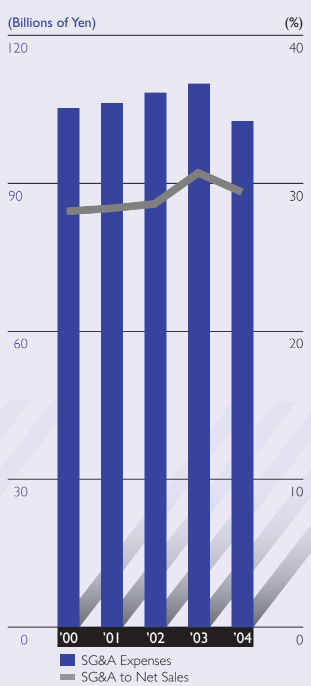
Cost of Sales and SG&A Expenses

The cost of sales was down 5.8%, to ¥219.3 billion. This decline was attributable to cost reductions, such as the rationalization of amino acid production in Bio-Chemicals operations, and to the transfer of alcoholic beverage operations. Gross profit rose 2.5%, to ¥129.5 billion. Selling, general and administrative (SG&A) expenses were down 6.9%, to ¥102.7 billion. One reason for this decrease was the transfer of alcoholic

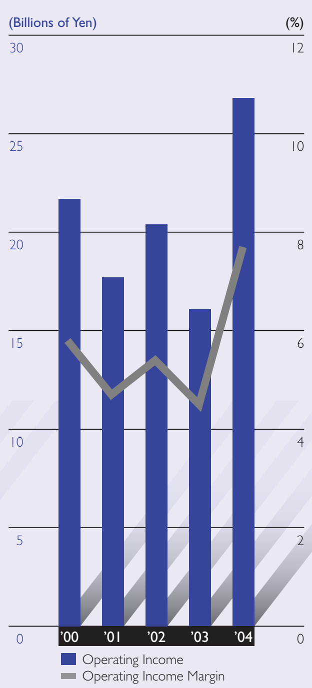
Gross Profit



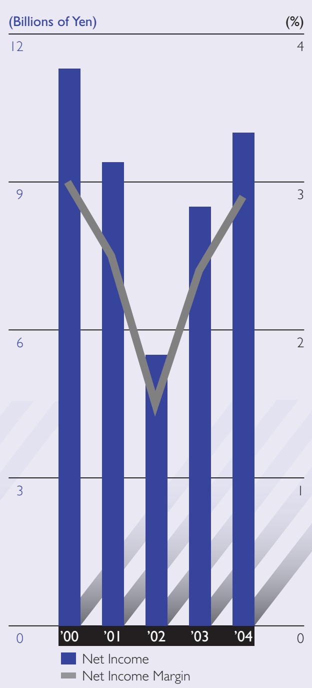
SG&A Expenses



Operating Income



Net Income



beverage operations, which resulted in lower labor and distribution costs. Another reason was a decrease of ¥1.9 billion in retirement benefits expense, which was principally attributable to the Company's receipt in the previous fiscal year of approval of an exemption from the obligation to pay for benefits related to future services under the substitutional portion of the pension fund.

Operating Income

Operating income was up 66.8%, to ¥26.8 billion. A significant factor in this increase was the progress of restructuring initiatives in Bio-Chemicals and Other operations. The operating income margin rose 3.2 percentage points, to 7.7%.

Other Revenue (Expenses)

Net other expenses were ¥11.5 billion, compared with net other revenue of ¥0.9 billion in the previous year. Gain on sale of investments in securities with limited relationship to operations and gain on sale of property, plant and equipment contributed to other revenue of ¥18.7 billion.

On the other hand, accompanying the dissolution of the retirement benefit trust, the Company recorded as other expense the entire amount of the unrecognized actuarial differences associated with cancellation of the Company's retirement benefit trust contract. Also, in accordance with its plans to move to an operating holding company system in the year ending March 2006, the Company decided to dispose of certain fixed assets, for which disposal expenses were recorded. Further, there was a loss associated with compensation for a product that was recalled by subsidiary Asahi Foods Products Co., Ltd., because it was contaminated with a foreign substance. Other expenses totaled ¥28.6 billion.

As a result, income before income taxes and minority interests declined 9.5%, to ¥15.4 billion.

Income Taxes

Current and deferred income taxes totaled ¥5.5 billion, a decline of ¥3.0 billion from the previous year's level of ¥8.5 billion. The effective tax rate was 35.9%, down from 49.9% in the previous year. The decline in income taxes was attributable to an increase in tax credits due to the application of research and development tax benefits.

Net Income

Net income was up 18.1%, to ¥10.0 billion. Return on equity was 4.5%, an increase of 0.6 percentage points from 3.9% in the previous year.

Performance by Segment

Sales, operating expenses, and operating income (loss) for each

	Millions of Yen						Thousands of U.S. Dollars (Note 1)
	2004	2003	2002	2001	2000	1999	**2004**
Sales by Industry Segment:							
Pharmaceuticals	**¥142,866**	¥140,594	¥142,297	¥141,450	¥142,338	¥143,216	**$1,351,745**
Bio-Chemicals	**58,968**	58,525	55,496	52,720	47,657	53,617	**557,934**
Chemicals	**66,899**	65,158	60,410	60,659	63,893	66,359	**632,974**
Food[2]	**56,703**	72,322	103,531	103,353	106,320	107,428	**536,503**
Other	**63,168**	63,485	59,777	57,627	55,166	54,330	**597,672**
Corporate, elimination and other	**(39,766)**	(40,799)	(42,843)	(40,199)	(40,464)	(40,279)	**(376,251)**
Total	**¥348,838**	¥359,285	¥378,668	¥375,610	¥374,910	¥384,671	**$3,300,577**
Operating Income (Loss) by Industry Segment:							
Pharmaceuticals	**¥11,908**	¥11,014	¥18,959	¥19,574	¥23,799	¥25,618	**$112,668**
Bio-Chemicals	**8,492**	1,975	1,268	(1,191)	(2,096)	2,635	**80,348**
Chemicals	**2,893**	1,100	(1,174)	(2,684)	(1,064)	(4,264)	**27,373**
Food[2]	**2,001**	(368)	(440)	919	(1,110)	(2,430)	**18,933**
Other	**1,781**	2,597	1,756	1,141	1,390	1,719	**16,851**
Corporate, elimination and other	**(239)**	(229)	(12)	(47)	737	179	**(2,261)**
Total	**¥26,836**	¥16,089	¥20,357	¥17,712	¥21,656	¥23,457	**$253,912**

Notes: 1. U.S. dollar amounts are translated from Japanese yen, for convenience only, at the rate of ¥105.69=US$1, the approximate exchange rate at March 31, 2004.
2. Due to the transfer of alcoholic beverage operations in September 2002, the name of the Liquor and Food segment was changed to the Food segment from the year ended March 31, 2004.

Kyowa Hakko business segment are outlined below. The figures include inter-segment transactions.

Pharmaceuticals

Sales in the Pharmaceuticals Segment, Kyowa Hakko's core line of business, increased 1.6% from the previous year, to ¥142.9 billion, accounting for 36.8% of total sales. Operating expenses rose 1.1%, to ¥131.0 billion, and operating income was up 8.1%, to ¥11.9 billion.

Bio-Chemicals

Sales in the Bio-Chemicals Segment increased 0.8% from the previous year, to ¥59.0 billion, accounting for 15.2% of total sales. Operating expenses declined 10.7%, to ¥50.5 billion, and operating income grew 330.0%, to ¥8.5 billion.

Chemicals

Sales in the Chemicals Segment increased 2.7% from the previous year, to ¥66.9 billion, accounting for 17.2% of total sales. Operating expenses edged down 0.1%, to ¥64.0 billion, and operating income was up 163.0%, to ¥2.9 billion.

Food

Sales in the Food Segment decreased 21.6%, to ¥56.7 billion. This decline was attributable to the September 2002 transfer of the Company's alcoholic beverage operations, excluding *mirin* sweet sake seasoning, because alcoholic beverage sales up to the date of the transfer were included in the previous year's figure. This segment accounted for 14.6% of total sales. Operating expenses were down 24.7%, to ¥54.7 billion, and operating income was ¥2.0 billion, compared with an operating loss of ¥0.4 billion in the previous year.

Other

Sales in the Other Segment declined 0.5%, to ¥63.2 billion, accounting for 16.2% of total sales. Kyowa Hakko's other businesses include the operations of subsidiaries engaged in transportation, warehousing, and sales of industrial apparatus. Operating expenses increased 0.8%, to ¥61.4 billion, and operating income was down 31.4%, to ¥1.8 billion.

Cash Flows

Net cash provided by operating activities in fiscal 2004 amounted to ¥34.3 billion, a rise of ¥16.1 billion from the previous fiscal year. Income before income taxes and minority interests declined ¥1.6 billion, and, the net result of changes in trade receivables, inventories, and trade payables was an inflow of ¥3.8 billion, ¥9.9 billion less than in the previous year. On the other hand, noncash outflows, such as increases in reserve for retirement benefits and reserve for loss on disposal of fixed assets had a significant influence. Also, income taxes paid declined ¥14.7 billion, from ¥16.7 billion in the previous year to ¥1.9 billion in the year under review.

Net cash provided by investing activities was ¥10.5 billion, an increase of ¥7.9 billion from the previous year. Proceeds from transfer of alcoholic beverage operations of ¥13.1 billion were recorded in the previous year, and their absence in the year under review had the effect of decreasing inflows. Items that had the effect of increasing inflows included a ¥13.0 billion rise in proceeds from sale of investments in securities, a ¥5.0 billion decrease in acquisition of investments in securities, and a ¥3.6 billion decline in acquisition of property, plant and equipment.

Net cash used in financing activities was ¥44.2 billion, an increase of ¥5.5 billion. Dividends paid were ¥3.2 billion, about the same level as in the previous year. Net proceeds from short-term debt declined ¥7.0 billion, and two items recorded in the previous year—redemption of convertible bond of ¥10.0 billion and payment of employees' savings deposits for transferring to bank of ¥13.4 billion—were not recorded in the year under review. In accordance with a debt assumption agreement, ¥33.7 billion was entrusted to fund principal and interest payments for the 15th, 16th, and 17th unsecured bond issues. Also, acquisition of treasury stock rose ¥1.4 billion from the previous year.

Cash and cash equivalents at fiscal year-end edged up ¥0.3 billion, from ¥24.6 billion at the previous year-end to ¥24.9 billion at the end of the year under review. This increase was attributable to the items outlined above and to the effect of exchange rate fluctuations on the cash and cash equivalents of overseas subsidiaries.

Uses of Funds

The Company's principal uses of funds are purchases of raw materials and other items for the manufacture of products, production expenses, and SG&A expenses. Major operating expenses are labor costs, R&D expenses, and sales promotion expenses. Also, the Kyowa Hakko Group implements ongoing capital investment with such goals as the enhancement of production facilities, rationalization, the implementation of environmental measures, and the promotion of R&D.

In regard to funds required for payments of principal and interest on bonds, due to the conclusion of the debt assumption agreement (effective early redemption), sufficient funds have been entrusted for payments of interest and principal. The interest burden associated with interest-bearing debt other than bonds represents a low percentage of outflows, and the balance of interest-bearing debt is at a level where the influence of a rise in interest rates would be limited.

Financial Position

At the end of fiscal 2004, total current assets were ¥194.1 billion, a decrease of 0.9% from the previous year-end. Total assets were down 2.1%, to ¥361.1 billion.

Total current liabilities rose 4.1%, to ¥98.9 billion at fiscal year-end. Short-term borrowings declined, but income taxes payable increased.

Bonds and other long-term debt at year-end were down ¥34.0 billion, to ¥0.1 billion, due to early redemption accompanying the debt assumption agreement in October 2003 for ¥33.0 billion in bonds.

Reserve for retirement benefits increased ¥16.2 billion because, accompanying the dissolution of the retirement benefit trust, the Company recorded as other expense the entire amount of the unrecognized actuarial differences associated with cancellation of the retirement benefit trust contract.

As a result, interest-bearing debt was down 74.3% from the previous year-end, to ¥13.4 billion, less than 10% of the level of ¥151.5 billion recorded five years ago at the end of March 1999. The debt/equity ratio[1] declined substantially, from 23.7% at the previous fiscal year-end to 5.9% at the end of the year under review.

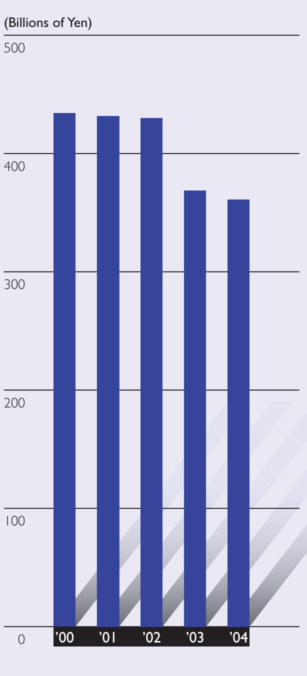
Total shareholders' equity rose 2.7% from the previous year-end, to ¥225.0 billion, due primarily to an increase of ¥6.7 billion in retained earnings. With the equity ratio rising to 62.3%, from 59.4% at the end of the previous year, the Company further strengthened its stability.

Management Indices

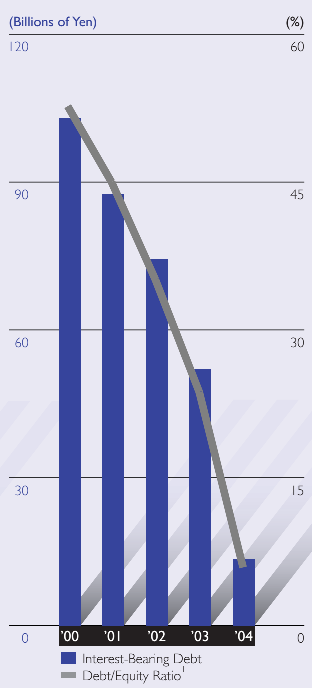
Profitability

Return on equity (ROE) increased to 4.51%, from 3.94% in the previous fiscal year, and return on assets (ROA) rose to 2.74%, from 2.12%. However, operating return on assets was 7.35%, a significant increase from 4.03% in the previous year. Under our Eighth Medium-Term Management Plan, we have set an operating return on assets target of 8.0%. We are working to further reduce interest-bearing debt, to streamline our balance sheet, and to establish a profit-generating structure, and we are approaching that target. EBITDA[2] was ¥27.5 billion in the year under review, a decrease of 17.7% from the previous year.

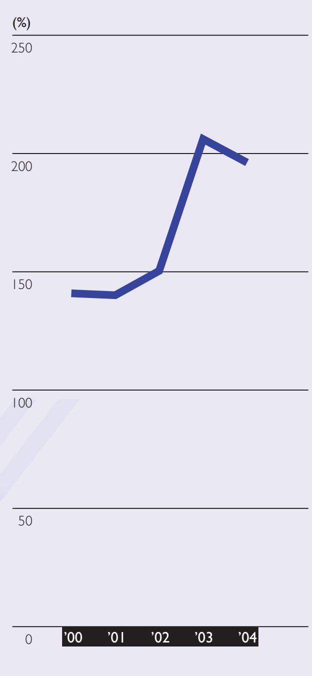
Total Assets



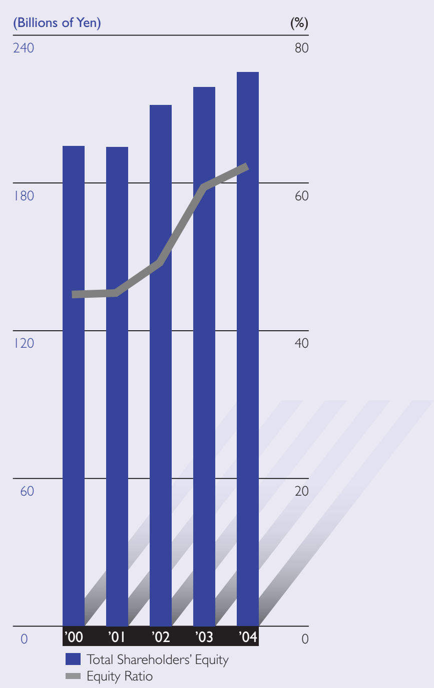
Interest-Bearing Debt



Current Ratio



Total Shareholders' Equity



Note 1: Debt/equity ratio = Interest-bearing debt (short-term borrowings + current portion of long-term debt + long-term debt) / total shareholders' equity

Per Share Data

In the fiscal year under review, net income per share was ¥23.0, up from ¥19.4 in the previous year. Total shareholders' equity per share increased from ¥505.4 to ¥522.6. Cash dividends per share for fiscal 2004 were unchanged at ¥7.5, comprising interim and year-end per-share dividends of ¥3.75 each.

Other Important Items

Statement on the Fine Imposed by the European Commission

On June 7, 2000, the Company and Kyowa Hakko Europe GmbH ("KHEG") had a fine of 13,200 thousand Euro imposed on them by a Decision of the European Commission with allegations that the Company and KHEG had violated EU competition law due to their involvement in a cartel for the sale of amino acid lysine within the EEA (European Economic Area) prior to June 1995. On August 25, 2000, the Company and KHEG lodged an appeal to the Court of First Instance of the European Communities with regard to the amount of the fine. On July 9, 2003, the court handed down its decision that the fine imposed by the European Commission was appropriate. The Company has accepted this decision and has paid the fine and interest. The loss of ¥1.9 billion was recorded as other expense.

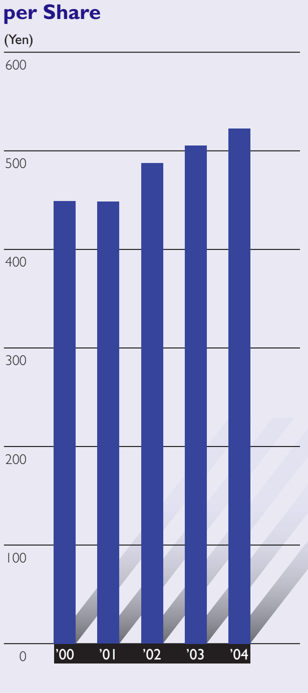
Capital Expenditures

The Kyowa Hakko Group is investing continuously with the

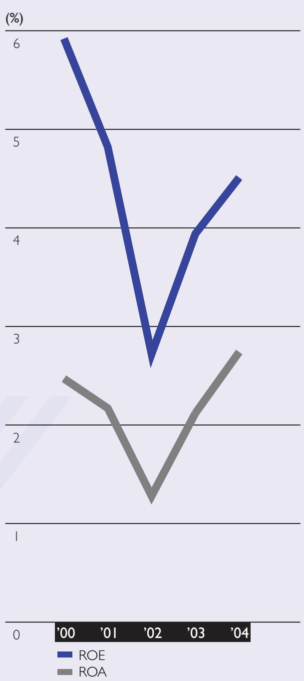
Billions of Yen

	Capital Expenditures			Depreciation and Amortization		
	2004	2003	2002	**2004**	2003	2002
Pharmaceuticals	**¥3.6**	¥ 4.2	¥ 4.5	**¥ 4.5**	¥ 5.1	¥ 5.4
Bio-Chemicals	**1.7**	3.7	2.6	**2.7**	3.9	4.9
Chemicals	**1.8**	2.2	1.7	**2.7**	3.6	4.1
Food	**1.9**	1.4	2.2	**1.1**	1.7	2.9
Other	**0.1**	0.1	0.2	**0.1**	0.1	0.1
Corporate, elimination and other	**(0.0)**	0.3	0.2	**0.2**	0.4	0.4
Total	**¥9.0**	¥11.8	¥11.5	**¥11.4**	¥14.8	¥17.8

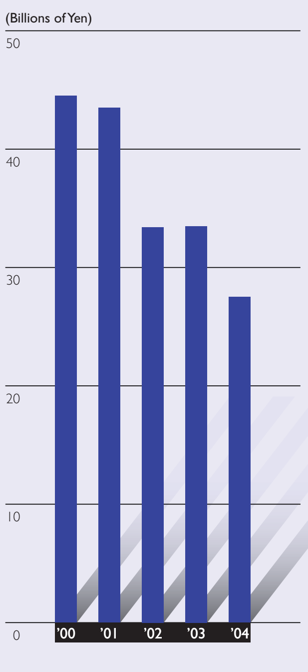
Total Shareholders' Equity per Share



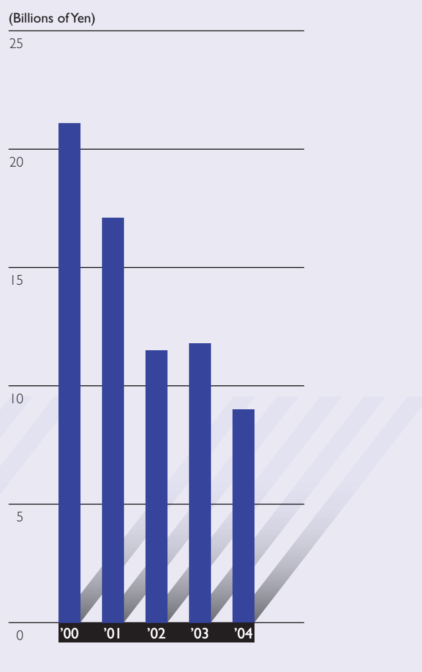
ROE and ROA



EBITDA[2]



Capital Expenditures



Note 2: EBITDA = Income before income taxes and minority interests + interest expenses + depreciation and amortization

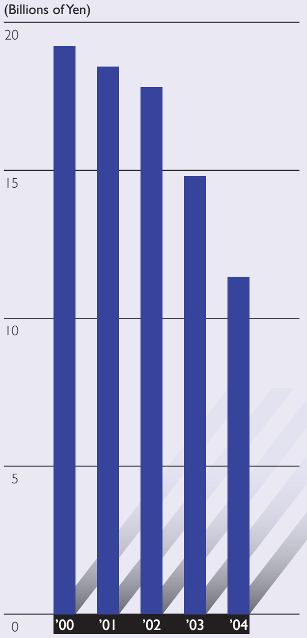
goals of enhancing and rationalizing production facilities and promoting R&D activities. Capital expenditures during fiscal 2004 decreased 23.3% from the previous fiscal year, to ¥9.0 billion, and depreciation and amortization declined 23.1%, to ¥11.4 billion. Accordingly, capital expenditures remained within the range of depreciation and amortization and we were able to fund those expenditures internally.

Retirement Benefit Obligations

At the end of the year under review, projected pension benefit obligations totaled ¥70.1 billion at a discount rate of 2.5%, the same rate as in the previous year. The market value of pension fund assets at year-end was ¥26.6 billion, resulting in unfunded pension benefit obligations of ¥43.6 billion. Subtracting the unrecognized actuarial differences of ¥10.4 billion and adding the unrecognized prior service costs of ¥0.6 billion leaves ¥33.8 billion, which was recorded in the consolidated balance sheets as reserve for retirement benefits. The unrecognized actuarial differences will be amortized over a 10-year period starting from the following year using the straight-line method. The unrecognized prior service costs will be amortized over a 5-year period starting from the point at which they arose using the straight-line method.

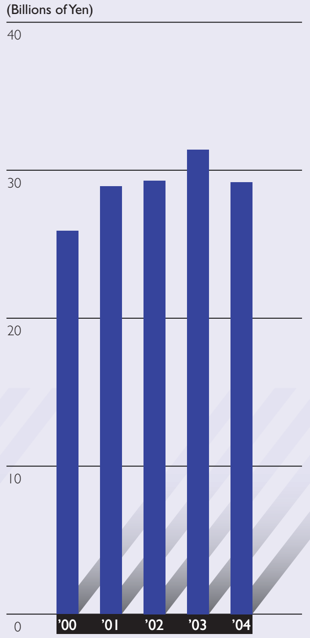
Depreciation and Amortization

(Billions of Yen)



R&D Expenses

(Billions of Yen)



Retirement Benefit Expense

Expected return on plan assets (calculated at 2.8%) of ¥0.6 billion and amortization of unrecognized prior service costs of ¥0.3 billion were subtracted from the total of service cost of ¥2.8 billion, interest cost of ¥1.8 billion, and amortization of unrecognized actuarial differences of ¥3.0 billion. To this was added special severance payment of ¥1.6 billion, for a sum of ¥8.3 billion. Accompanying the cancellation of the retirement benefit trust contract, the Company recorded as other expense the entire amount of the unrecognized actuarial differences associated with cancellation of the trust contract—¥16.2 billion—resulting in a total of ¥24.5 billion in retirement benefit expense for the year under review.

R&D Expenses

R&D expenses, which are included in production expenses and in selling, general and administrative expenses, declined 7.1% from the previous fiscal year, to ¥29.2 billion, or 8.4% of consolidated net sales. R&D expenses in Pharmaceuticals amounted to ¥24.7 billion, accounting for 84.6% of total R&D expenses and 17.2% of Pharmaceuticals Segment sales.

Ability to Raise Funds

Kyowa Hakko plays the central role in securing a low-cost stable supply of funds to support the operational activities of the Group.

The Company maintains a short-term rating sufficient to meet demand for short-term funds, and the Company can raise short-term funds through the flexible issuance of domestic commercial paper. Also, the Company works to improve its financial position and boost its creditworthiness while considering its funding situation.

Acquisition of Treasury Stock

Out of the upper limit of 20 million shares of treasury stock set at the general shareholders' meeting held on June 27, 2003, the Company acquired 2.6 million shares at a cost of ¥1.7 billion. As a result of careful consideration of trends in funds and the stock price, 87% of the limit on treasury stock acquisition has not been exercised. Also, to facilitate the execution of a more flexible capital policy, the provisions for acquisition of treasury stock were changed at the general meeting of shareholders held on June 29, 2004, to make it possible for treasury stock to be acquired through a decision of the board of directors.

RISK FACTORS

Operating Risks

In regard to the Kyowa Hakko Group's management performance and financial position, the major risks that could have a significant influence on the judgment of investors include, but are not limited to, those outlined below.

Matters in this section dealing with the future represent the judgment of the Kyowa Hakko Group as of the end of the fiscal year under review, March 31, 2004.

Political, Economic, and Social Risks

1. Risk associated with the operating environment in the domestic pharmaceutical industry

In the Group's core Pharmaceuticals operations, under the domestic public drug price system, when drug prices are revised the selling prices for the majority of drugs are generally reduced. The Group's management performance and financial position could be adversely affected by such revisions.

Also, as a result of such factors as future trends in health care system reforms targeting control of health care spending, intensified competition following the entrance into the domestic market of foreign companies, and a decline in the relative position of the Group in the domestic industry due to integration and reorganization in the pharmaceutical industry, the Group's management performance and financial position could be adversely affected.

2. Risk of declines in product sales prices due to fluctuations in the balance of supply and demand

The Group's products include those for which market conditions are significantly affected by the global balance of supply and demand, such as, in Chemicals, solvents, plasticizers, and raw materials for plasticizers. Declines in the sales prices of these products could adversely affect the Group's management performance and financial position.

3. Risk of declines in profitability due to significant crude oil price fluctuations

The primary raw materials for the products of the Group's Chemicals operations include ethylene and propylene, which are made from naptha, which is refined from crude oil. The prices of those raw materials are significantly affected by fluctuations in crude oil prices, which could adversely affect the Group's management performance and financial position.

4. Potential risk in overseas operational activities

The Group's overseas operations are subject to inherent risks, such as unforeseeable laws and regulations, unfavorable changes to the tax system, unfavorable political or economic developments, difficulty in employing people, and social disorder caused by terrorism, war, or other factors, that could adversely affect the Group's management performance and financial position.

Management Risks

1. Risk that substantial R&D investment will not be recovered

The Group conducts substantial R&D investment in the development of new products and technologies, including the development of new drugs; in the improvement of existing products; and in the development of new applications for existing products. Various factors could result in those efforts being unsuccessful, which could worsen the Group's future growth potential and profitability and could adversely affect the Group's management performance and financial position.

2. Risk from failure of capital investment

When the Group considers investment profitability and determines that an investment will be effective, substantial capital investment may be made for such purposes as manufacturing new products or increasing production capacity for existing products. If actual results differ from assumptions, the amount of the capital investment might not be recovered as planned, and the Group's management performance and financial position could be adversely affected.

3. Retirement benefit system risks

The Group's retirement benefit obligations and retirement allowance expenses are calculated in accordance with actuarially determined assumptions, such as discount rate, retirement rate, and salary increase rate assumptions. If actual results differ from assumptions or if assumptions must be changed, or if system changes are implemented, such as changes to benefit levels, the Group's management performance and financial position could be adversely affected.

Kyowa Hakko and certain subsidiaries have defined benefit pension plans. If the pension plan finances worsen in the future due to stock price declines or if there are changes to the system, such as salary level changes, it could become necessary for the Company to provide supplementary funds, which could have an adverse influence on the Group's cash flows.

4. Deferred tax asset recovery risk

The amount of deferred tax assets in the Group's consolidated balance sheets is based on a judgment as to the likelihood of recovery in accordance with estimates of the future taxable income of Kyowa Hakko and consolidated subsidiaries. If it is determined that a portion or all of the deferred tax assets of a company are not recoverable, the Group's deferred tax assets will be reduced, and the Group's management performance and financial position could be adversely affected.

5. Product defect risks

At plants in countries where the Group has operations, all types of products are manufactured in accordance with quality control standards accepted in that country. In the event of a product defect that leads to a major product recall or compensatory payments, the Group's reliability could be significantly affected, and the Group's management performance and financial position could be adversely affected.

6. Legal regulation risks

The Group emphasizes compliance to ensure that it does not violate the laws to which it is subject in the course of carrying out its operations in Japan and overseas. The Group is working to bolster internal control functions through such means as administrative oversight. If, because the Group is unable to observe these legal regulations, new product development is delayed or stopped, or manufacturing or sales activities are restricted, the Group's reliability could be damaged, and the Group's management performance and financial position could be adversely affected.

Also, in the future, if the legal regulations that must be observed in Japan and overseas change, the resulting situation could affect the Group's operations and the Group's management performance and financial position could be adversely affected.

7. Risk of lawsuits

The Group is working to establish an effective compliance system, but in regard to the execution of its operational activities in Japan and overseas, the Group or related parties might be sued for a number of reasons. The fact that a lawsuit has been filed and its result could affect the reliability of the Group, and the Group's management performance and financial position could be adversely affected.

8. Intellectual property risks

The basic strategy of the Group's management calls for the creation of new products and new technologies through R&D. The Group is working to accumulate technologies that differentiate it from other companies, to acquire intellectual property, and to strengthen its information management system. If the Group is unable to appropriately maintain and control intellectual property, its market competitiveness could be adversely affected.

In addition, a warning or lawsuit claiming that the Group's products or technologies are violating the intellectual property rights of another party could adversely affect the Group's operational activities, management performance, and financial position.

9. Risk of failure of tie-ups with other companies

To make the most appropriate use of management resources in its operations, the Group conducts joint operational activities with many other companies and external research institutions, such as technological tie-ups and joint ventures, the outsourcing of production, joint research, and the outsourcing of research. However, in the future, in the event that the tie-up relationship is not successful, which could happen for a number of reasons, such as the dissolution of the tie-up relationship, the Group's management performance and financial position could be adversely affected.

10. Influence on production activities from strengthened environment-related regulations

Fermentation waste liquid that is generated in production processes for fermented products, such as amino acids, is handled and emitted in accordance with the environment-related laws of the country where the manufacturing activities are conducted. In the future, measures to strengthen environment-related regulations could lead to restrictions on production activities and increases in production costs, and the Group's management performance and financial position could be adversely affected.

Disaster- and Accident-Related Risks

1. Influence of disasters and accidents

The Group conducts periodic disaster prevention tests and facility maintenance for all of its facilities in order to minimize the adverse influence on operations of such events as the stoppage of production lines. In the event of an accident or disaster, which could occur for a number of reasons, the reliability of the Group and the Group's management performance and financial position could be adversely affected.

2. Risk of the spread of infectious diseases

In regions where the Group has operations, including overseas, in the event of social disorder due to expansion in infectious disease damage, such as from SARS (severe acute respiratory syndrome) or avian influenza, the Group's operational activities could be curtailed. Also, in the Group's food operations, raw material procurement could be curtailed, and sales of products using raw materials from birds could be adversely affected. As a result, the Group's management performance and financial position could be adversely affected.

CONSOLIDATED BALANCE SHEETS

KYOWA HAKKO KOGYO CO., LTD. and Its Consolidated Subsidiaries
As at March 31, 2004 and 2003

ASSETS	Millions of Yen 2004	Millions of Yen 2003	Thousands of U.S. Dollars (Note 4) 2004
Current Assets:			
Cash	**¥ 24,301**	¥ 17,611	**$ 229,927**
Time deposits	**939**	7,539	**8,884**
Accounts and notes receivable:			
Trade	**100,290**	101,569	**948,907**
Unconsolidated subsidiaries and affiliates	**7,919**	8,588	**74,927**
Other	**1,685**	2,961	**15,943**
	109,894	113,118	**1,039,777**
Inventories	**50,495**	51,573	**477,765**
Deferred tax assets (Note 8)	**6,529**	3,877	**61,775**
Other current assets	**2,067**	2,373	**19,557**
Less: allowance for doubtful accounts	**(163)**	(213)	**(1,542)**
Total current assets	**194,062**	195,878	**1,836,143**
Investments and Advances:			
Investments in securities (Note 5)	**43,192**	43,668	**408,667**
Investments in and advances to unconsolidated subsidiaries and affiliates (Note 5)	**18,501**	18,000	**175,050**
Long-term loans to employees, mostly for housing	**48**	75	**454**
Long-term loans and other investments	**6,235**	6,688	**58,993**
Less: reserve for write-down of investments in securities	**(206)**	(170)	**(1,949)**
Less: allowance for doubtful accounts	**(797)**	(968)	**(7,541)**
	66,973	67,293	**633,674**
Property, Plant and Equipment (Note 7)**:**			
Buildings and structures	**122,937**	128,018	**1,163,185**
Machinery and equipment	**211,303**	236,118	**1,999,271**
	334,240	364,136	**3,162,456**
Less: accumulated depreciation	**(261,410)**	(285,205)	**(2,473,365)**
	72,830	78,931	**689,091**
Land	**21,820**	21,663	**206,453**
Construction in progress	**2,035**	1,502	**19,254**
	96,685	102,096	**914,798**
Deferred Tax Assets (Note 8)	**1,957**	1,459	**18,516**
Other Assets	**1,419**	2,046	**13,427**
	¥ 361,096	¥ 368,772	**$ 3,416,558**

The accompanying notes are an integral part of the statements.

LIABILITIES AND SHAREHOLDERS' EQUITY

	Millions of Yen 2004	Millions of Yen 2003	Thousands of U.S. Dollars (Note 4) 2004
Current Liabilities:			
Short-term borrowings (Note 6)	**¥ 13,232**	¥ 17,891	**$125,196**
Accounts and notes payable:			
Trade (Note 5)	**44,744**	41,918	**423,351**
Unconsolidated subsidiaries and affiliates	**3,625**	4,499	**34,298**
Construction and acquisition of properties	**1,393**	2,133	**13,180**
Other	**13,507**	14,812	**127,799**
	63,269	63,362	**598,628**
Income taxes payable	**8,767**	2,135	**82,950**
Reserve for accrued sales returns	**94**	124	**889**
Reserve for accrued sales rebates	**956**	932	**9,045**
Reserve for accrued sales promotion expenses	**796**	530	**7,531**
Reserve for loss on disposal of fixed assets	**1,157**	—	**10,947**
Guarantee deposits from customers	**8,226**	7,948	**77,831**
Other current liabilities	**2,417**	2,124	**22,871**
Total current liabilities	**98,914**	95,046	**935,888**
Long-Term Debt (Note 6)	**126**	34,078	**1,192**
Deferred Tax Liabilities (Note 8)	**86**	330	**814**
Reserve for Retirement Benefits:			
Employees (Note 9)	**33,769**	17,601	**319,510**
Directors and corporate auditors	**781**	813	**7,390**
Reserve for loss on disposal of fixed assets	**669**	—	**6,330**
Other Non-Current Liabilities	**321**	406	**3,037**
Minority Interests in Consolidated Subsidiaries	**1,388**	1,451	**13,132**
Commitments and Contingent Liabilities (Notes 7 and 12)			
Shareholders' Equity:			
Common stock:			
Authorized: 987,900,000 shares at March 31, 2004 and 2003			
Issued: 434,243,555 shares at March 31, 2004 and 2003	**26,745**	26,745	**253,051**
Additional paid-in capital	**43,182**	43,180	**408,572**
Retained earnings (Note 17)	**144,927**	138,226	**1,371,246**
	214,854	208,151	**2,032,869**
Unrealized Gains on Available-for-Sale Securities (Note 5)	**14,637**	13,485	**138,490**
Translation Adjustments	**(2,136)**	(2,051)	**(20,209)**
Treasury Stock, at cost, 3,826,534 shares at March 31, 2004	**(2,313)**	(538)	**(21,885)**
Total shareholders' equity	**225,042**	219,047	**2,129,265**
	¥361,096	¥368,772	**$3,416,558**

CONSOLIDATED STATEMENTS OF INCOME

KYOWA HAKKO KOGYO CO., LTD. and Its Consolidated Subsidiaries
For the years ended March 31, 2004, 2003 and 2002

	Millions of Yen			Thousands of U.S. Dollars (Note 4)
	2004	2003	2002	**2004**
Net Sales (Note 15)	**¥348,838**	¥359,285	¥378,668	**$3,300,577**
Cost of Sales (Notes 7, 9 and 13)	**219,331**	232,957	249,924	**2,075,229**
Gross profit	**129,507**	126,328	128,744	**1,225,348**
Selling, General and Administrative Expenses (Notes 7, 9 and 11)	**102,671**	110,239	108,387	**971,436**
Operating income (Note 15)	**26,836**	16,089	20,357	**253,912**
Other Revenue (Expenses):				
Interest and dividend income	**781**	778	827	**7,390**
Interest expenses	**(804)**	(1,717)	(3,114)	**(7,607)**
Write-down of investments in securities	**(18)**	(306)	(119)	**(170)**
Gain on sale of investments in securities	**12,978**	1,688	12,726	**122,793**
Foreign exchange (loss) gain	**(1,309)**	(2,350)	916	**(12,385)**
Insurance premium received	**405**	340	458	**3,832**
Gain on sale of property, plant and equipment	**3,959**	3,489	1,819	**37,459**
Equity in earnings of affiliates	**552**	221	1,223	**5,223**
Loss on restructuring of certain subsidiaries and affiliates (Note 11)	**(843)**	(6,047)	(21,081)	**(7,976)**
Arising from the lump-sum recognition of the previous years' unrecognized actuarial differences associated with cancellation of the Company's retirement benefit trust contract	**(16,227)**	—	—	**(153,534)**
Loss on disposal of fixed assets relevant to organizational restructuring (Note 11)	**(3,225)**	—	—	**(30,514)**
Loss on recalling products	**(2,086)**	—	—	**(19,737)**
Administrative fines in a cartel for sales of amino lysine within European Economic Area (Note 11)	**(1,901)**	—	—	**(17,987)**
Expenses on support for employees' early retirement	**(1,464)**	—	—	**(13,852)**
Loss on redemption of bond	**(681)**	—	—	**(6,443)**
Gain on the transfer of the alcoholic beverage operations (Note 11)	**—**	3,247	—	**—**
Gain on the transfer of the substitutional portion of contributory pension plan (Note 9)	**—**	2,873	—	**—**
Other, net	**(1,576)**	(1,312)	(1,550)	**(14,912)**
	(11,459)	904	(7,895)	**(108,420)**
Income before income taxes and minority interests	**15,377**	16,993	12,462	**145,492**
Income Taxes (Note 8):				
Current	**9,463**	3,227	16,514	**89,535**
Deferred	**(3,936)**	5,253	(9,525)	**(37,240)**
	5,527	8,480	6,989	**52,295**
	9,850	8,513	5,473	**93,197**
Minority Interests in Losses (Earnings) of Consolidated Subsidiaries	**167**	(28)	62	**1,580**
Net income	**¥ 10,017**	¥ 8,485	¥ 5,535	**$ 94,777**

	Yen			U.S. Dollars (Note 4)
Per Share Data (Note 16):				
Net income—basic	**¥23.0**	¥19.4	¥12.7	**$0.218**
Net income—diluted (*)	**—**	—	—	**—**
Cash dividends	**7.5**	7.5	7.5	**0.071**
Weighted Average Number of Shares (Thousands of shares)	**431,497**	433,748	434,244	

** 1. Diluted net income per share for fiscal 2002 is not disclosed because there were anti-dilutive effects.*
2. Diluted net income per share for fiscal 2004 and 2003 is not disclosed because there were no residual securities.

The accompanying notes are an integral part of the statements.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

KYOWA HAKKO KOGYO CO., LTD. and Its Consolidated Subsidiaries
For the years ended March 31, 2004, 2003 and 2002

	Number of shares of common stock (thousands)	Millions of Yen		
		Common stock	Additional paid-in capital	Retained earnings
Balance at March 31, 2001	434,244	¥26,745	¥43,180	¥129,694
Net income for the year ended March 31, 2002	—	—	—	5,535
Cash dividends	—	—	—	(1,628)
Directors' and corporate auditors' bonuses	—	—	—	(80)
Interim cash dividends	—	—	—	(1,628)
Increase due to application of inflation accounting to the accounts of Mexican subsidiary	—	—	—	6
Other	—	—	—	(2)
Balance at March 31, 2002	434,244	26,745	43,180	131,897
Net income for the year ended March 31, 2003	—	—	—	8,485
Cash dividends	—	—	—	(1,627)
Directors' and corporate auditors' bonuses	—	—	—	(75)
Interim cash dividends	—	—	—	(1,628)
Increase due to application of inflation accounting to the accounts of Mexican subsidiary	—	—	—	119
Increase due to additional unconsolidated subsidiaries	—	—	—	1,018
Increase due to merger	—	—	—	39
Other	—	—	—	(2)
Balance at March 31, 2003	434,244	26,745	43,180	138,226
Net income for the year ended March 31, 2004	**—**	**—**	**—**	**10,017**
Cash dividends	**—**	**—**	**—**	**(1,615)**
Directors' and corporate auditors' bonuses	**—**	**—**	**—**	**(82)**
Interim cash dividends	**—**	**—**	**—**	**(1,625)**
Increase due to application of inflation accounting to the accounts of Mexican subsidiary	**—**	**—**	**—**	**6**
Gain on sale of treasury stock	**—**	**—**	**2**	**—**
Balance at March 31, 2004	**434,244**	**¥26,745**	**¥43,182**	**¥144,927**

	Number of shares of common stock (thousands)	Thousands of U.S. Dollars (Note 4)		
		Common stock	Additional paid-in capital	Retained earnings
Balance at March 31, 2003	434,244	$253,051	$408,553	$1,307,844
Net income for the year ended March 31, 2004	**—**	**—**	**—**	**94,777**
Cash dividends	**—**	**—**	**—**	**(15,281)**
Directors' and corporate auditors' bonuses	**—**	**—**	**—**	**(776)**
Interim cash dividends	**—**	**—**	**—**	**(15,375)**
Increase due to application of inflation accounting to the accounts of Mexican subsidiary	**—**	**—**	**—**	**57**
Gain on sale of treasury stock	**—**	**—**	**19**	**—**
Balance at March 31, 2004	**434,244**	**$253,051**	**$408,572**	**$1,371,246**

The accompanying notes are an integral part of the statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

KYOWA HAKKO KOGYO CO., LTD. and Its Consolidated Subsidiaries
For the years ended March 31, 2004, 2003 and 2002

	Millions of Yen			Thousands of U.S. Dollars (Note 4)
	2004	2003	2002	**2004**
Cash Flows from Operating Activities:				
Income before income taxes and minority interests	**¥ 15,377**	¥ 16,993	¥ 12,462	**$ 145,492**
Adjustments to reconcile income before income taxes and minority interests to net cash provided by operating activities:				
Depreciation and amortization	**11,358**	14,768	17,819	**107,465**
Equity in earnings of affiliates	**(552)**	(221)	(1,223)	**(5,223)**
Write-down of investments in securities	**18**	306	119	**170**
Increase in reserve for retirement benefits	**16,408**	1,212	766	**155,246**
Increase in reserve for loss on disposal of fixed assets	**1,826**	—	—	**17,277**
(Decrease) Increase in reserve for retirement benefits to directors and corporate auditors	**(32)**	27	(152)	**(303)**
(Increase)Decrease in allowance for doubtful accounts	**(153)**	(470)	3	**(1,448)**
Gain on sale of securities	**(12,978)**	(1,687)	(12,726)	**(122,793)**
Gain on disposal of property, plant and equipment	**(2,432)**	(2,748)	(1,335)	**(23,011)**
Gain on the transfer of the alcoholic beverage operations	**—**	(3,247)	—	**—**
Loss on restructuring of certain subsidiaries and affiliates	**843**	6,047	21,081	**7,976**
Loss on recalling products	**2,086**	—	—	**19,737**
Administrative fines in a cartel for sales of amino lysine within European Economic Area	**1,901**	—	—	**17,987**
Expenses on support for employees' early retirement	**1,464**	—	—	**13,852**
Loss on redemption of bond	**681**	—	—	**6,443**
Interest and dividend income	**(781)**	(778)	(827)	**(7,390)**
Interest expenses	**804**	1,717	3,114	**7,607**
Decrease in trade receivables	**1,792**	15,895	2,843	**16,955**
Decrease (Increase) in inventories	**407**	4,184	(477)	**3,851**
Increase (Decrease) in trade payables	**1,554**	(6,466)	(8,081)	**14,703**
Payment of bonuses to directors and corporate auditors	**(90)**	(81)	(86)	**(852)**
(Decrease) Increase in consumption tax payables	**(182)**	(1,060)	302	**(1,722)**
Others	**1,019**	(8,467)	(2,218)	**9,644**
	40,338	35,924	31,384	**381,663**
Interest and dividend received	**833**	815	1,058	**7,882**
Interest expenses paid	**(1,080)**	(1,878)	(3,241)	**(10,219)**
Payment for administrative fines in a cartel for sales of amino lysine within European Economic Area	**(2,074)**	—	—	**(19,623)**
Compensation payment incurred in connection with recalling products	**(359)**	—	—	**(3,397)**
Payment of expenses on support for employees' early retirement	**(1,454)**	—	—	**(13,757)**
Income taxes paid	**(1,940)**	(16,668)	(12,246)	**(18,356)**
Net cash provided by operating activities	**34,264**	18,193	16,955	**324,193**
Cash Flows of Investing Activities:				
Increase in time deposits	**(399)**	(436)	(434)	**(3,775)**
Decrease in time deposits	**633**	456	564	**5,989**
Acquisition of property, plant and equipment	**(9,202)**	(12,783)	(11,831)	**(87,066)**
Proceeds from sale of property, plant and equipment	**4,714**	4,151	2,785	**44,602**
Acquisition of investments in securities	**(227)**	(5,256)	(1,349)	**(2,148)**
Proceeds from sale of investments in securities	**15,613**	2,573	18,798	**147,724**
Proceeds from sale of investment in consolidated subsidiary	**(521)**	—	—	**(4,930)**
Additional investments in consolidated subsidiaries	**—**	—	(1,096)	**—**
Net decrease in short-term loans receivable	**113**	767	799	**1,069**
Increase in long-term loans receivable	**(238)**	(82)	(185)	**(2,252)**
Decrease in long-term loans receivable	**320**	1,101	339	**3,028**
Proceeds from transfer of alcoholic beverage operations	**—**	13,073	—	**—**
Others	**(329)**	(978)	(13)	**(3,111)**
Net cash provided by/(used in) investing activities	**10,477**	2,586	8,377	**99,130**
Cash Flows of Financing Activities:				
Net proceeds from short-term debt	**(4,006)**	(11,036)	(13,106)	**(37,904)**
Proceeds from long-term debt	**—**	—	150	**—**
Repayment of long-term debt	**(1,514)**	(568)	(570)	**(14,325)**
Redemption of bond (Note 6, 14)	**(33,681)**	—	—	**(318,677)**
Redemption of convertible bond	**—**	(9,997)	—	**—**
Payment of employees' savings deposits for transferring to bank	**—**	(13,449)	—	**—**
Acquisition of treasury stock	**(1,790)**	(437)	(116)	**(16,936)**
Proceeds from sale of treasury stock	**17**	—	63	**161**
Dividends paid	**(3,243)**	(3,250)	(3,251)	**(30,684)**
Dividends paid to minority	**(9)**	(10)	(11)	**(85)**
Others	**—**	(1)	(2)	**—**
Net cash used in financing activities	**(44,226)**	(38,748)	(16,843)	**(418,450)**
Effect of Exchanges on Cash and Cash Equivalents	**(192)**	731	819	**(1,817)**
Increase (Decrease) in Cash and Cash Equivalents	**323**	(17,238)	9,308	**3,056**
Cash and Cash Equivalents at the Beginning of the Year	**24,588**	41,908	32,600	**232,643**
Decrease in Cash and Cash Equivalents Due to Deconsolidation of Subsidiary	**—**	(127)	—	**—**
Increase in Cash and Cash Equivalents Due to Merger	**—**	45	—	**—**
Cash and Cash Equivalents at the End of the Year	**¥ 24,911**	¥ 24,588	¥ 41,908	**$ 235,699**

Relation between cash and cash equivalents at year-end and the account booked in the balance sheets

	Millions of Yen			Thousands of U.S. Dollars (Note 4)
	2004	2003	2002	**2004**
Cash and time deposits	**¥25,240**	¥25,150	¥38,903	**$238,811**
Time deposits whose maturity periods exceed three months	**(329)**	(562)	(341)	**(3,112)**
Investments in accounts receivable securitization	**—**	—	3,346	**—**
	¥24,911	¥24,588	¥41,908	**$235,699**

The accompanying notes are an integral part of the statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

KYOWA HAKKO KOGYO CO., LTD. and Its Consolidated Subsidiaries
For the years ended March 31, 2004, 2003 and 2002

1. BASIS OF PRESENTING CONSOLIDATED FINANCIAL STATEMENTS

The accompanying consolidated financial statements have been prepared from accounts and records maintained by KYOWA HAKKO KOGYO CO., LTD. (the "Company") and its consolidated subsidiaries (hereinafter referred to in total as the "Companies"). The Company and its domestic consolidated subsidiaries have maintained 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 generally accepted accounting principles and practices prevailing in Japan, which are different in certain respects as to application and disclosure requirements from International Financial Reporting Standards.

Certain items presented in the consolidated financial statements submitted to the Director of Kanto Finance Bureau in Japan have been reclassified for the convenience of readers outside Japan.

The Company's fiscal year is from April 1 to March 31. Therefore, "fiscal 2004" begins on April 1, 2003 and ends on March 31, 2004.

2. ACCOUNTING CHANGE

(1) Treasury Stock and Reduction of Legal Reserves

Effective from fiscal 2003, the Company and its domestic consolidated subsidiaries adopted the Financial Accounting Standards No. 1 "Financial Accounting Standards for Treasury Stock and Reduction of Legal Reserves." As a result of adoption of the new regulation, there was no effect on the operating results for fiscal 2003.

(2) Per Share Information

Effective from fiscal 2003, the Company and its domestic consolidated subsidiaries adopted the Financial Accounting Standards No. 2 "Financial Accounting Standards for Earnings per Share" and the Financial Accounting Standards Implementation Guidance No. 4 "Implementation Guidance for Accounting Standards for Earnings per Share". See Note 16 for the effect of this accounting change.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(1) Principles of Consolidation

The Company had 47 subsidiaries as at March 31, 2004 (49 as at March 31, 2003). The consolidated financial statements include the accounts of the Company and 23 subsidiaries in fiscal 2004 (24 for fiscal 2003).

Effective from October 1, 2003, Fermentaciones Mexicanas, S.A. de C.V. (incorporated in Mexico and hereinafter referred to as "Fermex") was excluded from consolidation, as the Company transferred all of its holding shares in December 2003.

Major subsidiaries are listed on the next page.

The remaining 24 (25 as at March 31, 2003) subsidiaries, whose combined total assets, net sales, net income and retained earnings are not significant in relation to those of the consolidated financial statements of the Companies, have been excluded from consolidation.

The accounts of 8 (9 as at March 31, 2003) overseas consolidated subsidiaries, Biokyowa Inc., Kyowa Hakko U.S.A., Inc., and Kyowa America, Inc. (all incorporated in the U.S.A.), Kyowa Hakko Europe GmbH (incorporated in Germany), Agroferm Hungarian-Japanese Fermentation Industry Ltd. (incorporated in Hungary and referred to as "Agroferm"), Kyowa Hakko (H.K.) Co., Ltd. and Kyowa Foods (H.K.) Co., Ltd. (incorporated in China) and Kyowa Italiana Farmaceutici S.R.L. (incorporated in Italy), are based on their accounting records maintained in conformity with generally accepted accounting principles and practices prevailing in their respective countries. Although certain differences exist in the accounting principles adopted by the overseas subsidiaries, essentially no adjustments have been made to their accounts in order to conform to Japanese accounting principles in the accompanying consolidated financial statements, as allowed under accounting principles and practices generally accepted in Japan.

The accounts of Fermex are based on inflation accounting as generally accepted in Mexico. Such inflation accounting includes the revaluation of fixed assets and the restatement of shareholders' equity adjusted by the National Consumer Price Index growth factor and the recognition of the effect of inflation on monetary assets and liabilities.

Financial statements of all overseas subsidiaries are prepared on a calendar year basis. For all domestic consolidated subsidiaries, they adopt a March 31 fiscal year-end basis.

Significant transactions that occurred between January 1 and March 31 are reflected in the accompanying consolidated financial statements.

Name of company	Direct and indirect equity ownership percentage	Capital stock (Millions)
Domestic subsidiaries:		
Kyowa Yuka Co., Ltd.	100.0%	¥5,300
Kyowa Medex Co., Ltd.	100.0	450
Kyowa F.D. Foods Co., Ltd.	100.0	275
Miyako Kagaku Co., Ltd.	52.9	111
Chiyoda Kaihatsu Co., Ltd.	100.0	113
Overseas subsidiaries:		
Biokyowa Inc. (U.S.A.)	100.0	$20
Agroferm Hungarian-Japanese Fermentation Industry Ltd. (Hungary)	100.0	HuF 3,506
Kyowa Hakko U.S.A., Inc. (U.S.A)	100.0	$1
Kyowa Hakko Europe GmbH (Germany)	100.0	EURO 1
Kyowa America, Inc. (U.S.A.)	100.0	$53

Any difference between the cost of an investment in a subsidiary and the amount of underlying equity in net assets of the subsidiary, if any at the date of establishment of control, has been amortized using a method which the Company determined based on the specific circumstances of each consolidated subsidiary.

All assets and liabilities of consolidated subsidiaries are revalued to fair market value as of the date of establishment of the control.

(2) Accounting for Investments in Unconsolidated Subsidiaries and Affiliates

The Company had 24 (25 at March 31, 2003) unconsolidated subsidiaries and 23 (25 at March 31, 2003) affiliates. The equity method is applied to the investments in 6 (6 at March 31, 2003) major domestic affiliates since the investments in the remaining unconsolidated subsidiaries and affiliates would not have had a material effect on the consolidated financial statements.

The 6 affiliates are accounted for using the equity method. The most significant affiliate is as follows:

Name of company	Equity ownership percentage	Capital stock (Millions of Yen)
J-PLUS Co., Ltd.	50.0%	¥480

Differences, arising from application of the equity method to unconsolidated subsidiaries and affiliates, between the cost of the investment and the amount of the underlying equity in net assets are fully amortized in the year when incurred.

The investments in the remaining unconsolidated subsidiaries and affiliates are stated at cost or less.

(3) Inventories Valuation

Inventories are valued at cost, cost being determined mainly by using the average cost method.

(4) Securities Valuation

Held-to-maturity debt securities are valued at amortized or accumulated cost.

Available-for-sale securities, for which market value is available, are valued at fair market value prevailing at the fiscal year-end.

Available-for-sale securities, for which market value is not available, are valued at cost, cost being determined by the moving average method.

Where fair market value has declined by more than 30%, which is deemed to be "significantly declined in value", the Company measures the recoverability of each security and recognizes a subsequent loss on write-down, if necessary.

See Note 5.

(5) Property, Plant and Equipment

Depreciation is computed mainly using the declining-balance method.

The Company and its domestic consolidated subsidiaries compute depreciation expense for buildings (other than related equipment and leasehold improvements) acquired on and after April 1, 1998 using the straight-line method.

The range of useful lives are principally as follows:

Buildings and structures:	15-50 years
Machinery and equipment:	4-15 years

(Additional Information)
Effective from April 1, 2003, the Company and certain of its subsidiaries changed method, from the group depreciation method to the individual calculation for each asset, using declining-balance method. This change is due to the introduction of a new management system for fixed assets.

Compared to the conventional method, operating income increased by ¥1,119 million ($10,588 thousand) and income before income taxes and minority interests increased by ¥1,139 million ($10,777 thousand).

The impact on segment information as a result of this change is described in detail in the segment information section.

See Note 15.

(6) Reserves and Allowances

Allowance for Doubtful Accounts
An allowance for doubtful accounts is made against potential losses on collection at an amount measured using a historical bad debt ratio, plus an amount individually measured on collectibility of receivables that are expected to be uncollectible due to bad financial condition or insolvency.

Reserve for Accrued Sales Returns
A reserve for accrued sales returns is provided on the basis of the maximum amount deductible under Japanese income tax laws. The amount of the reserve is determined based on the past years' experience of the Companies.

Reserve for Accrued Sales Rebates
A reserve for accrued sales rebates is provided at an amount determined based on the balance of receivables for pharmaceutical products from the sales agents and distributors at the year-end and the estimated rebate rates to be applied under the agreements.

Reserve for Accrued Sales Promotion Expenses
A reserve for accrued sales promotion expenses is provided at an amount equivalent to probable sales promotion expenses related to pharmaceutical inventories held by distributors. The amount of the reserve is determined based on the balance of inventories at year-end and the Companies' past experience ratio for such expenses.

Reserve for Write-Down of Investments in Securities
A reserve for the write-down of investments in securities is measured on the basis of the financial positions of the investees, such as subsidiaries and other investments, and provided for any decline in value of those investments.

Reserve for Retirement Benefits to Employees
A reserve for retirement benefits to employees is provided at an amount equal to the present value of the projected benefit obligation less fair value of the plan assets at the year-end.

Unrecognized prior service costs are amortized on a straight-line basis over five years from the year they occur.

Unrecognized actuarial differences are amortized on a straight-line basis over ten years from the year after they occur.

(Additional Information)
For the fiscal 2004, the Company cancelled its corporate pension trust contract on September 25, 2003, with the approval of the trust administrator, beneficiary (our employees and the employee's pension fund) and trustee (trust bank), and contributed to unfunded pension cost in connection with the welfare pension fund.

The Company fully amortized unrecognized actuarial losses associated with the cancellation of the corporate pension trust and accounted for other expense of ¥16,227million ($153,534 thousand).

For the fiscal 2003, following the enactment of the Welfare Pension Insurance Law in Japan, on March 1, 2003, the KYOWA HAKKO KOGYO CO., LTD. Group contributory pension plan obtained approval from Japan's Ministry of Health, Labour and Welfare for exemption from the future benefit obligation with respect to the portion of the contributory pension plan that the Company and its domestic subsidiaries operate on behalf of the Government (the so-called substitutional portion).

The Company and certain of its domestic consolidated subsidiaries applied transitional provisions as prescribed in paragraph 47-2 of the "Practical Guidelines of Accounting for Retirement Benefits (Interim Report)" (Accounting Committee Report No. 13 issued by the Japanese Institute of Certified Public Accountants) and the settlement of the substitutional portion was recognized at the date of approval from Japan's Ministry of Health, Labour and Welfare.

See Note 9 for the effect of this accounting.

Reserve for Retirement Benefits to Directors and Corporate Auditors
A reserve for retirement benefits to directors, including executive directors, and corporate auditors is provided in accordance with the Company's bylaws.

Reserve for loss on disposal of fixed assets
Reserve for loss on disposal of fixed assets is provided through establishment of an operating holding company, the Company comprehensively examined utilization of fixed assets after an organizational restructuring, and determined the disposal of certain fixed assets, and estimated the related loss.

(7) Foreign Currency Translation

All monetary assets and liabilities of the Company and its domestic consolidated subsidiaries denominated in foreign currencies are translated into yen at the spot rate prevailing at the year-end. Resulting translation gains or losses are charged or credited to income.

Assets and liabilities of overseas subsidiaries are translated into yen at the spot rate prevailing at the respective year-end of overseas subsidiaries, while income and expenses are translated at the annual average rate. Resulting translation adjustments are included in "shareholders' equity".

(8) Accounting for Leases

Leases that transfer substantially all the risks and rewards of ownership of the assets are accounted for as capital leases, except that leases do not transfer ownership of the assets at the end of the lease term are accounted for as operating leases, in accordance with accounting principles and practices generally accepted in Japan.

See Note 7.

(9) Accounting for Hedging

Gains or losses arising from changes in the fair value of the derivatives designated as "hedging instruments" are deferred as an asset or liability and included in net income for the same year during which the gains or losses on the hedged items or transactions are recognized. However, certain foreign currency receivables and payables covered by forward exchange contracts are translated at the contract rate, if applicable.

The derivatives designated as hedging instruments by the Companies are principally currency swap and forward exchange contracts for receivables/payables denominated in foreign currency.

The Companies have a policy to utilize the above hedging instruments in order to reduce the Companies' risk of fluctuation in interest and exchange rates. Therefore, the Companies' purchase of the hedging instruments are limited to, at maximum, the amounts of the hedged items.

The Companies evaluate the effectiveness of its hedging activities by reference to the accumulated gains or losses on the hedging instruments and the related hedged items from the commencement of the hedges.

See Note 10.

(10) Income Taxes

Income taxes of the Company and its domestic consolidated subsidiaries consist of corporate income taxes, local inhabitant taxes and enterprise taxes.

Income taxes are determined using the asset and liability method, where deferred tax assets and liabilities are recognized for temporary differences between the tax basis of assets and liabilities and their reported amount in the financial statements.

See Note 8 for details of deferred tax assets/liabilities.

(11) Cash and Cash Equivalents

Cash and cash equivalents in the consolidated statements of cash flows are comprised of cash on hand, bank deposits, which are able to be withdrawn on demand at any time, and short-term investments with an original maturity of three months or less, which are readily convertible into cash and considered to represent a low risk of market price fluctuation.

(12) Accounting for Consumption Taxes

In Japan, consumption taxes are imposed at a flat rate of 5 percent on all domestic consumption of goods and services, with certain exemptions. Consumption taxes imposed on the Companies' domestic sales to customers are withheld by the Companies at the time of sale and are paid to the national government and the local public body subsequently. The consumption tax withheld upon sale and the consumption tax paid by the Company and its domestic consolidated subsidiaries on the purchases of goods and services are not included in the related amounts in the accompanying consolidated statements of income.

(13) Appropriation of Retained Earnings

Under the Japanese Commercial Code and the Articles of Incorporation of the Company, the plan for appropriation of retained earnings (including cash dividend payments) proposed by the Board of Directors should be approved at the shareholders' meeting, which must be held within three months after the end of each fiscal year. The appropriation charged to retained earnings, as reflected in the accompanying consolidated statements of shareholders' equity, represents that applicable to the immediately preceding fiscal year that was approved at the shareholders' meeting and disposed of during the year.

As is customary in Japan, the payment of bonuses to directors and corporate auditors is made out of retained earnings instead of being charged to income for the year, which constitutes a part of the appropriation mentioned above.

(14) Net Income and Dividends per Share

Net income per share of common stock is based upon the weighted average number of shares of common stock outstanding, exclusive of treasury stock, during each year. Cash dividends per share represent dividends declared as applicable to the respective period.

(15) Reclassification

Certain fiscal 2003 and 2002 figures are reclassified to conform to the current year representation.

4. UNITED STATES DOLLAR AMOUNTS

The consolidated financial statements are prepared in Japanese yen. The dollar amounts included in the consolidated financial statements and notes thereto represent the arithmetical results of translating yen to dollars on the basis of ¥105.69=U.S.$1, the approximate exchange rate at March 31, 2004. The inclusion of such dollar amounts is solely for convenience and is not intended to imply that yen amounts can be converted into dollars at ¥105.69=U.S.$1 or at any other rate.

5. SECURITIES

a) Available-for-sale securities for which market value is available in 2004 and 2003:

	March 31, 2004		
	Millions of Yen		
	Historical cost	Fair market value	Unrealized gain (loss)
Securities with unrealized gain:			
Shares	**¥6,955**	**¥31,761**	**¥24,806**
Other securities, excluding bonds	**20**	**20**	**0**
Securities with unrealized loss:			
Shares	**372**	**365**	**(7)**

	March 31, 2004		
	Thousands of U.S. Dollars		
	Historical cost	Fair market value	Unrealized gain (loss)
Securities with unrealized gain:			
Shares	**$65,806**	**$300,511**	**$234,705**
Other securities, excluding bonds	**189**	**189**	**0**
Securities with unrealized loss:			
Shares	**3,520**	**3,453**	**(67)**

	March 31, 2003		
	Millions of Yen		
	Historical cost	Fair market value	Unrealized gain (loss)
Securities with unrealized gain:			
Shares	¥8,252	¥31,206	¥22,954
Other securities, excluding bonds	20	20	0
Securities with unrealized loss:			
Shares	1,579	1,310	(269)

b) Amount of available-for-sale securities sold in fiscal 2004 and 2003:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	**2004**
Amount sold	**¥15,572**	¥2,899	**$147,337**
Realized gain	**12,965**	1,834	**122,670**
Realized loss	**(21)**	(12)	**(199)**

c) Details of investments in securities without market quotation in 2004 and 2003:

	Millions of Yen		Thousands of U.S. Dollars
Description	**2004**	2003	**2004**
Available-for-sale securities:			
Unlisted shares (excluding OTC shares)	**¥10,029**	¥10,118	**$94,890**
Other securities	**1,017**	1,006	**9,622**

d) Maturity schedule of available-for-sale securities with scheduled maturity:

	March 31, 2004
	Millions of Yen
Less than one year	¥ —
More than one year less than five years	26
More than five years less than ten years	—
Thereafter	—

	March 31, 2004
	Thousands of U.S. Dollars
Less than one year	$ —
More than one year less than five years	246
More than five years less than ten years	—
Thereafter	—

e) Assets pledged as collateral and relevant debt:

	March 31		
	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	**2004**
Investments in securities	**¥174**	¥124	**$1,646**
Accounts and notes payable—trade	**321**	278	**3,037**

f) Investments in unconsolidated subsidiaries and affiliates:

	March 31		
	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	**2004**
Investments in shares	**¥16,441**	¥15,961	**$155,559**
Participations	**1,438**	1,222	**13,606**

6. SHORT-TERM AND LONG-TERM DEBT

Short-term debt consists principally of bank overdrafts bearing interest of 0.74% and 0.97%, the weighted average interest rate on outstanding balances as at March 31, 2004 and 2003, respectively. It is normal business custom in Japan for short-term bank loans to be rolled over each year.

Short-term borrowings as at March 31, 2004 and 2003, are summarized as follows:

	March 31		
	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	**2004**
Short-term bank loans	**¥13,187**	¥17,249	**$124,771**
Current portion of long-term borrowings	**45**	642	**425**
	¥13,232	¥17,891	**$125,196**

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

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	**2004**
Loans from banks, other financial institutions, etc., due from 2005 to 2012 with mortgage and collateral (Note 2)	**¥126**	¥ 1,078	**$1,192**
2.55 per cent. bond due 2008	**—**	15,000	**—**
2.525 per cent. bond due 2008	**—**	15,000	**—**
1.98 per cent. bond due 2008	**—**	3,000	**—**
	¥126	¥34,078	**$1,192**

Notes: 1. All bonds shown above are unsecured.
2. The interest rate on long-term loans (excluding current portion) from banks was 2.25%, the weighted average interest rate on outstanding balances at the year-end.
3. The bond was accounted for as redeemed due to a debt assumption contract. The debt assumption contract requires a counterparty to assume obligations of paying principal and interests on the bond. See Note 12 for underlying obligations of the Company.

Annual maturities of long-term debt, except for bonds, are as follows:

	Millions of Yen	Thousands of U.S. Dollars
Within one year	¥ 45	$ 425
More than one year less than two years	39	369
More than two years less than three years	31	293
More than three years less than four years	30	284
More than four years less than five years	17	161
More than five years	9	85
	¥171	$1,617

7. LEASE TRANSACTIONS

(1) Finance Leases

Information relating to finance leases, excluding those for which the ownership of the leased assets is considered to the lessee, as of, and for the years ended March 31, 2004 and 2003, is as follows.

The acquisition cost, accumulated depreciation and net book value of leased assets, at March 31, 2004 and 2003, are as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	**2004**
Acquisition cost	**¥2,071**	¥2,175	**$19,595**
Accumulated depreciation	**1,139**	1,094	**10,777**
Net book value	**¥ 932**	¥1,081	**$ 8,818**

Lease payments and depreciation for the years ended March 31, 2004 and 2003, amounted to ¥432 million ($4,087 thousand) and ¥512 million, respectively.

Depreciation is calculated using the straight-line method over the lease term of the leased assets assuming no residual value.

The scheduled maturities of future lease rental payments of finance leases as of March 31, 2004 and 2003, were as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	**2004**
Due within one year	**¥340**	¥ 404	**$3,217**
Due over one year	**592**	677	**5,601**
	¥932	¥1,081	**$8,818**

(2) Operating Leases

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	**2004**
Due within one year	**¥194**	¥ 5	**$1,836**
Due over one year	**356**	12	**3,368**
	¥550	¥17	**$5,204**

8. INCOME TAXES

The tax effects of temporary differences that give rise to significant portions of deferred tax assets and liabilities as of March 31, 2004, 2003 and 2002 are as follows:

Balance sheet item	March 31, 2004 Millions of Yen	March 31, 2004 Thousands of U.S. Dollars
Deferred tax assets:		
Reserve for bonuses	¥ 1,345	$ 12,726
Enterprise taxes payable	906	8,572
Non-deductible portion of reserve for accrued sales rebates, discounts and sales promotion	766	7,248
Non-deductible portion of reserve for retirement benefits to employees	12,002	113,559
Reserve for retirement benefits to directors and corporate auditors	318	3,009
Tax loss carried forward	581	5,497
Loss on write-down of investments in securities	538	5,090
Prepaid expense in tax accounting	1,370	12,962
Non-deductible portion of depreciation of property, plant and equipment	1,343	12,707
Loss on write-down of golf membership	393	3,718
Impairment on investments in certain consolidated subsidiaries	416	3,936
Loss on write-down of fixed assets held by overseas subsidiaries	1,187	11,231
Reserve for loss on disposal of fixed assets	743	7,030
Others	4,828	45,681
Sub-total	¥ 26,736	$ 252,966
Valuation allowance	(5,708)	(54,007)
Total deferred tax assets	¥ 21,028	$ 198,959
Deferred tax liabilities:		
Deferred gain, mainly related to expropriation of fixed assets	¥ (2,347)	$ (22,206)
Unrealized gains on available-for-sale securities	(10,082)	(95,392)
Others	(199)	(1,884)
Total deferred tax liabilities	¥(12,628)	$(119,482)
Deferred tax assets, net	¥ 8,400	$ 79,477

Note: Classification of "Deferred tax assets, net" on the consolidated balance sheet as of March 31, 2004 is as follows:

Balance sheet item		Millions of Yen	Thousands of U.S. Dollars
Current assets	Deferred tax assets	¥6,529	$61,775
Non-current assets	Deferred tax assets	1,957	18,516
Non-current liabilities	Deferred tax liabilities	(86)	(814)
		¥8,400	$79,477

	March 31, 2003
	Millions of Yen
Deferred tax assets:	
Non-deductible portion of reserve for bonuses	¥ 1,063
Enterprise taxes payable.	216
Non-deductible portion of reserve for accrued sales rebates, discounts and sales promotion	659
Non-deductible portion of reserve for retirement benefits to employees	4,319
Reserve for retirement benefits to directors and corporate auditors	327
Tax loss carried forward	3,823
Loss on write-down of investments in securities	855
Prepaid expense in tax accounting	1,234
Non-deductible portion of depreciation of property, plant and equipment	1,123
Loss on write-down of golf membership	489
Impairment on investments in certain consolidated subsidiaries	6,305
Loss on write-down of fixed assets held by overseas subsidiaries	1,581
Others	2,221
Sub-total	¥ 24,215
Valuation allowance	(5,608)
Total deferred tax assets	¥ 18,607
Deferred tax liabilities:	
Deferred gain, mainly related to expropriation of fixed assets	¥ (2,396)
Special depreciation of property, plant and equipment held by an overseas subsidiary	(2,029)
Unrealized gains on available-for-sale securities	(9,129)
Others	(47)
Total deferred tax liabilities	¥(13,601)
Deferred tax assets, net	¥ 5,006

Note: Classification of “Deferred tax assets, net” on the consolidated balance sheet as of March 31, 2003 is as follows:

		Millions of Yen
Current assets	Deferred tax assets	¥3,877
Non-current assets	Deferred tax assets	1,459
Non-current liabilities	Deferred tax liabilities	(330)
		¥5,006

	March 31, 2002
	Millions of Yen
Deferred tax assets:	
Non-deductible portion of reserve for bonuses	¥ 1,002
Enterprise taxes payable.	1,409
Non-deductible portion of reserve for accrued sales rebates, discounts and sales promotion	814
Non-deductible portion of reserve for retirement benefits to employees	5,082
Reserve for retirement benefits to directors and corporate auditors	406
Tax loss carried forward	7,293
Loss on write-down of investments in securities	764
Prepaid expense in tax accounting	861
Non-deductible portion of depreciation of property, plant and equipment	884
Loss on write-down of golf membership	457
Impairment on investments in certain consolidated subsidiaries	10,344
Loss on write-down of fixed assets held by overseas subsidiaries	3,934
Others	3,029
Sub-total	¥ 36,279
Valuation allowance	(11,460)
Total deferred tax assets	¥ 24,819
Deferred tax liabilities:	
Deferred gain, mainly related to expropriation of fixed assets	¥ (2,205)
Special depreciation of property, plant and equipment held by an overseas subsidiary	(2,530)
Unrealized gains on available-for-sale securities	(10,709)
Others	(519)
Total deferred tax liabilities	¥(15,963)
Deferred tax assets, net	¥ 8,856

Note: Classification of "Deferred tax assets, net" on the consolidated balance sheet as of March 31, 2002 is as follows:

		Millions of Yen
Current assets	Deferred tax assets	¥5,041
Non-current assets	Deferred tax assets	4,318
Non-current liabilities	Deferred tax liabilities	(503)
		¥8,856

Note: Deferred tax assets relating to operating losses are recorded in accordance with the Japanese accounting standards which require that the benefit of tax loss carryforwards be estimated and recorded as an asset, with the deduction of a valuation allowance if it is expected that some portion or all of the deferred tax assets will not be realized.

Reconciliation between the statutory tax rate and the effective tax rate as at March 31, 2004, 2003 and 2002 is as follows:

	March 31		
	2004	2003	2002
Statutory tax rate	**41.7%**	41.7%	41.69%
Permanent differences:			
Non-deductible expenses such as entertainment expenses	**10.1**	8.8	13.51
Non-taxable income such as dividend income	**(1.8)**	(1.2)	(3.05)
Special corporate tax credit	**(9.1)**	—	—
Future tax benefits deemed not to be realized	**(37.7)**	(19.3)	82.52
Equity in earnings of affiliates	**(1.5)**	(0.5)	(4.09)
Impairment on investments in certain consolidated subsidiaries	**38.3**	16.2	(70.14)
Adjustment of deferred tax assets due to change in tax rate	**—**	2.3	—
Others	**(4.1)**	1.9	(4.36)
Effective tax rate	**35.9%**	49.9%	56.08%

Due to the change in local tax law during fiscal 2003, the effective tax rate used in the calculation of deferred tax assets and liabilities is reduced from 41.7% to 40.3%. As a result, for fiscal 2003, deferred tax assets, net of deferred tax liabilities, income taxes and unrealized gains on available-for-sale securities increased by ¥56 million, ¥383 million and ¥327 million, respectively.

9. RESERVE FOR RETIREMENT BENEFITS TO EMPLOYEES

The Company and its domestic consolidated subsidiaries operate various defined benefit plans, such as a contributory pension plan, a qualified pension plan and a severance payment plan.

Following the enactment of the Welfare Pension Insurance Law in Japan, on March 1, 2003, the KYOWA HAKKO KOGYO CO., LTD. Group contributory pension plan obtained approval from Japan's Ministry of Health, Labour and Welfare for exemption from the future benefit obligation with respect to the portion of the contributory pension plan that the Company and its domestic subsidiaries operate on behalf of the Government (the so-called substitutional portion).

a) The reserve for retirement benefits as of March 31, 2004, 2003 and 2002 is analyzed as follows:

	Millions of Yen			Thousands of U.S. Dollars
	2004	2003	2002	**2004**
Projected benefit obligations	**¥(70,112)**	¥(73,334)	¥(124,705)	**$(663,374)**
Plan assets	**26,551**	23,240	62,191	**251,216**
Unfunded benefit obligations	**(43,561)**	(50,094)	(62,514)	**(412,158)**
Unrecognized actuarial differences	**10,352**	33,310	47,321	**97,947**
Unrecognized prior service costs (Note 3)	**(560)**	(817)	(2,111)	**(5,299)**
	¥(33,769)	¥(17,601)	¥ (17,304)	**$(319,510)**

Notes: 1. The table as of March 31, 2002 includes the amounts of the substitutional portion of the contributory pension plan.
2. Certain subsidiaries calculate the projected benefit obligation by the simple method permitted under the accounting standard generally accepted in Japan.
3. Unrecognized prior service costs incurred in fiscal 2002, were due to a change in the benefit level prescribed by the contributory pension plan and a severance payment plan. Unrecognized prior service costs (reduction of liability) incurred in fiscal 2003, were due to a change in the age of eligibility for annuity payments for the basic portion of the contributory pension plan.
4. The Company and certain of its domestic consolidated subsidiaries applied transitional provisions as prescribed in paragraph 47-2 of the "Practical Guidelines of Accounting for Retirement Benefits (Interim Report)" (Accounting Committee Report No. 13 issued by the Japanese Institute of Certified Public Accountants) and the settlement of the substitutional portion was recognized at the date of approval from Japan's Ministry of Health, Labour and Welfare. The amount of plan assets to be returned was ¥29,633 million at the end of fiscal 2003.

b) The net periodic pension expense related to the retirement benefits for fiscal 2004, 2003 and 2002 is as follows:

	Millions of Yen			Thousands of U.S. Dollars
	2004	2003	2002	**2004**
Service cost (Notes 1 and 2)	**¥ 2,795**	¥ 5,018	¥ 3,875	**$ 26,446**
Interest cost	**1,794**	3,029	3,629	**16,974**
Expected return on plan assets	**(648)**	(2,277)	(2,366)	**(6,131)**
Amortization of unrecognized actuarial differences	**3,002**	4,913	1,810	**28,404**
Amortization of unrecognized prior service costs	**(257)**	(980)	(527)	**(2,432)**
Special severance payment	**1,623**	28	198	**15,356**
	¥ 8,309	¥ 9,731	¥ 6,619	**$ 78,617**
Gain on the transfer of the substitutional portion of contributory pension plan	**—**	(2,873)	—	**—**
Arising from the lump-sum recognition of the previous years' unrecognized actuarial differences associated with cancellation of the Company's retirement benefit trust contract	**16,227**	—	—	**153,534**
	¥24,536	¥ 6,858	¥ 6,619	**$232,151**

Notes: 1. Excludes employees' contributions made to the contributory pension plan operated by the Company.
2. Includes net periodic pension expense incurred by the subsidiaries which apply the simple method.

c) Assumptions used in calculation of the above information are as follows:

	As of March 31, 2004	As of March 31, 2003	As of March 31, 2002
Method of attributing the projected benefits to periods of services	**Benefit/year of service approach**	Benefit/year of service approach	Benefit/year of service approach
Discount rate	**2.5%**	2.5%	2.5%
Expected rate of return	**2.8%**	3.6%	3.1%

10. DERIVATIVE TRANSACTIONS

(1) Conditions of Derivative Financial Instruments

In the normal course of business, the Companies use various financial instruments, including derivative financial instruments, to manage their exposures to market risks. The Companies do not use derivative financial instruments for speculative purposes. These instruments include foreign currency swaps, foreign exchange contracts, and interest rate swaps and cap agreements.

All such instruments involve risk, including the credit risk of non-performance by counterparties. However, at March 31, 2004, in the management's opinion, there was no significant risk of loss in the event of non-performance of the counterparties on these financial instruments, because all counterparties were major financial institutions and securities companies with high credit ratings. Also, the Companies do not use derivative financial instruments for highly leveraged transactions.

(2) Fair Value Information of Derivative Financial Instruments

Under the Japanese Regulation for Consolidated Financial Statements, fair value information is not required about outstanding derivative financial instruments which are hedged for exposing to losses from market volatility. All outstanding derivative financial instruments have been hedged by the Companies.

Therefore, no item was required to be disclosed in this section as of March 31, 2004.

11. SUPPLEMENTARY STATEMENTS OF INCOME

a) The major elements of selling, general and administrative expenses for each of the three years in the period ended March 31, 2004, 2003 and 2002 are as follows:

	Millions of Yen			Thousands of U.S. Dollars
	2004	2003	2002	**2004**
Research and development expenses	**¥28,724**	¥30,932	¥28,732	**$271,776**
Salaries	**17,449**	17,886	18,915	**165,096**
Sales promotion	**8,104**	8,856	10,347	**76,677**
Bonuses to employees	**7,092**	7,326	7,782	**67,102**

b) Loss on disposal of fixed assets relevant to organizational restructuring is the loss related to the disposal of fixed assets which were identified through a review of the utilization of our fixed assets after organizational restructuring. Details are as follows:

	Millions of Yen	Thousands of U.S. Dollars
	2004	2004
Provision for cost of disposal of fixed assets	¥1,826	$17,277
Loss on disposal of fixed assets	1,399	13,237
	¥3,225	$30,514

c) Detail of the Administrative fines in a cartel for sales of amino lysine within European Economic Area(EEA) is as follows:

On June 7, 2000, the Company and Kyowa Hakko Europe GmbH(“KHEG”) had a fine of 13,200 thousand Euro imposed on them by a Decision of the European Commission with allegations that the Company and KHEG had violated EU competition law due to their involvement in a cartel for the sale of amino acid lysine within EEA prior to June 1995. On August 25, 2000, the Company and KHEG lodged an appeal to the Court of the European Communities with regard to the amount of the fine. However, the Company decided to accept the ruling of the European first court of instance on July 9, 2003 to recognize that the European Commission’s verdict in question is appropriate and to pay the above-mentioned fine(13,200 thousand Euro). The amount accounted for as a fine regarding lysine sales within EEA is the difference between the fine and accrued liability accounted in fiscal year 2001 (1,120 thousand Euro) and interest for delay of payment of the fine.

d) Loss on restructuring of certain subsidiaries and affiliates consisted of the following:

	Millions of Yen	Thousands of U.S. Dollars
	2004	2004
Provision for loss on write-down of investments	¥ 35	$ 331
Loss on sale of investment in affiliates	550	5,204
Other	258	2,441
	¥843	$7,976

	Millions of Yen
	2003
Loss on write-down of fixed assets	¥3,241
Foreign exchange loss	1,350
Provision for doubtful accounts	388
Valuation loss on inventories	214
Provision for loss on write-down of investments	147
Loss on write-down of investments in affiliates	37
Loss on sales of investments in affiliates	5
Other	665
	¥6,047

	Millions of Yen
	2002
Loss on write-down of fixed assets	¥19,491
Loss on sales/disposal of fixed assets	555
Loss on sales of investments in affiliates	511
Provision for doubtful accounts	241
Loss on write-down of investments in affiliates	112
Provision for loss on write-down of investments	38
Other	133
	¥21,081

e) Gain on the transfer of the alcoholic beverage operations consisted of the following:

	Millions of Yen
	2003
Gain on transfer of operations	¥5,069
Gain on corporate separation	988
Loss on transition of retirement benefit obligation	(592)
Lump-sum payment of employment transfer and special retirement benefits	(548)
Loss on disposal of inventories	(509)
Loss on disposal of property and equipment	(215)
Other	(946)
	¥3,247

12. CONTINGENT LIABILITIES

(1) The Companies and its consolidated subsidiaries had contingent liabilities arising from notes discounted by banks in the amount of ¥54 million ($511 thousand) and from notes endorsed in the amount of ¥13 million ($123 thousand) at March 31, 2004.

The Company and its consolidated subsidiaries are contingently liable for guarantees of loans borrowed by Sanbo-Brewer Ltd. and others in the amounts of ¥360 million ($3,406 thousand) and ¥351 million ($3,321 thousand), respectively, at March 31, 2004.

(2) Contingent liabilities under a debt assumption agreement were to totaled ¥33,000 million ($312,234 thousand).

13. RELATED PARTY TRANSACTIONS

The Company discloses material transactions of the Company with its related companies, representing more than 10 percent of the consolidated sales or the total amount of the consolidated cost of sales and the consolidated selling, general and administrative expenses, excluding transactions with consolidated subsidiaries which are eliminated in the consolidated financial statements. Also, the Company discloses material balances and transactions with related companies where such balances and transactions, including the related amount in the footnote, represent more than 1 percent of the consolidated total assets, excluding transactions with consolidated subsidiaries which are eliminated in the consolidated financial statements. No such transaction occurred in fiscal 2004, 2003 and 2002.

Material transactions and balances of the Company with its related individuals, including shareholders and directors, representing more than ¥1 million shall be disclosed, but are not applicable for the years ended March 31, 2004, 2003 and 2002.

14. CASH FLOW INFORMATION

(1) Summary of assets and liabilities excluded following the transfer of alcoholic beverage operations:

	Millions of Yen
	2003
Current assets	¥11,247
Fixed assets	2,775
Total assets	¥14,022
Current liabilities	¥ 2,441
Non-current liabilities	1,750
Total liabilities	¥ 4,191

(2) Payment information of principal and interest on the 15th, 16th and 17th unsecured corporate bond, which were transferred on a debt assumption contract.

15. SEGMENT INFORMATION

(1) Industry Segment Information

The Companies operate principally in the following 5 industry segments:

Industry segments:	**Major products:**
(1) Pharmaceuticals Division	Ethical drugs and diagnostic reagents
(2) Bio-Chemicals Division	Bulk pharmaceuticals, animal health products and agrochemicals
(3) Chemicals Division	Solvents, plasticizers and their raw materials and specialty chemicals
(4) Food Division	Seasonings, confectionery and baking ingredients, processed foods and alcohol
(5) Other Division	Transportation, warehouse and sales of apparatus for industry

	Millions of Yen							
	Industry segment							
Year ended March 31, 2004	Pharmaceuticals	Bio-Chemicals	Chemicals	Food	Other	Total	Corporate, elimination and other	Consolidated total
I. Sales and Operating Income:								
Sales:								
Sales to outside customers	**¥141,376**	**¥50,474**	**¥61,829**	**¥51,824**	**¥43,335**	**¥348,838**	**¥ —**	**¥348,838**
Inter-segment sales/transfers	**1,490**	**8,494**	**5,070**	**4,879**	**19,833**	**39,766**	**(39,766)**	**—**
Total sales	**142,866**	**58,968**	**66,899**	**56,703**	**63,168**	**388,604**	**(39,766)**	**348,838**
Operating expenses	**130,958**	**50,476**	**64,006**	**54,702**	**61,387**	**361,529**	**(39,527)**	**322,002**
Operating income	**¥ 11,908**	**¥ 8,492**	**¥ 2,893**	**¥ 2,001**	**¥ 1,781**	**¥ 27,075**	**¥ (239)**	**¥ 26,836**
II. Assets, Depreciation and amortization and Capital Expenditures:								
Assets	**¥108,255**	**¥63,078**	**¥67,349**	**¥40,274**	**¥42,812**	**¥321,768**	**¥ 39,328**	**¥361,096**
Depreciation and amortization	**4,476**	**2,749**	**2,651**	**1,149**	**122**	**11,147**	**211**	**11,358**
Capital expenditures	**3,552**	**1,722**	**1,758**	**1,889**	**128**	**9,049**	**(8)**	**9,041**

	Thousands of U.S. Dollars							
	Industry segment							
Year ended March 31, 2004	Pharmaceuticals	Bio-Chemicals	Chemicals	Food	Other	Total	Corporate, elimination and other	Consolidated total
I. Sales and Operating Income:								
Sales:								
Sales to outside customers	**$1,337,648**	**$477,566**	**$585,003**	**$490,340**	**$410,020**	**$3,300,577**	**$ —**	**$3,300,577**
Inter-segment sales/transfers	**14,097**	**80,368**	**47,971**	**46,163**	**187,652**	**376,251**	**(376,251)**	**—**
Total sales	**1,351,745**	**557,934**	**632,974**	**536,503**	**597,672**	**3,676,828**	**(376,251)**	**3,300,577**
Operating expenses	**1,239,077**	**477,586**	**605,601**	**517,570**	**580,821**	**3,420,655**	**(373,990)**	**3,046,665**
Operating income	**$ 112,668**	**$ 80,348**	**$ 27,373**	**$ 18,933**	**$ 16,851**	**$ 256,173**	**$ (2,261)**	**$ 253,912**
II. Assets, Depreciation and amortization and Capital Expenditures:								
Assets	**$1,024,269**	**$596,821**	**$637,232**	**$381,058**	**$405,071**	**$3,044,451**	**$ 372,107**	**$3,416,558**
Depreciation and amortization	**42,351**	**26,010**	**25,083**	**10,871**	**1,154**	**105,469**	**1,996**	**107,465**
Capital expenditures	**33,607**	**16,293**	**16,634**	**17,873**	**1,211**	**85,618**	**(75)**	**85,543**

As described in additional information of Note 3 (5) to the Consolidated financial statements, effective April 1, 2003, the Company changed its depreciation method for certain fixed assets which are applied to declining balance method, from the group depreciation method to the individual depreciation method for each asset.

Compared to the group depreciation method, operational expense decreased by ¥438 million ($4,144 thousand) in "Pharmaceuticals" segment, ¥224 million ($2,120 thousand) in "Bio-Chemicals" segment, ¥365 million ($3,453 thousand) in "Chemicals" segment, ¥84 million ($795 thousand) in "Food" segment and ¥8 million ($76 thousand) in "Corporate, elimination and other" segment, and operating profit increased by the same amount in the respective segments.

	Millions of Yen							
	Industry segment						Corporate, elimination and other	Consolidated total
Year ended March 31, 2003	Pharmaceuticals	Bio-Chemicals	Chemicals	Liquor and Food	Other	Total		
I. Sales and Operating Income (Loss):								
Sales:								
Sales to outside customers	¥138,341	¥50,921	¥60,343	¥67,745	¥41,935	¥359,285	¥ —	¥ 359,285
Inter-segment sales/transfers	2,253	7,604	4,815	4,577	21,550	40,799	(40,799)	—
Total sales	140,594	58,525	65,158	72,322	63,485	400,084	(40,799)	359,285
Operating expenses	129,580	56,550	64,058	72,690	60,888	383,766	(40,570)	343,196
Operating income (loss)	¥ 11,014	¥ 1,975	¥ 1,100	¥ (368)	¥ 2,597	¥ 16,318	¥ (229)	¥ 16,089
II. Assets, Depreciation and amortization and Capital Expenditures:								
Assets	¥109,167	¥65,085	¥68,859	¥40,275	¥30,501	¥313,887	¥54,885	¥368,772
Depreciation and amortization	5,055	3,898	3,629	1,677	131	14,390	378	14,768
Capital expenditures	4,185	3,664	2,150	1,401	130	11,530	261	11,791

	Millions of Yen							
	Industry segment						Corporate, elimination and other	Consolidated total
Year ended March 31, 2002	Pharmaceuticals	Bio-Chemicals	Chemicals	Liquor and Food	Other	Total		
I. Sales and Operating Income (Loss):								
Sales:								
Sales to outside customers	¥139,724	¥48,637	¥55,446	¥ 99,261	¥35,600	¥378,668	¥ —	¥378,668
Inter-segment sales/transfers	2,573	6,859	4,964	4,270	24,177	42,843	(42,843)	—
Total sales	142,297	55,496	60,410	103,531	59,777	421,511	(42,843)	378,668
Operating expenses	123,338	54,228	61,584	103,971	58,021	401,142	(42,831)	358,311
Operating income (loss)	¥ 18,959	¥ 1,268	¥ (1,174)	¥ (440)	¥ 1,756	¥ 20,369	¥ (12)	¥ 20,357
II. Assets, Depreciation and amortization and Capital Expenditures:								
Assets	¥117,196	¥70,794	¥71,162	¥ 72,327	¥30,631	¥362,110	¥ 68,003	¥430,113
Depreciation and amortization	5,368	4,881	4,149	2,860	137	17,395	424	17,819
Capital expenditures	4,523	2,586	1,729	2,243	161	11,242	212	11,454

(2) Geographic Segment Information

Areas other than Japan are classified into "Americas", "Europe" and "Asia":

Classification:	Area:
(1) Americas	North America, Latin America
(2) Europe	Whole Europe
(3) Asia	Whole Asia

Sales and assets in Americas, Europe and Asia consist of less than 10% of total sales and total assets, respectively, therefore, all are totally referred to as "Other areas".

	Millions of Yen				
	Geographic segment			Corporate,	
Year ended March 31, 2004	Japan	Other areas	Total	elimination and other	Consolidated total
I. Sales and Operating Income:					
Sales:					
Sales to outside customers	**¥315,262**	**¥33,576**	**¥348,838**	**¥ —**	**¥348,838**
Inter-segment sales/transfers	**16,509**	**5,663**	**22,172**	**(22,172)**	**—**
Total sales	**331,771**	**39,239**	**371,010**	**(22,172)**	**348,838**
Operating expenses	**307,629**	**35,638**	**343,267**	**(21,265)**	**322,002**
Operating income	**¥ 24,142**	**¥ 3,601**	**¥ 27,743**	**¥ (907)**	**¥ 26,836**
II. Assets:					
Assets	**¥289,031**	**¥21,190**	**¥310,221**	**¥50,875**	**¥361,096**

	Thousands of U.S. Dollars				
	Geographic segment			Corporate,	
Year ended March 31, 2004	Japan	Other areas	Total	elimination and other	Consolidated total
I. Sales and Operating Income:					
Sales:					
Sales to outside customers	**$2,982,893**	**$317,684**	**$3,300,577**	**$ —**	**$3,300,577**
Inter-segment sales/transfers	**156,202**	**53,581**	**209,783**	**(209,783)**	**—**
Total sales	**3,139,095**	**371,265**	**3,510,360**	**(209,783)**	**3,300,577**
Operating expenses	**2,910,672**	**337,194**	**3,247,866**	**(201,201)**	**3,046,665**
Operating income	**$ 228,423**	**$ 34,071**	**$ 262,494**	**$ (8,582)**	**$ 253,912**
II. Assets:					
Assets	**$2,734,705**	**$200,492**	**$2,935,197**	**$ 481,361**	**$3,416,558**

As described in additional information of Note 3 (5) to the Consolidated financial statements, effective April 1, 2003, the Company changed its depreciation method for certain fixed assets which are applied to declining balance method, from the group depreciation method to the individual depreciation method for each asset.

Compared to the group depreciation method, operational expense decreased by ¥1,119 million ($10,588 thousand) and operating profit increased by the same amount in the "Japan" segment.

	Millions of Yen				
	Geographic segment				
Year ended March 31, 2003	Japan	Other areas	Total	Corporate, elimination and other	Consolidated total
I. Sales and Operating Income (Loss):					
Sales:					
Sales to outside customers	¥322,691	¥36,594	¥359,285	¥ —	¥ 359,285
Inter-segment sales/transfers	17,176	6,477	23,653	(23,653)	—
Total sales	339,867	43,071	382,938	(23,653)	359,285
Operating expenses	322,460	44,325	366,785	(23,589)	343,196
Operating income (loss)	¥ 17,407	¥ (1,254)	¥ 16,153	¥ (64)	¥ 16,089
II. Assets:					
Assets	¥292,495	¥22,921	¥315,416	¥ 53,356	¥368,772

	Millions of Yen				
	Geographic segment				
Year ended March 31, 2002	Japan	Other areas	Total	Corporate, elimination and other	Consolidated total
I. Sales and Operating Income (Loss):					
Sales:					
Sales to outside customers	¥343,241	¥35,427	¥378,668	¥ —	¥378,668
Inter-segment sales/transfers	16,972	7,385	24,357	(24,357)	—
Total sales	360,213	42,812	403,025	(24,357)	378,668
Operating expenses	337,831	44,326	382,157	(23,846)	358,311
Operating income (loss)	¥ 22,382	¥ (1,514)	¥ 20,868	¥ (511)	¥ 20,357
II. Assets:					
Assets	¥336,475	¥29,451	¥365,926	¥ 64,187	¥430,113

(3) Overseas Sales

The classification of overseas sales is as follows:

Classification:	**Area:**
(1) Americas	North America, Latin America
(2) Europe	Whole Europe
(3) Asia	Whole Asia
(4) Other areas	Oceania, Africa

Year ended March 31, 2004	Millions of Yen				
	Americas	Europe	Asia	Other areas	Total
I. Overseas sales	**¥19,712**	**¥17,717**	**¥20,629**	**¥210**	**¥ 58,268**
II. Consolidated net sales					**348,838**
III. Ratio of overseas sales to consolidated net sales	**5.6%**	**5.1%**	**5.9%**	**0.1%**	**16.7%**

Year ended March 31, 2004	Thousands of U.S. Dollars				
	Americas	Europe	Asia	Other areas	Total
I. Overseas sales	**$186,508**	**$167,632**	**$195,184**	**$1,986**	**$ 551,310**
II. Consolidated net sales					**3,300,577**
III. Ratio of overseas sales to consolidated net sales	**5.6%**	**5.1%**	**5.9%**	**0.1%**	**16.7%**

Year ended March 31, 2003	Millions of Yen				
	Americas	Europe	Asia	Other areas	Total
I. Overseas sales	¥21,701	¥18,072	¥22,167	¥322	¥ 62,262
II. Consolidated net sales					359,285
III. Ratio of overseas sales to consolidated net sales	6.0%	5.0%	6.2%	0.1%	17.3%

Year ended March 31, 2002	Millions of Yen				
	Americas	Europe	Asia	Other areas	Total
I. Overseas sales	¥21,577	¥15,239	¥19,385	¥192	¥ 56,393
II. Consolidated net sales					378,668
III. Ratio of overseas sales to consolidated net sales	5.7%	4.0%	5.1%	0.1%	14.9%

Note: Overseas sales are sales by the Companies to customers outside of Japan.

16. PER SHARE DATA

	Yen			U.S. Dollars
	2004	2003	2002	**2004**
Net assets per share	**¥522.6**	¥505.4	¥487.5	**$4.945**
Net income—basic	**¥23.0**	¥19.4	¥12.7	**$0.218**
Net income—diluted (*)	**—**	—	—	**—**

* 1. Diluted net income per share for fiscal 2002 is not disclosed because there were anti-dilutive effects.
2. Diluted net income per share for fiscal 2004 and 2003 is not disclosed because there were no residual securities.

Effective from fiscal 2003, the Company and its domestic consolidated subsidiaries adopted the Financial Accounting Standards No. 2 "Financial Accounting Standards for Earnings per Share" and the Financial Accounting Standards Implementation Guidance No. 4 "Implementation Guidance for Accounting Standards for Earnings per Share".

By applying this method, the amounts of net income per share and net assets per share for fiscal 2002 is calculated as follows:

	Yen
	2002
Net assets per share	¥487.4
Net income—basic	¥12.6
Net income—diluted (*)	—

* Diluted net income per share for fiscal 2002 is not disclosed because there were anti-dilutive effects.

Basis for the calculation of net income per share data is as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	**2004**
Net income	**¥10,017**	¥8,485	**$94,777**
Less: Components not pertaining to common shareholders			
Bonuses to directors and corporate auditors	**(93)**	(90)	**880**
Net income pertaining to common shareholders	**¥ 9,924**	¥8,395	**$93,897**

	2004	2003
Average outstanding shares to common stock:	431,497,240	433,747,760 shares

17. SUBSEQUENT EVENTS

a) Subsequent to March 31, 2004, the Company's Board of Directors, with the approval by shareholders on June 29, 2004, declared a cash dividend of ¥1,614 million ($15,271 thousand), equal to ¥3.75 ($0.04) per share, which was applicable to earnings of the year ended March 31, 2004 and payable to shareholders on the register on March 31, 2004.

b) The Company's Board of Directors meeting held on April 27, 2004 approved to transfer all shares of the subsidiary, Agroferm Hungarian-Japanese Fermentation Industry Ltd. (incorporated in Hungary), which engages in production of amino acid for animal consumption, and entered into a transferring contract on May 1, 2004

1) Reason for transfer of shares
   To focus management resources on high-value-added amino acids for pharmaceuticals, food products, industrial use
2) Summary of transferee of shares
   a) Name: Degussa AG
   b) Representative: Utz-Hellmuth Felcht, the chairman of Board of Directors
   c) Location: Federal Republic of Germany
   d) Description of business: Chemical Engineering
3) Signing of contract: May 1, 2004
4) Scheduled date of transfer: June 30, 2004
5) Summary of the transferred subsidiary
   a) Name: Agroferm Hungarian-Japanese Fermentation Industry Ltd.
   b) Description of business: Production and sales of amino acid for animal consumption
   c) Capital: 3,505,730 thousand Hungarian Forint
   d) Issued number of shares: 350,573 shares
   e) Controlling share: Kyowa Hakko Kogyo Co., Ltd. 100%
6) Other
   The Company exclusively licenses its intellectual property rights of amino acid for animal consumption such as Lysine, Threonine and Triptphan to Degussa AG to the extent it continues its domestic sales and distribution as in the past.

REPORT OF INDEPENDENT AUDITORS

To the Board of Directors and Shareholders of
KYOWA HAKKO KOGYO CO., LTD.

We have audited the accompanying consolidated balance sheets of KYOWA HAKKO KOGYO CO., LTD. and its subsidiaries as of March 31, 2004 and 2003, and the related consolidated statements of income, shareholders' equity and cash flows for the three years ended March 31, 2004, all expressed in Japanese Yen. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Japan. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated 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 KYOWA HAKKO KOGYO CO., LTD. and its subsidiaries as of March 31, 2004 and 2003, and the consolidated results of their operations and their cash flows for the three years ended March 31, 2004 in conformity with accounting principles generally accepted in Japan.

The amounts expressed in U.S. dollars, which are provided solely for the convenience of the readers, have been translated on the basis set forth in Note 4 to the accompanying consolidated financial statements.

ChuoAoyama PricewaterhouseCoopers

Tokyo, Japan
June 29, 2004

PRINCIPAL SUBSIDIARIES AND AFFILIATES

(As of March 31, 2004)

Name of Company	Percentage Owned Directly or Indirectly by the Company	Capital Stock (Millions)	Principal Business
Pharmaceuticals			
Kyowa Medex Co., Ltd.[1]	100.0%	¥450	Manufacture and sale of diagnostic reagents
Shinwa Pharmaceutical Co., Ltd.[1]	100.0	¥95	Manufacture and sale of herbal medicines and health foods
Kyowa Medical Promotion Co., Ltd.[1]	100.0	¥50	Sales promotion of pharmaceuticals
Bio-Chemicals			
Kyowa Hakko U.S.A., Inc. (U.S.A.)[1]	100.0	$1	Sale of pharmaceuticals, fine chemicals, foods, and chemicals
Kyowa Hakko Europe GmbH (Germany)[1]	100.0	Euro1	Sale of pharmaceuticals, fine chemicals, feed additives, and chemicals
Kyowa Italiana Farmaceutici S.R.L. (Italy)[1]	100.0	Euro1	Sale of pharmaceuticals and fine chemicals
Biokyowa Inc. (U.S.A.)[1]	100.0	$20	Manufacture and sale of fine chemicals
Agroferm Hungarian-Japanese Fermentation Industry Ltd. (Hungary)[1,3]	100.0	HuF3,506	Manufacture and sale of feed additives
Kyowa Hakko (H.K.) Co., Ltd. (Hong Kong)[1]	100.0	HK$1	Sale of pharmaceuticals, feed additives, foods, and chemicals
Chemicals			
Kyowa Yuka Co., Ltd.[1,4]	100.0	¥5,300	Manufacture and sale of chemicals
Kurogane Kasei Co., Ltd.[2]	40.0	¥90	Manufacture and sale of chemicals
J-PLUS Co., Ltd.[2]	50.0	¥480	Manufacture and sale of plasticizers
Food			
Riken Kagaku Co., Ltd.[1]	100.0	¥30	Manufacture and sale of pharmaceuticals and chemicals
Kyowa F.D. Foods Co., Ltd.[1]	100.0	¥275	Manufacture and sale of foods
Ohland Foods Co., Ltd.[1]	100.0	¥50	Manufacture and sale of foods
Kyowa HiFoods Co., Ltd.[1]	100.0	¥60	Manufacture, importation, and sale of foods and household goods
Asahi Foods Products Co., Ltd.[1]	78.0	¥36	Manufacture and sale of foods
Kyushu Kyowa Shokuhin Hanbai Co., Ltd.[1]	100.0	¥50	Wholesale of foods
Kyowa Foods (H.K.) Co., Ltd. (Hong Kong)[1,5]	100.0	HK$2	Sale of foods
Aji-Nihon Co., Ltd.[2]	46.3	¥95	Manufacture and sale of foods and seasonings
Zenmi Foods Inc.[2]	50.0	¥190	Manufacture and sale of foods
Other			
Miyako Kagaku Co., Ltd.[1]	52.9	¥111	Wholesale of pharmaceuticals, chemicals, and foods
Chiyoda Kaihatsu Co., Ltd.[1]	100.0	¥113	Transportation, trading, and insurance
Kyowa Engineering Co., Ltd.[1]	100.0	¥70	Design and installation of equipment and facilities and sale of health foods
Kyowa Warehouse & Transportation Co., Ltd.[1]	100.0	¥70	Warehousing and transportation
Seifu Co., Ltd.[1]	100.0	¥40	Office building administration and financing
Kyowa America, Inc. (U.S.A.)[1]	100.0	$53	Coordination and monitoring of subsidiaries in the United States
Japan Synthetic Alcohol Co., Ltd.[2]	33.3	¥480	Manufacture and sale of various types of alcohol
Musashino Chemical Laboratory, Ltd.[2]	25.0	¥238	Manufacture and sale of organic synthetic chemicals

Notes: 1. Consolidated subsidiary
2. Affiliate accounted for by the equity method
3. In May 2004, the Company agreed to sell all shares to Degussa AG, of Germany.
4. Accompanying the separation of the Chemicals Company into a wholly owned subsidiary, its name was changed to Kyowa Hakko Chemical Co., Ltd., on April 1, 2004.
5. Currently being liquidated

OVERSEAS NETWORK

(As of June 29, 2004)

AMERICAS

Kyowa America, Inc.
767 Third Avenue, 19th Floor,
New York, NY 10017, U.S.A.
TEL: 1-212-319-5353
FAX: 1-212-421-1283

Biokyowa Inc.
5469 Nash Road, P.O. Box 1550,
Cape Girardeau, MO 63702-1550, U.S.A.
TEL: 1-573-335-4849
FAX: 1-573-335-1466

Kyowa Hakko U.S.A., Inc.
767 Third Avenue, 19th Floor,
New York, NY 10017, U.S.A.
TEL: 1-212-319-5353
FAX: 1-212-421-1283

West Coast Office
85 Enterprise, Suite 430,
Aliso Viejo, CA 92656, U.S.A.
TEL: 1-949-425-0707
FAX: 1-949-425-0708

Kyowa Pharmaceutical, Inc.
212 Carnegie Center, Suite 101,
Princeton, NJ 08540, U.S.A.
TEL: 1-609-919-1100
FAX: 1-609-919-1111

BioWa, Inc.
212 Carnegie Center, Suite 101,
Princeton, NJ 08540, U.S.A.
TEL: 1-609-580-7500
FAX: 1-609-919-1108

Select Supplements, Inc.
5800 Newton Drive,
Carlsbad, CA 92008, U.S.A.
TEL: 1-760-431-7509
FAX: 1-760-804-8073

EUROPE

Kyowa Hakko Europe GmbH
Immermannstrasse. 3,
D-40210, Düsseldorf, Germany
TEL: 49-211-17-728-0
FAX: 49-211-17-728-41

Kyowa Hakko U.K. Ltd.
258 Bath Road, Slough,
Berkshire SL1 4DX, United Kingdom
TEL: 44-1753-566000
FAX: 44-1753-566010

Kyowa Italiana Farmaceutici S.R.L.
Viale Fulvio Testi 280, 20126, Milano, Italy
TEL: 39-02-644-704-1
FAX: 39-02-644-704-44

Kyowa Hakko Kogyo Co., Ltd.
Hungary Direct Commercial Representative Office
H-1022 Budapest II Bég utca. 3-5,
1st Floor, Hungary
TEL: 36-1-212-0645
FAX: 36-1-212-0644

Agroferm Hungarian-Japanese Fermentation Industry Ltd. (Agroferm)
Budapest Office
H-1022 Budapest II Bég utca. 3-5,
1st Floor, Hungary
TEL: 36-1-212-0645
FAX: 36-1-212-0644

Kaba Plant
H-4183 Kaba, Nádudvari útfél, Hungary
TEL: 36-54-480-560
FAX: 36-54-480-528

ASIA

Kyowa Hakko Industry (Singapore) Pte Ltd.
260 Orchard Road, #12-04,
The Heeren, Singapore 238855
TEL: 65-733-4948
FAX: 65-733-0819

Kyowa Hakko (Thailand) Ltd.
101/11 Srinakarintra Road,
Suanluang Praves, Bangkok 10250, Thailand
TEL: 66-2-321-9387
FAX: 66-2-321-9389

Kyowa Hakko (Malaysia) SDN BHD.
20, Jalan SS 19/5, 47500 Subang Jaya,
Selangor, Darul Ehsan, Malaysia
TEL: 60-3-5734-0669
FAX: 60-3-5734-0990

Kyowa Hakko Kogyo Co., Ltd.
Beijing Representative Office
100004, Beijing Fortune Bldg., Room 609,
No. 5, Dong San Huan Bei Lu,
Chao Yang District, Beijing,
People's Republic of China
TEL: 86-10-6590-8515
FAX: 86-10-6590-8517

Kyowa Hakko Kogyo Co., Ltd.
Shanghai Representative Office
1376 Nanjing Road West, Room 704,
Shanghai 200040,
People's Republic of China
TEL: 86-21-6279-8310
FAX: 86-21-6279-8320

Kyowa Hakko (H.K.) Co., Ltd.
Room 2103, Hang Lung Centre,
2-20 Paterson Street, Causeway Bay,
Hong Kong, People's Republic of China
TEL: 852-2895-6795
FAX: 852-2576-6142, 2576-6191

Guangzhou Representative Office
Room 411, China Hotel Office Tower,
Liu Hua Road, Guangzhou 510015,
People's Republic of China
TEL: 86-20-8667-5381
FAX: 86-20-8667-5472

Shanghai Guan Sheng Yuan Kyowa Amino Acid Co., Ltd.
621 Yun Ling Donglu, Shanghai 200062,
People's Republic of China
TEL: 86-21-5280-1270
FAX: 86-21-5280-3162

Kyowa Pharmaceutical (H.K.) Co., Ltd.
Room 2103, Hang Lung Centre,
2-20 Paterson Street, Causeway Bay,
Hong Kong, People's Republic of China
TEL: 852-2895-6795
FAX: 852-2576-6142

Wuxi Xiehe Food Co., Ltd.
No. 158 Xu Xiang Lane, Li Yuan,
Wuxi 214072, People's Republic of China
TEL: 86-51-0512-9781
FAX: 86-51-0510-9484

Yantai Kyowa Foods Co., Ltd.
Zhao Wang Zhuang Town, Laiyang City,
Shangdong 265225, People's Republic of China
TEL: 86-535-761-5778
FAX: 86-535-761-1787

PRINCIPAL PRODUCTS

PHARMACEUTICALS

Antibiotics
Pasetocin®, Fortimicin®, Sagamicin®, Minostacin

Anticancer Agents
Mitomycin, 5-FU, Leunase®, Adriacin®, Hysron® H-200, Dacarbazine, Farmorubicin®, Platosin®, Navelbine®

Central Nervous System Agents
Depakene®, EC-Doparl, Doparl®, Benozil®, Neoperidol®

Cardiovascular Agents
Meditrans® tape, Inovan®, Apiracohl®, Coniel®, Pre Dopa®, Dobupum™

Contrast Medium
Imagenil®

Gastrointestinal Agents
Nauzelin®, Glumin®, Glumal®, Navoban®

Antiallergic Agents
Allelock®, Celtect®

Hormones
Desmopressin, Hysron®

Vitamins
Vitaroxin®

Other Metabolic Agents
Gludiase®, ATP Kyowa, Activacin®

Agents for Blood and Fluid Disorders
Neu-up®, Emeradole®, Leukoprol®

Ointment
Propaderm®

Antimycological Agent
Itrizole®

Transdermal Analgesic Agent
Durotep® Patch

Diagnostic Medical Devices
Clinical Chemistry Diagnostic Reagents (Determiner® HDL-C), Immunological Reagents (Determiner® HbA1c, Chemilumi series, Allegro Lite series), Controls (Infectrol, Accurun series), Full Auto Micro Plate EIA Analyzer (AP series), Fecal Occult Blood Test Analyzer (HM-JACK® plus), Diabetes Mellitus Test Analyzer (DM-JACK®)

BIO-CHEMICALS

Fine Chemicals for Pharmaceutical and Industrial Use
Amino Acids (L-Alanine, L-Arginine, L-Histidine, L-Isoleucine, L-Ornithine, L-Aspartate, L-Proline, L-Serine, L-Threonine, L-Valine, etc.), Nucleic Acids (ATP, Orotic Acid, etc.), L-Malic Acid, Enzymes, Sodium hyaluronate

Bulk Pharmaceuticals
Citicoline, Dacarbazine, Minocycline HCl, Ubidecarenone (CoQ10)

Agrochemicals
Plant growth regulators (Gibberellin, Fulmet®)

Animal Health Products
Nanaomycin, Polyup®, Atomolate®, Benesal®, Lysozyme chloride for pisciculture, Fantacin® for pisciculture, Ampicirin for pisciculture

Amino Acids for Feed Use
L-Lysine HCl, L-Tryptophan, L-Threonine, L-Arginine, L-Valine

Feeds and Feed Additives for Fish and Animals
Evian® Kyowa, Fry Feed Kyowa, Aminoplus®, Driselase®, Phytase

Pet Care Products
Elendaite®, E&D shampoo and rinse, Amino Glutamine Kyowa (H), Green Mussel E

CHEMICALS

Solvents
Butyl Alcohol, Acetone, Butyl Glycol Ether, Ethyl Acetate, Butyl Acetate, PM (Propylene Glycol Monomethyl Ether)

Plasticizers and Their Raw Materials
DOP (Di-2-Ethylhexyl Phthalate), DINP (Di-Isononyl Phthalate), DIDP (Di-Isodecyl Phthalate), 2-Ethylhexyl Alcohol, Oxocol® 900 (Isononyl Alcohol)

Organic Acids
Acetic Acid, 2-Ethyl Hexanoic Acid, Isononanoic Acid

Diols
1-3 Butylene Glycol, 2,4-Di-Ethyl-1,5 Pentanediol, Butyl Ethyl Propanediol

FOOD

Natural Seasonings
Hydrolyzed vegetable and animal proteins; Animal, vegetable, fish, shellfish, and yeast extracts; Soup stocks

Kokumi Seasonings
Simmerin®

Umami Seasonings
MSG (Monosodium glutamate), IMP (Sodium 5'-inosinate), WMP (Mix of IMP and Sodium 5'-guanylate)

Bakery Products and Ingredients
Baker's yeast, Prepared mixes, Baking improvers, Activated gluten, Fermented flavor enhancers

Health Foods*
Vitamins, Minerals, Carotenoids, Probiotics, Peptides, Remake series

Freeze-Dried Foods
Instant egg-drop soup, Various food materials

Raw Material Alcohol*
For use in refined sake, For use in food preservatives and disinfectants

** Effective April 1, 2004, these products have been transferred to the Bio-Chemicals segment.*

DIRECTORS AND OFFICERS

(As of June 29, 2004)

BOARD OF DIRECTORS

Chairman and Chief Executive Officer
Tadashi Hirata[1]

President and Chief Operating Officer
Yuzuru Matsuda [1, 2]

Senior Managing Directors
Toru Doiuchi [2]

Yoshito Imai [2]
Company President, Pharmaceuticals Company

Managing Directors
Sadao Teshiba [2]

Tomonori Yuji [2]
Company President, Bio-Chemicals Company

Kazuhiko Yamanoe [2]

Nobuo Kanda [2]

Corporate Auditors
Takeshi Asaoka

Masahiro Kawaguchi

Akira Taniguchi

Kozo Fujita

Notes: 1. Representative Director
2. Also serving as Executive Officer

EXECUTIVE OFFICERS

Senior Executive Officers
Fumio Suzuki

Noriyuki Hina

Hiroyuki Kuniyasu

Executive Officers
Shinzo Ishii

Kyozo Tsuchiya

Shin Kawahara

Toshifumi Asada

Shoji Hari
President and Chief Executive Officer, Kyowa Hakko Chemical Co., Ltd.

Yukinobu Kotani

Yutaka Yoshida

Kenichi Fukuhara

Fumio Norimatsu
Company President, Food Company

Masaji Kasai

Yoshiki Tsunekane

CORPORATE DATA

(As of March 31, 2004)

KYOWA HAKKO KOGYO CO., LTD.

Head Office
1-6-1, Otemachi, Chiyoda-ku,
Tokyo 100-8185, Japan
TEL: 81-3-3282-0007
FAX: 81-3-3284-1968
URL: http://www.kyowa.co.jp/

Number of Employees
6,294 [Parent Company: 4,372]

Date of Foundation
July 1, 1949

Paid-in Capital
¥26,745 million

Principal Plants
Domestic
Hofu, Ube, Sakai, Fuji, Tsuchiura
Kyowa Yuka (Yokkaichi, Chiba), Kyowa Medex (Fuji)
Overseas
Biokyowa (U.S.A.), Agroferm (Hungary)

Principal Laboratories
Tokyo Research Laboratories
Pharmaceutical Research Institute
Technical Research Laboratories
Toxicological Research Laboratories
Sakai Research Laboratories
Foods Research Laboratories
Tsukuba Research Laboratories
Aquaculture Research Laboratories
Kyowa Yuka Co., Ltd., Yokkaichi Research Laboratories
Kyowa Medex Co., Ltd., Research Laboratories

INVESTOR INFORMATION

(As of March 31, 2004)

Stock Listings
Tokyo, Osaka, Nagoya, Fukuoka, and Sapporo

Securities Code Number
4151

Transfer Agent of Common Stock
The Chuo Mitsui Trust and Banking Company, Limited
33-1, Shiba 3-chome, Minato-ku, Tokyo 105-8574, Japan

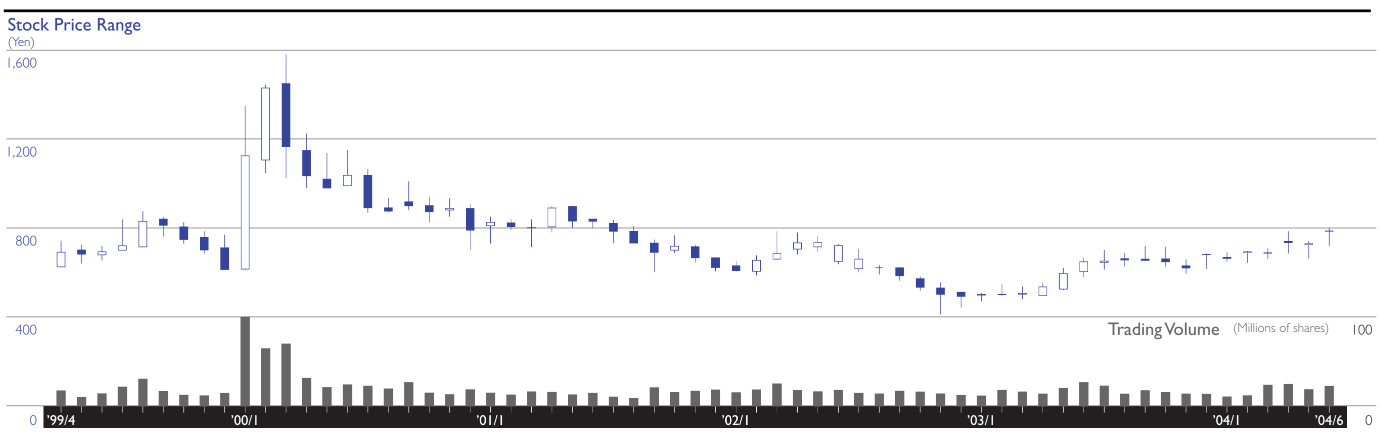
Number of Shares of Common Stock
Authorized: 987,900,000
Issued: 434,243,555

Number of Shareholders
80,708

Principal Shareholders

	Number of Shares Held (Thousands)	Percentage of Total Shares Issued
The Master Trust Bank of Japan, Ltd. (Trust account)	38,413	8.84%
The Dai-ichi Life Mutual Insurance Co.	35,230	8.11
Japan Trustee Services Bank, Ltd. (Trust account)	29,049	6.68
The Norinchukin Bank	18,083	4.16
NIPPONKOA Insurance Company, Limited	8,981	2.06
Mizuho Trust & Banking Co., Ltd. (Retirement Benefit Trust for Mizuho Bank, Ltd.)	8,075	1.85
Mizuho Bank, Ltd.	7,126	1.64
Kyowa Fund	5,351	1.23
Kyowa Hakko Kogyo Co., Ltd., Employee Stock Ownership Association	5,313	1.22
SOMPO JAPAN INSURANCE INC.	5,296	1.21

Stock Price



KYOWA HAKKO KOGYO CO., LTD.
1-6-1, Otemachi, Chiyoda-ku, Tokyo 100-8185, Japan
TEL: 81-3-3282-0007
FAX: 81-3-3284-1968
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This report is printed on recycled paper using Non-VOC (non-volatile organic compound) ink for waterless printing.

Printed in Japan
July 2004