KYOWA HAKKO

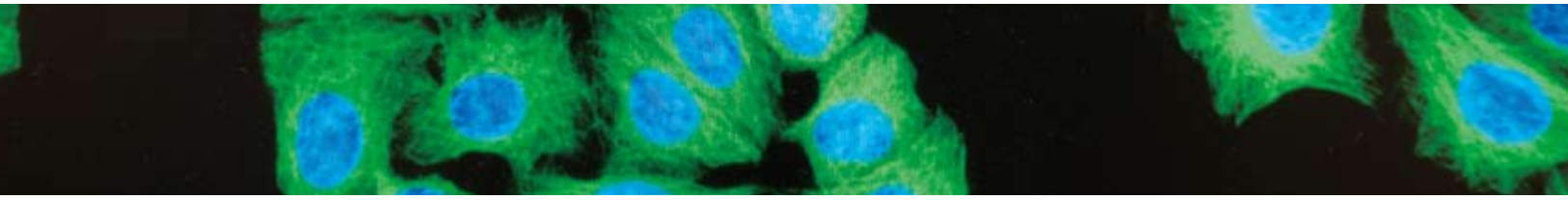
In the Vanguard of the Life Sciences Revolution

ANNUAL REPORT 2007

Year ended March 31, 2007

KYOWA HAKKO KOGYO CO., LTD. Annual Report 2007

Kyowa Hakko Kogyo Co., Ltd., is an R&D-based company with special strengths in biotechnology. The Company is dedicated to the creation of new value in the life sciences, especially in its core business segments of Pharmaceuticals and Bio-Chemicals, and strives to contribute to the health and well-being of people around the world.



In Pharmaceuticals, since contributing to the eradication of tuberculosis in Japan with the introduction of streptomycin and developing Mitomycin C, now a leading cancer chemotherapy agent, the Company has actively engaged in the R&D, production, and sale of pharmaceuticals that address needs in such areas as cancer, allergies, and hypertension.

In Bio-Chemicals, Kyowa Hakko is a global leader in fermented bulk products, such as amino acids and nucleic acids developed with biotechnology.

The Company's Chemicals operations are expanding lineups of specialty chemicals that contribute to environmental conservation.

Kyowa Hakko's Food operations draw on the Company's fermentation and other original technologies to differentiate the Company from competitors in the development of food ingredients, especially natural seasonings.

Note to Performance Forecasts

Forecasts contained in the Annual Report 2007 represent judgments based on information available as of June 20, 2007. It should be noted that there is a possibility that actual results could differ significantly due to such factors as exchange rate fluctuations.

CONTENTS

2 Financial Highlights

3 **To Our Shareholders**

In the fiscal year ended March 2007, our net sales and operating income exceeded initial plans by substantial margins. At the same time, our aggressive investment in therapeutic antibodies and other drivers of future growth are steadily showing results.

11 Special Feature:

In the Vanguard of the Life Sciences Revolution

Kyowa Hakko is dedicated to supporting advances in the life sciences through cutting-edge biotechnology, based on its original fermentation technologies.

For further details on those pioneering initiatives, see page 11 >>

19 Review of Operations
At a Glance
• Pharmaceuticals • Bio-Chemicals • Chemicals • Food

30 Intellectual Property

32 Corporate Social Responsibility

35 Corporate Governance

38 Management Members

39 Financial Section
• Eleven-Year Selected Financial Data
• Management's Discussion and Analysis
• Risk Factors
• Consolidated Financial Statements and Notes
• Report of Independent Auditors

77 Principal Subsidiaries and Affiliates

78 Overseas Network

79 Principal Products

80 Corporate Data

80 Investor Information

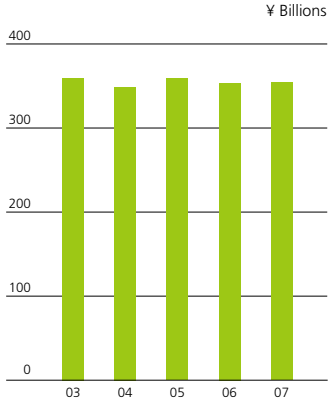
FINANCIAL HIGHLIGHTS

KYOWA HAKKO KOGYO CO., LTD. AND ITS CONSOLIDATED SUBSIDIARIES
For the years ended March 31, 2007, 2006 and 2005

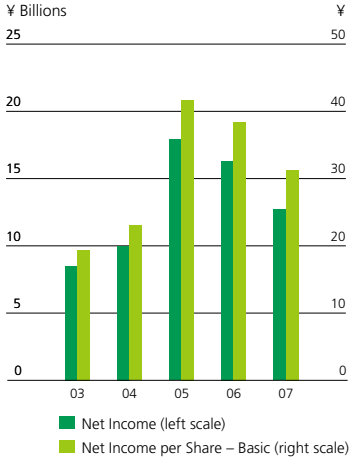
	Millions of Yen			Thousands of U.S. Dollars[1]
	2007	2006	2005	2007
For the Year:				
Net sales	¥354,274	¥353,440	¥358,963	$3,000,034
Operating income	30,699	25,535	33,507	259,963
Net income	12,694	16,273	17,932	107,494
Capital expenditures	14,498	10,859	7,647	122,771
Depreciation and amortization	10,006	9,789	10,565	84,732
R&D expenses	33,342	32,876	28,762	282,344
At Year-End:				
Total assets	¥378,871	¥384,381	¥374,493	$3,208,324
Interest-bearing debt	13,137	12,216	12,193	111,246
Total shareholders' equity[2]	220,427	232,621	235,439	1,866,601
Total net assets	244,082	257,491	—	2,066,915
		Yen		U.S. Dollars[1]
Per Share Data:				
Net income — basic[3]	¥ 31.3	¥ 38.4	¥ 41.7	$0.265
Total net assets	607.5	604.9	556.3	5.144
Cash dividends	10.0	10.0	10.0	0.085
		%		
Ratios:				
Return on assets (ROA)	3.33	4.29	4.88	
Return on equity (ROE)	5.10	6.63	7.79	

1. U.S. dollar amounts are translated from Japanese yen, for convenience only, at the rate of ¥118.09=US$1, the approximate exchange rate at March 31, 2007.
2. Due to a change in accounting standards, figures for total shareholders' equity in the years ended March 31, 2007 and 2006, have been restated.
3. 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.

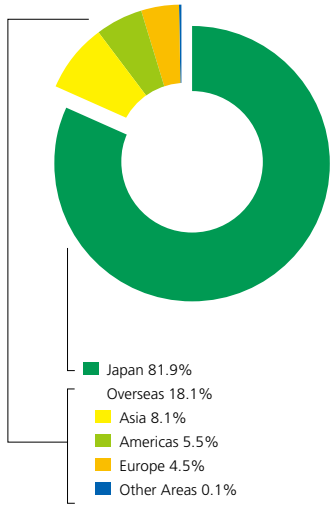
Net Sales



Net Income/ Net Income per Share



Sales Composition by Geographic Area



Yuzuru Matsuda President and Chief Executive Officer

In the second year of the Ninth Medium-Term Management Plan, both net sales and operating income exceeded initial targets by substantial margins.

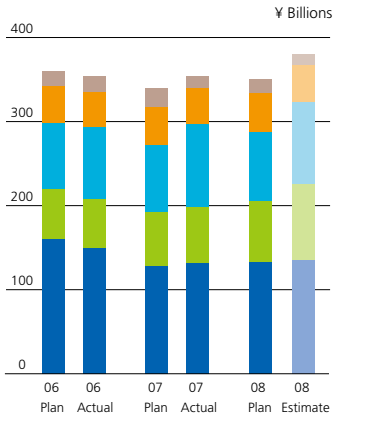
OPERATING ENVIRONMENT AND PERFORMANCE

The domestic economy is on a course of recovery, while conditions in Pharmaceuticals operations are becoming more challenging. In April 2006, National Health Insurance (NHI) official drug prices were reduced by an industrywide average of 6.7%. In addition, with aggressive inroads being made by European and U.S. pharmaceutical companies and the market for generics expanding, competition among companies continued to intensify on a global scale. In Bio-Chemicals operations, the prices of raw materials and fuel increased, while price competition in amino acids escalated in Japan and overseas. As a result, market conditions remained difficult. Chemicals operations were affected by the price of crude oil, and market conditions in Japan and overseas were marked by high prices overall. In Food operations, accompanying the diversification of consumers' food preferences, the ability to respond rapidly to changes in the market structure has become essential.

In this setting, the Group, in accordance with the Ninth Medium-Term Management Plan and its fundamental policy of "growth and development," conducted aggressive, future-oriented investment and worked to bolster competitiveness with strategic sales promotion measures and comprehensive cost reduction initiatives.

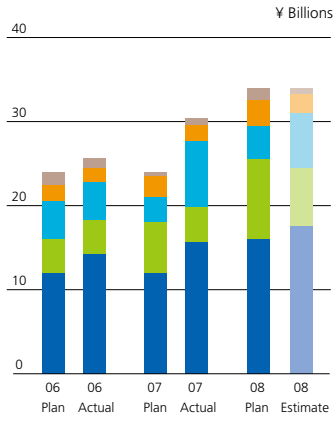
As a result, in fiscal 2007, ended March 31, 2007 — the second year of the Ninth Medium-Term Management Plan — net sales and operating income exceeded initial targets. Net sales were up 0.2% from the previous fiscal year, to ¥354.3 billion, and operating income increased 20.2%, to ¥30.7 billion. We recorded extraordinary losses, such as loss on sale of stock in related companies and impairment loss, and net income declined 22.0%, to ¥12.7 billion. Annual dividends in the year under review were ¥10.0 per share, unchanged from the previous fiscal year.

Sales Targets by Segment

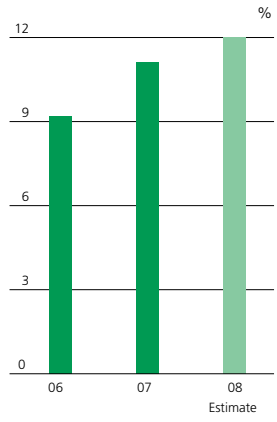


* Figures for Other include inter-segment transactions.

Operating Income Targets by Segment



Return on Invested Capital*



* Return on invested capital = operating income / total fixed assets + accounts receivables + inventories – trade payables

We have reinforced our earnings foundation with the introduction of the operating holding company system.

OPERATING HOLDING COMPANY SYSTEM IN PROGRESS

As in the previous year — the first year under the medium-term management plan — we exceeded the plan's targets in the year under review, the second year of the plan. The reasons for this performance included the introduction of the operating holding company system in April 2005, which has met our expectations.

Reflecting on the Group's results in previous years, we worked through a stage during which our core Pharmaceuticals operations provided our profits, while one of the other operations recorded operating losses for several consecutive years. To enhance this situation, we introduced the operating holding company system designed to make the Kyowa Hakko Group a more competitive enterprise. Specifically, we took steps to instill a sense of urgency regarding reforms among our employees; certain divisions were spun off as separate companies, and the others were restructured to operate independently within Kyowa Hakko. This way, each segment handled its own operations and worked to increase its competitiveness. This approach was communicated throughout the Group, from directors to employees. Thanks to the employees' understanding of the operating holding company system and their motivated work, we were able to boost our competitiveness in each field of operations and steadily generate profits in fields that had been operating at a loss.

Despite a reduction in NHI official drug prices, domestic sales were bolstered and core products recorded solid results.

PHARMACEUTICALS OPERATIONS

Bolstering Domestic Sales

In the year under review, major adverse factors included reductions in NHI drug prices and the termination of our distribution tie-up for the antifungal agent Itrizole®. However, the SMART (Sales and Marketing Transformation) Project took effect, and solid performances were recorded by such core products as Coniel®, an agent for treating hypertension and angina pectoris; Allelock®, an antiallergic agent; Durotep® Patch, an analgesic for persistent cancer pain; and Navelbine®, an anticancer agent. As a result, we were able to offset a portion

of the decline in sales brought about by the adverse factors mentioned above. In particular, Coniel® went off patent, and in July 2006 generic versions were placed on the market. Nevertheless, we stepped up our sales activities and recorded unit sales on a par with the level in the previous year, thereby minimizing the influence of the generics.

With the new patent for Potelligent® technology, our therapeutic antibody business has been substantially strengthened.

Therapeutic Antibody Business Expanded

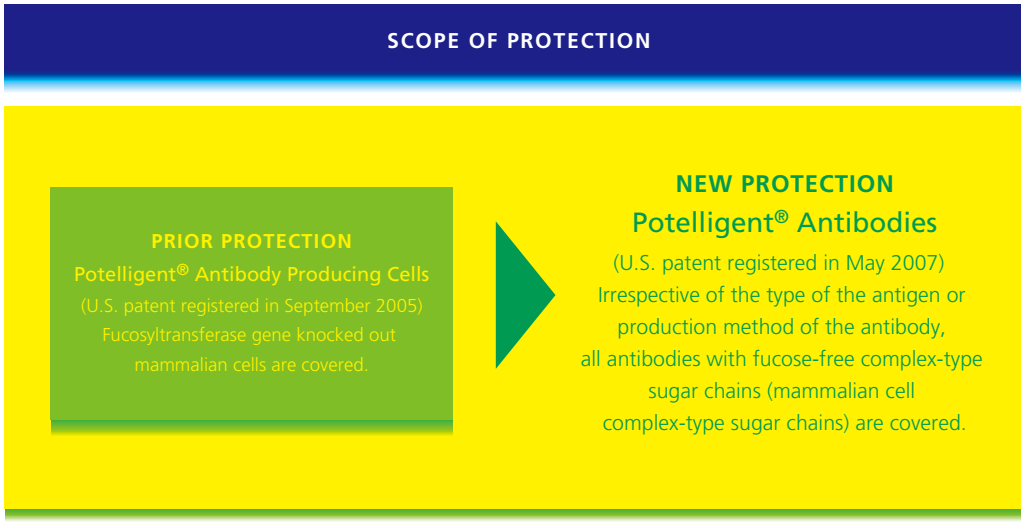
Our therapeutic antibody business is the focus of considerable attention. On a strong base of biotechnology, we have continued therapeutic antibody R&D since the early 1980s, and these efforts are bearing fruit. We have concluded licensing agreements for Potelligent® technology, our high antibody-dependent cellular cytotoxicity (ADCC) antibody production technology, with nine companies, including Genentech, Inc. and Takeda Pharmaceutical Company Limited. Moreover, we are currently in negotiations with more than five additional companies.

Activities undertaken in the year under review included the registration of a material patent for Potelligent® technology in May 2007 in the United States. This patent provides much greater coverage than the antibody production cell patent that was registered in September 2005 in the United States. The new patent covers all antibodies with fucose-free complex-type sugar chains, even if they are made with a new technology. This extended patent coverage has substantially strengthened our therapeutic antibody business strategies.

Regarding our therapeutic antibody pipeline, in December 2006 we licensed BIW-8405, which targets the interleukin-5 receptor (IL-5R) and is now in phase I clinical trials, to MedImmune, Inc., a leading U.S. biopharmaceutical company. BIW-8405 is an agent for treating asthma to which Potelligent® technology has been applied. KW-0761, which also uses Potelligent® technology, entered phase I clinical trials in England for seasonal allergic rhinitis in January 2006 and in Japan for hematologic cancer in February 2007.

Moreover, at the Fuji plant we are building facilities for the production of antibodies for clinical trials. In addition to establishing a foundation for the expansion of the therapeutic antibody business, we have followed up Potelligent® technology with the development of a new technology, Complegent™ high complement dependent cytotoxicity (CDC) antibody technology.

Potelligent® Technology: Significantly Stronger U.S. Patent Protection



We are working to maximize the value of our pipeline.

Antiparkinson Agent KW-6002: NDA Filed

In April 2007, we filed a New Drug Application (NDA) in the United States for the antiparkinson agent KW-6002 as adjunct therapy to levodopa. Since we do not have an international sales network, we need to enter into a tie-up with a company with such sales capabilities. When approval is confirmed and value is maximized, we will engage in alliance negotiations, including straight out-licensing.

In the United States, phase IIa clinical trials for KW-6002 as monotherapy for Parkinson's disease were completed. Based on our evaluation of such factors as the drug's commercial potential, we decided to put clinical trials on hold in the United States. Moreover, phase IIa trials for restless legs syndrome were concluded in the United States, but because efficacy was not clearly confirmed, development for this indication was discontinued.

Increasingly Active Licensing

In addition to licenses for Potelligent® technology, licensing activities involving our own development pipeline are accelerating. In December 2005, we licensed a mitotic kinesin Eg5 inhibitor to Eli Lilly and Company, of the United States, and clinical trials are expected to begin shortly. In September 2006, we licensed the anticancer agent KW-2401 (phase II) to Keryx Biopharmaceuticals, Inc., of the United States. In February 2007, we licensed the malignant melanoma treatment KW-2871 (phase I/IIa) to Life Science Pharmaceuticals, Inc., of the United States, and the therapeutic antibody BIW-8405 (phase I), which uses Potelligent® technology, to MedImmune, also of the United States.

Regarding our in-licensed products, in January 2007 we concluded a joint development and sales agreement with Zeria Pharmaceutical Co., Ltd., of Japan, for Asacol®, an agent for treating inflammatory bowel diseases, which is now in phase III clinical trials. In April 2007, we licensed the exclusive development and marketing rights for ARQ197 in Japan and certain other Asian countries from ArQule,Inc. ARQ 197 is an anticancer agent targeting solid tumors that has completed phase I trials in the United States.

Increased Out-Licensing and In-Licensing

	Code Name	Company	Stage	Remarks
Out-licensing	CEP-701	Cephalon	PC P1 P2 P3	Anticancer (acute myelocytic leukemia)
	KW-3902	NovaCardia	PC P1 P2 P3	Congestive heart failure, renal failure
	Eg5 inhibitor	Eli Lilly	PC	Mitotic kinesin Eg5 inhibitor
	KW-2401	Keryx Biopharmaceuticals	PC P1 P2	Anticancer
	KW-2871	Life Science Pharmaceuticals	PC P1 P2	Anticancer
	(Low-fucose antibody)			(malignant melanoma)
	BIW-8405 (Potelligent® antibody)	MedImmune	PC P1	IL-5R antibody
In-licensing	KW-6500	Britannia Pharmaceuticals	PC P1	Antiparkinson (injection)
	Z-206 (Asacol®)	Zeria Pharmaceutical	PC P1 P2 P3	Inflammatory bowel disease (Crohn's disease)
	ARQ 197	ArQule	PC	Anticancer

PC Preclinical P1 Phase I P2 Phase II P3 Phase III

Moreover, we continue to record growth in pharmaceutical exports and technology out-licensing revenues. Exports and royalty revenues of olopatadine hydrochloride, the active ingredient of the antiallergic agent Allelock®, are making substantial contributions to our results. Olopatadine hydrochloride has been licensed to Alcon Laboratories, Inc., of the United States, and the Alcon Group is marketing olopatadine hydrochloride as Patanol® eye drops around the world.

We are focusing on the development of new products and applications in the areas of pharmaceutical and industrial raw materials and health care products.

BIO-CHEMICALS OPERATIONS

Higher Sales of Raw Materials for Pharmaceutical and Industrial Use

Raw materials for pharmaceutical and industrial use — centered on amino acids, nucleic acids, and related compounds — recorded higher sales during the year, as demand increased overseas and domestic sales of raw materials for generic pharmaceutical products grew. We introduced innovative amino acid production technology at our U.S. production base, Biokyowa Inc., and worked to reduce costs. However, in addition to intensified price competition for amino acids in Japan and overseas, rises in the prices of raw materials and fuel put pressure on profits.

In health care operations, growth in sales of raw materials for health care products was slow, while overseas sales of amino acids for use in dietary supplements and domestic mail-order sales of the Remake® series lineup were strong. Overall, sales of health care products increased. In alcohol, sluggish conditions for raw material alcohol for use in alcoholic beverages continued, while industrial-use alcohol, which was deregulated in April 2006, recorded significant growth in sales volumes.

Focus on Fine Chemicals and Health Care Products

In the field of fine chemicals, which includes pharmaceutical raw materials and intermediates and industrial raw materials for such products as cosmetics, we are focusing on the development of new products and applications. In the health care business, coenzyme Q10 remains subject to intense price competition. Nevertheless, it remains an important part of our lineup of health care products, and we are working to build coenzyme Q10 into a strategic product over the medium-to-long term. In the domestic mail-order business, we devoted resources to sales promotions and worked aggressively to enhance sales. For example, through advertisements in newspapers and other media, we appealed to consumers about our brand value with the slogan, "Kyowa Hakko — Health Care Products You Can Trust." As a result, mail-order sales were favorable.

CHEMICALS OPERATIONS

Focus on Environment-Friendly Products and Other Specialty Chemicals

Strong demand supported an increase in domestic shipments, and, accompanying higher prices for crude oil and naphtha, raw material and fuel prices were up. In this setting, we raised the prices of core products, and substantial year-on-year sales gains were recorded. Despite a decline from the previous year in shipments, export sales increased due to higher prices overseas for raw materials for plasticizers and solvents.

Currently, we are focused on environment-friendly products and other specialty chemicals. If substitutes for chlorofluorocarbons (CFCs) — which destroy the ozone layer — are used in air-conditioning, freezing, and refrigeration equipment, there will be a need for a shift to lubricants that are compatible with CFC substitutes. The raw materials for these lubricants are

environment-friendly products, such as isononanoic acid and 2-ethyl hexanoic acid. We have an especially large share of the domestic market for these specialty chemicals. Over the past several years, we have increased our production capacity for isononanoic acid and 2-ethyl hexanoic acid.

FOOD OPERATIONS

Focus on Natural Seasonings for the Food Service Industry

With consumers' heightening concerns regarding food safety and stronger regulations, we are devoting our full attention to quality assurance. In such fields as natural seasonings, flavor enhancers, and baking improvers, we are focusing on the development of food ingredients that are differentiated through the use of original technologies, including fermentation and cooking-reactions technologies.

In the year under review, in natural seasonings, sales of brewed seasonings for food service markets increased, while higher sales were recorded by baker's yeast, flavor enhancers, and baking improvers, which are the core products in bakery products and ingredients. In December 2006, we began the operation of a new natural seasonings plant in Jiangyin, China.

Expected to generate real synergies with a seamless integration of fermentation and synthesis.

DAIICHI FINE CHEMICAL ACQUIRED

In June 2007, we acquired from Daiichi Sankyo Co., Ltd., all the stock of Daiichi Fine Chemical Co., Ltd., which became our subsidiary and offers advanced technologies in organic synthesis.

In Bio-Chemicals operations, we have positioned pharmaceutical-related operations, such as pharmaceutical raw materials and intermediates, as a high-value-added field. By combining our strengths in fermentation technologies and the chemical synthesis technologies of Daiichi Fine Chemical, we will be able to create products with further value added. In-house, we are describing this merger as the seamless integration of fermentation and synthesis technologies, and we have high expectations that the acquisition will successfully generate favorable results.

I have no interest in M&A activities that are implemented simply for the sake of increasing operational scale. I am, however, interested in M&A activities that create new opportunities that were not previously possible or significantly speed up the development process. The acquisition of Daiichi Fine Chemical is one of those cases, and I believe it will be a typical example of an acquisition through which both companies can benefit from each other's strengths, and synergies can be leveraged.

GLOBAL INTELLECTUAL PROPERTY STRATEGY

In 1956, we invented the world's first process for fermentation-based L-glutamic acid production. Since that time, we have accumulated a wide range of experience in intellectual property (IP) rights, and we have moved ahead of other companies in frameworks and systems for protecting such rights.

However, as we prepare for further worldwide operational development, our global IP strategy will become even more important. In April 2007, we filed an NDA for the antiparkinson agent KW-6002 in the United States, but we still do not have a substantial base of international experience in new drug development. Given the importance of rapidly establishing a global strategy for IP rights, we are taking steps to reinforce our system for actively strengthening our IP strategy, such as recruiting people with significant expertise in this field.

CORPORATE SOCIAL RESPONSIBILITY

I believe the essence of corporate social responsibility (CSR) stems from the particular way that society benefits from a company's activities. The founder of Kyowa Hakko introduced streptomycin, a treatment for tuberculosis, in Japan, investing three times the amount of capital that was used to start the Company. He took this risk because he was dedicated to eradicating tuberculosis in Japan, and today this attitude is a fundamental aspect of Kyowa Hakko's corporate culture.

Of course, CSR, in a limited sense, comprises regulatory compliance, protecting the environment, and integrity in business dealings. Companies must thoroughly implement corporate governance and information disclosure and conduct highly transparent and rigorously sound business management.

However, a company's CSR activities do not end at this point. What matters most is that the work that each employee is undertaking at a company and the products and services that are being provided are useful to society and integrated into the social framework.

RAISING CORPORATE VALUE AND EARNING THE TRUST OF STAKEHOLDERS

Prior to the lifting of the ban on triangular mergers, takeover countermeasures are currently under thorough discussions.

I believe the ultimate safeguard is to increase corporate value. Managers operate a company with the trust of shareholders, and the success or failure of a takeover bid depends upon whether shareholders choose current management or the proposal made by the takeover group. To be chosen to continue the operation of a company, managers must conduct management activities in a way that increases transparency and raises corporate value. I think it is most important for companies to earn the trust of all stakeholders, including shareholders, customers, employees, suppliers, and local communities, and to be recognized by them as an essential, integral part of society.

On track to achieving objectives for the final year of the Ninth Medium-Term Management Plan.

PROSPECTS FOR FISCAL YEAR ENDING MARCH 31, 2008

In the fiscal year ending March 31, 2008 — the final year of the Ninth Medium-Term Management Plan — we are forecasting net sales of ¥380.0 billion, operating income of ¥34.0 billion, and operating return on invested capital (ROIC) of 12.0%. In addition, due to the outsourcing of pharmaceutical distribution, we decided to sell the site of a distribution center, so we expect to record a gain on sale of land as extraordinary income. Overall, we are forecasting net income of ¥25.0 billion. As a result, we expect to meet all the targets set out for the final year of the management plan, which are net sales of¥350.0 billion, operating income of ¥34.0 billion, and ROIC of more than 12.0%.

In the fiscal year ending March 31, 2008, in accordance with the current medium-term management plan, we will continue to conduct aggressive investment targeting future growth, and we will steadily implement comprehensive cost reduction measures. Under this plan, we have targeted reductions of ¥5.0 billion in labor costs. In addition, we plan to cut another ¥5.0 billion by reevaluating various costs, including procurement expenses for raw materials and equipment and sales promotion expenses. Together, we are targeting comprehensive cost reductions of ¥10.0 billion. We are making favorable progress in these endeavors.

As an R&D-oriented company, R&D activities are one of our lifelines. Accordingly, in the fiscal year ending March 31, 2008, R&D expenses, including those associated with the introduction of new drugs, will likely increase ¥3.0 billion from the year under review, to ¥36.3 billion. Capital expenditures will rise ¥3.3 billion, to ¥17.6 billion.

STABLE DIVIDENDS AND CANCELLATION OF TREASURY STOCK

The provision of a return to shareholders is one of our top management priorities. Our basic policy is to maintain stable dividend payments, and at this point we are planning to maintain our annual dividends at ¥10.0 per share in the fiscal year ending March 31, 2008. Subsequently, we will reconsider our dividend policy at the same time as we formulate the Tenth Medium-Term Management Plan.

Moreover, in the fiscal year ended March 31, 2007, we acquired 24.6 million shares of treasury stock and retired 35.0 million shares. Progress in the retirement of shares is another choice that has merits for shareholders as it contributes to increasing shareholder value.

Return to Shareholders

Treasury Stock:

Purchased in accordance with resolutions of the Board of Directors and General Shareholders' Meeting			Retired to increase shareholder value
Fiscal 2004	2.6 million shares		
Fiscal 2005	7.0 million shares		
Fiscal 2007	24.6 million shares	Retired	35.0 million shares

Dividends per Share:

Maintained stable dividends			Increased from fiscal 2005	
Fiscal 2004	¥7.5	Increased	Fiscal 2005 to 2007	¥10.0

We are striving to be a life sciences company with the world's leading biotechnologies.

AIMING TO ACHIEVE OUR LONG-TERM VISION

I believe managers always need to look about 10 to 15 years into the future to make management decisions. In this sense, it is important to have a vision of a company's future position. Our long-term vision is to be a life sciences company with the world's leading biotechnologies. In other words, we will be different from pharmaceutical companies. Our operations will be centered on a base of biotechnology derived from fermentation, a traditional Japanese technology. Through pharmaceuticals and other products, we will strive to be a life sciences company that contributes to the health and well-being of people as well as a unique company that is needed by society around the world. To achieve this vision, we must take on a range of challenges, such as therapeutic antibodies, and we appreciate your understanding of these endeavors.

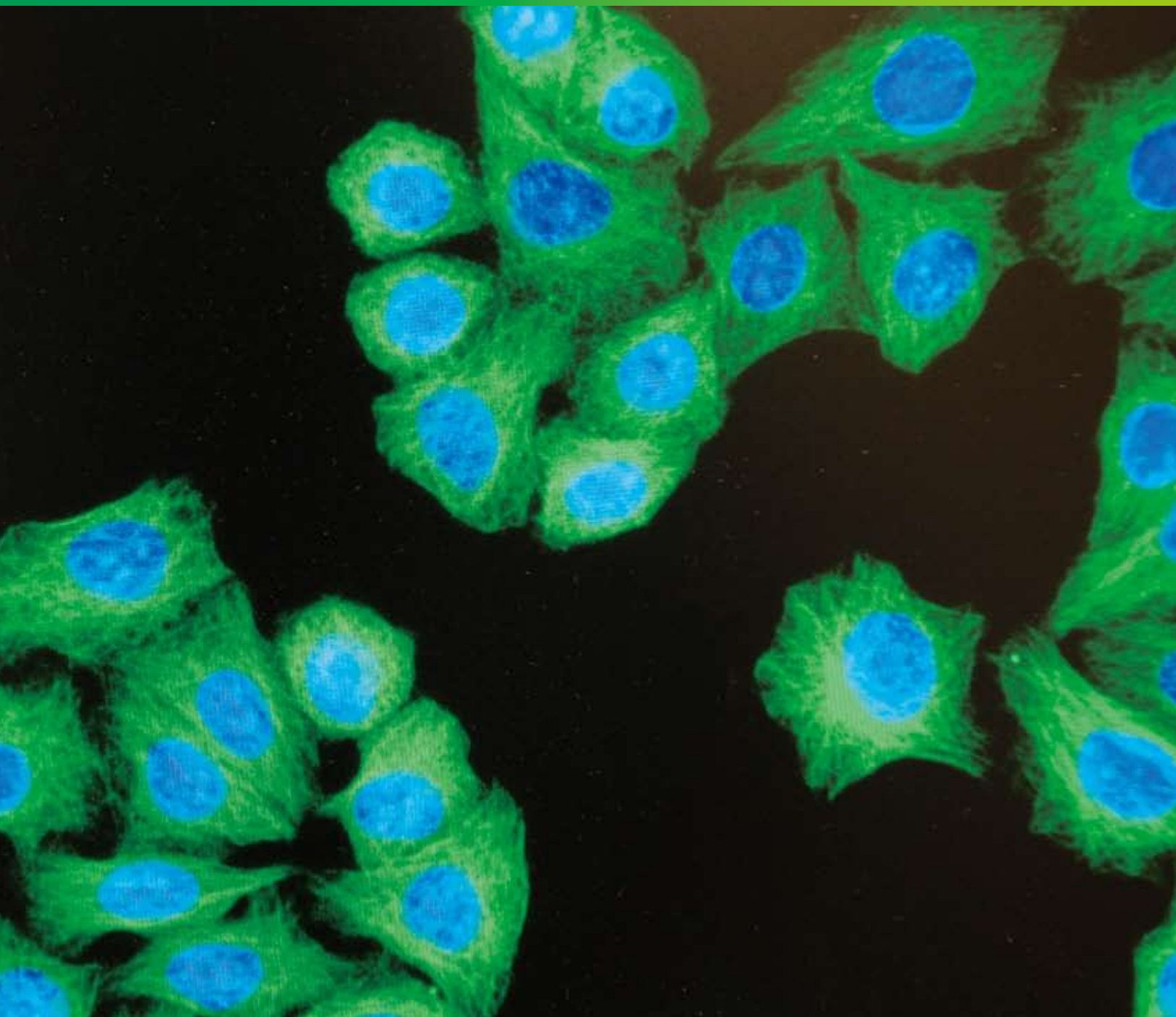
I would like to ask for your continued support in the years ahead.

June 20, 2007

President and Chief Executive Officer
Yuzuru Matsuda

Our Ninth Medium-Term Management Plan calls for building a foundation for future growth and development. As we approach the final year of the plan, major projects are making steady progress. In this section, we outline the progress we have made in three areas — the global development of Pharmaceuticals operations, the therapeutic antibody business, and targeting further growth in Bio-Chemicals operations.

In the Vanguard of the Life Sciences Revolution



Global Development of Pharmaceuticals Operations

BASIC POLICIES FOR NEW DRUG R&D

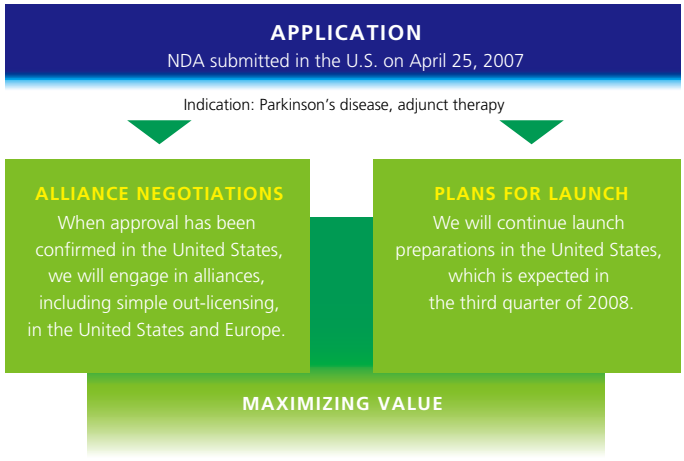
In the R&D of new drugs, Kyowa Hakko emphasizes the Proof of Concept (POC) Fast strategy. We strive to shorten the process from the discovery of original new drug candidates to phase IIa clinical trials, which first establish whether the drug has the expected efficacy in humans. This strategy enhances our competitiveness. By making the best choice among in-house development, out-licensing, and alliances, we endeavor to expand development opportunities and establish POC as rapidly as possible rather than overemphasize in-house development. In line with this policy, we licensed a mitotic kinesin Eg5 inhibitor, an anticancer drug candidate, to Eli Lilly and Company, of the United States, and the antibody KW-2871, which targets malignant melanoma, to Life Science Pharmaceuticals, Inc., also of the United States. After the POC of a new drug has been verified, for phase IIb clinical trials and subsequent stages we decide whether to pursue in-house development and file a New Drug Application (NDA), out-license the compound, or conduct joint development with another company. In making this decision, we look to maximize value based on a thorough analysis of our entire new drug development pipeline.

Moreover, in accordance with our policy of initially developing new drugs overseas to implement the POC Fast strategy, we have established three overseas bases — Kyowa Pharmaceutical, Inc., in Princeton, New Jersey, in the United States; Kyowa Hakko U.K. Ltd., in Slough, Berkshire, near London, in the United Kingdom; and a representative office in Beijing, China. We are conducting clinical development in the United States, Europe, and China.

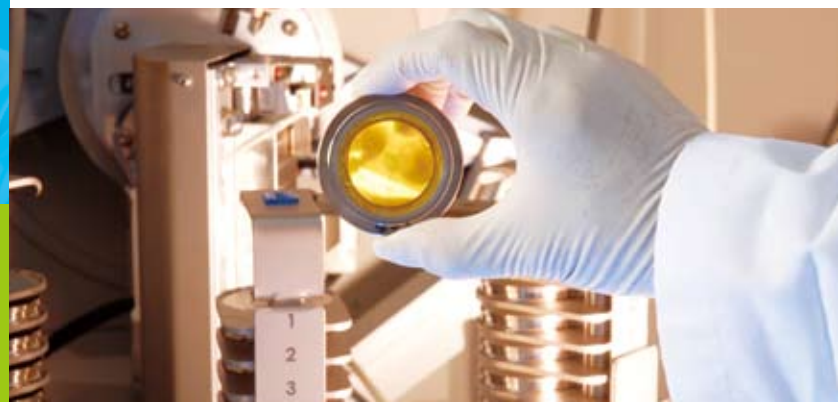
PROGRESS WITH KEY CANDIDATE DRUGS

KW-6002 KW-6002 is the world's first selective adenosine A2A receptor antagonist. We completed phase III clinical trials for KW-6002 as a treatment for Parkinson's disease in the United States and Europe, and in April 2007 we filed an NDA in the United States. When it is used as adjunct therapy to levodopa, KW-6002's effectiveness in improving the wearing-off phenomenon and motor function has been confirmed. Our objective is to acquire approval in 2008. To maximize the drug's value after approval has been acquired, we will engage in alliances, including straight out-licensing, while moving forward with preparations for the launch of this drug in the United States. In Japan, phase IIa trials of KW-6002 as adjunct therapy to levodopa were concluded in 2006, and currently phase IIb trials are under way. In the United States, phase IIa clinical trials for KW-6002 as monotherapy for Parkinson's disease were completed. Based on our evaluation of such factors as its commercial potential, we decided in April 2007 to suspend

KW-6002: Maximizing Value



In the Vanguard of
the Life Sciences Revolution



the clinical development of KW-6002 as monotherapy in the United States. Moreover, phase IIa trials for restless legs syndrome were concluded in the United States; however, efficacy was not clearly confirmed, so development for this indication was discontinued in January 2007.

KW-2871 KW-2871 is a monoclonal antibody that binds specifically to the GD3 cell surface antigen, which is expressed in about 90% of malignant melanoma cells. In the United States, phase I/II trials of KW-2871 as a therapeutic antibody that targets malignant melanoma cells were concluded. In February 2007, to maximize its value, we licensed KW-2871 to Life Science Pharmaceuticals, of the United States. In the future, through Life Science Pharmaceuticals, development will be conducted at the Ludwig Institute for Cancer Research and the University of Pittsburgh, in the United States, which are known for leading-edge research into malignant melanoma therapies. As a result, we anticipate that the time to the filing of its NDA and its launch will be shortened.

KW-0761 KW-0761 is a humanized monoclonal antibody for CC chemokine receptor 4 (CCR4) selectively expressed in T-helper type 2 (Th2) cells and other cells. Phase I clinical trials of KW-0761 as an agent for treating allergic disorders are currently under way in Europe. In Japan, KW-0761 is in phase I trials for malignant tumors (hematologic cancer), in which CCR4 is highly expressed.

KW-2449 KW-2449 is a compound that inhibits multiple kinases, such as FMS-like tyrosine kinase 3 (FLT-3), which is known as a poor prognostic factor expressed in many acute myeloid leukemia (AML) patients. It also inhibits Aurora kinases. Consequently, KW-2449 is expected to have a unique action against cancer. Target indications include not only hematologic malignancies, such as AML and chronic myeloid leukemia (CML), but also solid tumors. Currently, KW-2449 is in phase I trials in the United States.

KW-2478 Starting with a compound obtained through microbial screening, KW-2478 was designed by taking advantage of our organic synthesis and X-ray crystallography technologies. A compound with a new type of anticancer action, KW-2478 inhibits the functions of heat shock protein 90 (Hsp90) client proteins and induces the degradation of these proteins, which are involved in the survival, unlimited growth, metastasis, and other processes of cancer cells. Target indications are expected to include myeloma and lymphoma as well as solid tumors. Currently, KW-2478 is in phase I trials in Europe.

BUSINESS DEVELOPMENT IN CHINA

Currently, we are focusing efforts on marketing Coniel®, an agent for treating hypertension that was launched in December 2004. Phase III clinical trials are currently under way for the antiallergic agent Allelock® and for an additional indication of angina pectoris for Coniel®. We plan to file an application for this additional indication for Coniel® in summer 2007. In April 2006, we opened a production facility in the Suzhou Industrial Park in Jiangsu Province, China. In preparation for the production of such products as Allelock® and Coniel® for sale in China, we are conducting validation and other procedures required to begin the plant's operation.

Therapeutic Antibody Business

To maximize the value of Potelligent® technology — a highly competitive technology that was originally developed at the BioFrontier Laboratories — we will implement the following three strategies and expand our business. First, through BioWa, Inc., which we established in the United States, we will aggressively out-license Potelligent® technology. Second, we will conduct the clinical development of Potelligent® antibodies discovered by Kyowa Hakko. Presently, the clinical development of BIW-8405 and KW-0761, which were produced using this technology, are making steady progress. In the future, we expect the safety and efficacy of Potelligent®-enhanced antibodies to be confirmed in clinical studies. Third, we will conduct collaborative R&D with other companies. We will create unique antibodies that will be capable of fulfilling unmet medical needs by combining Potelligent® technology with promising antibodies from other companies. Primarily at the antibody research laboratories in the BioFrontier Laboratories, research for a number of antibodies is moving forward following KW-0761 and BIW-8405. In this setting, we formally decided in April 2006 to build a new therapeutic antibody production facility that is compliant with Good Manufacturing Practices (GMPs). The construction of this facility began in January 2007 at the Fuji plant, while completion is scheduled for the end of 2008, and operations are to begin in the first quarter of 2009. We expect the start-up of the therapeutic antibody production facility will increase the number of antibodies proceeding to clinical development and accelerate the enhancement of our pipeline.

Antibody Pipeline

Category	Code Name	Target	Antibody	Indications	Preclinical	Phase I	Phase II
Antiallergic	KW-0761[1]	CCR4	Humanized monoclonal	Allergic disorders	PC	P1	
Anticancer	KW-0761[1]	CCR4	Humanized monoclonal	T-cell lymphoma	PC	P1	
Anticancer	Undisclosed[1]	Tumor antigen	Humanized monoclonal	Solid tumor	PC		
Anticancer	Undisclosed[1]	Tumor antigen	Humanized monoclonal	Hematologic and solid tumors	PC		
Antiallergic	BIW-8405[1, 2]	IL-5 receptor	Humanized monoclonal	Asthma	PC	P1	
Anticancer	BIW-8962[1, 3]	Ganglioside GM2	Humanized monoclonal	Lung cancer, glioblastoma	PC		
Anticancer	BIW-8556[1, 3]	VEGF-R/FLT-1	Humanized monoclonal	Breast and colon cancers	PC		
Anticancer	BIW-8137[1, 3]	Ganglioside GD2	Humanized monoclonal	Solid tumor	PC		
Anticancer	BIW-7034[3]	FGF8	Humanized monoclonal	Prostate, breast, and ovary cancers	PC		

1. Potelligent® technology applied
2. Out-licensed to MedImmune in December 2006
3. Development conducted by BioWa

In the Vanguard of
the Life Sciences Revolution

STEPPING UP POTELLIGENT® LICENSING AT BIOWA

Since its founding as a U.S. subsidiary in February 2003, BioWa has aggressively licensed Potelligent® technology. In October 2005, following the issuance of a patent covering Potelligent® antibody producing cells, BioWa stepped up licensing efforts and granted licenses to MedImmune, Inc., a leading U.S. biopharmaceutical company; Igeneon GmbH, a wholly owned subsidiary of Aphton Corporation; and Genentech, Inc. We licensed to UCB in the year under review and to Takeda Pharmaceutical Company Limited in May 2007, for a total of nine companies, two of which have not been disclosed. Currently, we are conducting licensing negotiations with more than five additional pharmaceutical companies. In addition, in May 2007 a U.S. patent was issued that covers all antibodies with fucose-free complex-type sugar chains (mammalian cell complex-type sugar chains), irrespective of the type or production method of the antigen. With this patent, a license from BioWa will be indispensable in commercializing Potelligent® antibodies, regardless of the production method or the type of antigen. In the R&D of Potelligent® antibodies, the exclusive position of Kyowa Hakko and BioWa will be substantially strengthened.

In addition to simply granting licenses for Potelligent® technology, BioWa has been undertaking collaborative alliances to jointly develop therapeutic monoclonal antibodies with other companies since 2004. These initiatives combine bio-venture companies that have promising antigens or antibodies for the treatment of cancer and allergic inflammation and BioWa's Potelligent® technology. BioWa is presently in negotiations with several bio-venture companies.

In 2005, Kyowa Hakko licensed a humanized anti-IL-5R antibody to BioWa that has the potential to become an innovative treatment for asthma. The development of the antibody by BioWa's development team, which was established in March 2005, proceeded smoothly, resulting in the successful submission of an Investigational New Drug Application (IND) to the FDA in the United States in June 2006, followed by the commencement of phase I clinical trials. In December 2006, we licensed worldwide development and marketing rights, excluding Japan and certain other Asian countries, to MedImmune. BioWa will receive an upfront payment, milestone payments at various stages of development, and royalties from MedImmune. Through the licensing to MedImmune, the clinical development and commercialization of humanized anti-IL-5R antibodies in the United States will be accelerated thanks to MedImmune's strong track record in these areas.

Licensees of Potelligent® Technology

(As of May 2007)

OUT-LICENSED TO NINE COMPANIES

- Genentech
- Biogen Idec
- Igeneon*
- MedImmune
- Medarex
- UCB
- Takeda

Plus two other undisclosed contracts

* A wholly owned subsidiary of Aphton Corporation in the United States

BOLSTERING THERAPEUTIC ANTIBODY DEVELOPMENT

The market for therapeutic antibodies continues to record rapid growth. The scale of the global market has reached approximately ¥1.4 trillion, and it is expected to reach about ¥3.3 trillion by 2010. Aiming to launch products in this high-potential market, in 2006 we began the clinical development of KW-0761, a humanized monoclonal anti-CCR4 antibody. KW-0761, developed using Potelligent® technology, will be able to eliminate cells expressing CCR4 through antibody-dependent cellular cytotoxicity (ADCC). Possible indications for KW-0761 include diseases in which cells have high expression of CCR4, the target. CCR4 is highly expressed in Th2 cells, which produce a variety of cytokines involved in the inflammatory process, such as IL-4 and IL-5. Clinical development will proceed with indications for seasonal and year-round allergic rhinitis, atopic dermatitis, and bronchial asthma. Currently, KW-0761 is in phase I clinical trials in Europe. In Japan, KW-0761 is in phase I clinical trials for the indications of adult T-cell leukemia/lymphoma (ATLL) and peripheral T-cell lymphoma (PTCL), since CCR4 is highly expressed in ATLL and PTCL cells as well.

Similar to ADCC, complement dependent cytotoxicity (CDC) plays an important role in the pharmacological effects of therapeutic antibodies. To follow up on its Potelligent® high ADCC antibody technology, Kyowa Hakko has developed Complegent™ high CDC antibody technology. While Potelligent® technology increases ADCC activity more than 100 times through the removal of fucose from an antibody, the recently developed Complegent™ technology increases CDC activity more than 10 times through the chimerization of Fc chains of IgG1 and IgG3. The combination of Potelligent® technology and Complegent™ technology has the potential to simultaneously boost ADCC activity and CDC activity.

In the future, we will further bolster our efforts to strengthen our antibody pipeline and promote our licensing business using both technologies.

Targeting Further Growth in Bio-Chemicals Operations

FINE CHEMICALS

In the year under review, we recorded substantial growth in amino acids for pharmaceutical raw materials for use in such products as infusions. This growth demonstrates the depth of customer support for our safe, high-quality fermented materials. To achieve sustained growth in line with customer satisfaction, we will focus on the following points.

First, our priorities are safety and high quality. Shanghai Kyowa Amino Acid Co., Ltd., which has completed a new plant in Shanghai, has started to supply markets around the world with finished amino acid products made at the plant, which meets global GMP standards. We will also work to enhance quality assurance systems at other plants.

A stable supply of products at reasonable prices is indispensable to customer satisfaction. Accordingly, we will accelerate our research in such areas as the improvement of microbial strains, fermentation processes, and engineering analyses of equipment to facilitate efficient production at plants around the world. Examples of these measures include the introduction of new technology and laborsaving initiatives at Biokyowa Inc., in the U.S. state of Missouri.

Since we did not have a synthesis division, in the past we were unable to adequately meet some customer requests, such as those for increased value added through the application of synthesis processes to fermented materials. To resolve this issue, in April 2007 we reached an agreement with Daiichi Sankyo Co., Ltd., to acquire its manufacturing subsidiary, Daiichi Fine Chemical Co., Ltd., which has strengths in synthesis technologies. We expect the acquisition of this company to make major contributions to our business in pharmaceutical raw materials and intermediates.

Acquisition of Daiichi Fine Chemical

FERMENTATION

PURPOSE OF ACQUISITION

Organically combine Kyowa Hakko's fermentation technology with the synthesis technology of Daiichi Fine Chemical and manufacture high-value-added pharmaceutical raw materials and intermediates

SYNTHESIS

EXPECTED SYNERGY BENEFITS

- Expand customer network through links between sales and development divisions
- Expand sales through cross-selling in Cosmetics and Health foods
- Expand generic pharmaceutical raw materials business
- Enjoy benefits of bringing outsourced manufacturing in-house

PURSUE HIGHER VALUE ADDED IN BIO-CHEMICALS OPERATIONS AND TARGET SUSTAINED GROWTH

HEALTH CARE

In recent years, the domestic health care industry has been somewhat sluggish. Nevertheless, governments are working to control medical expenditures, and individuals are taking steps to enjoy healthier, longer lives. As a result, the health care industry is expected to register substantial growth around the world in the years ahead.

In this environment, to record growth and development in our operations, we must identify functions in health care materials and develop applications for them. We will continue to carry out these activities, centered on the Healthcare Products Development Center. To enhance customer satisfaction, these activities will typically include brand building and the development of formulations that are easy to process and readily absorbed.

Currently, raw materials for health care products around the world include such natural ingredients as those from plants and animals as well as synthetic ingredients. On the other hand, incidents harmful to health caused by unconfirmed ingredients occur one after another. The safety and security of products made with our fermentation technologies, and the quality assurance systems that support them, are part of the value that we provide to customers. Accordingly, we will continue working to strengthen our systems in the future.

At a Glance

page 20 >>

Kyowa Hakko

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, the segment is working to expand its business in overseas markets. To this end, we are conducting clinical development of new drugs in Europe, North America, and China and are moving ahead with therapeutic antibody operations based on our original strong-acting antibody technologies.

page 22 >>

BIO-CHEMICALS In domestic and overseas markets, the Bio-Chemicals segment conducts production and sales of fermented bulk products, such as amino acids, nucleic acids, and related compounds, which are used as raw materials for pharmaceuticals, health foods and dietary supplements, cosmetics, and pharmaceutical intermediates. In addition, the segment conducts mail-order sales of health care products in Japan, produces and markets alcohol for the alcoholic beverages and food industries, and supplies agrochemicals as well as livestock and fisheries products.

page 26 >>

Kyowa Hakko Chemical

CHEMICALS The Chemicals segment produces and markets basic chemicals and specialty chemicals. Basic chemicals include solvents used in paints and inks and raw materials for plasticizers used as additives in PVC products. Specialty chemicals include environment-friendly products and products for advanced technologies.

page 28 >>

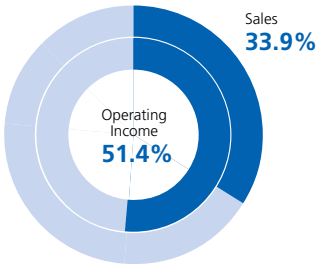
Kyowa Hakko Food Specialties

FOOD The Food segment develops, produces, and markets seasonings, principally natural seasonings made from meat, vegetables, or seafood; bakery products and ingredients, such as yeast and baking improvers; and processed foods, such as freeze-dried soup.

page 29 >>

Segments: Sales* and Operating Income*	Main Products

PHARMACEUTICALS



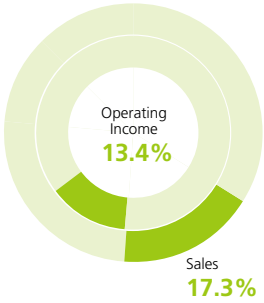
Ethical Drugs

Coniel® (hypertension and angina pectoris), Allelock® (antiallergic agent), Depakene® (antiepileptic agent), 5-FU (anticancer agent), Neu-up® (recombinant human G-CSF derivative), Durotep® Patch (transdermal analgesic agent)

Diagnostic Reagents

Determiner® series (clinical chemistry diagnostic reagents)

BIO-CHEMICALS



Fine Chemicals

Amino acids, nucleic acids, related compounds

Health Care Products

Amino acids, vitamins, minerals, carotenoids, peptides, Remake® series, Enguard® series

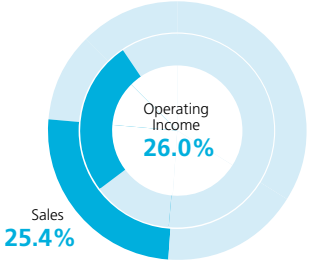
Agrochemicals and Livestock and Fisheries Products

Plant growth regulators, animal health products

Alcohol

For use in alcoholic beverages, for use in food preservatives and disinfectants

CHEMICALS



Solvents

Butyl alcohol, ethyl acetate, butyl acetate

Raw Materials for Plasticizers

Di-2-ethylhexyl alcohol, Oxocol® 900

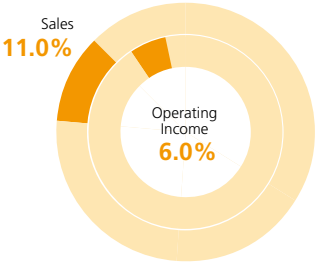
Environment-Friendly Products

Polyvinyl ether, 2-ethyl hexanoic acid, isononanoic acid (raw materials for lubricants in air-conditioning and refrigeration equipment that uses CFC substitutes)

Products for Advanced Technologies

Squaric acid and its derivatives (raw materials for recording media)

FOOD



Seasonings

Natural seasonings

Bakery Products and Ingredients

Baker's yeast, premixes, baking improvers

Processed Foods

Instant egg-drop soup

* Including inter-segment transactions

Industry Trends

• Japanese pharmaceutical companies are experiencing dramatic changes in their operating environment • The government is implementing reforms of the health care system, competition from major overseas pharmaceutical companies is intensifying, and the market for generics is expanding • Moreover, R&D expenses are increasing • In this setting, through the provision of high-quality medical information, Kyowa Hakko will strive to contribute to the spread of evidence-based medicine (EBM) and be a company that is trusted by patients and health care professionals • We will work to rapidly develop new drugs that meet medical needs • To this end, we are concentrating our management resources on our key areas of competence and core technologies: cancer, allergies, the central nervous system, and antibody production technologies • We are also pursuing alliances with other companies and aggressively utilizing external resources.

• Our core fermented bulk products, such as amino acids, nucleic acids, and related compounds, are used in a wide range of fields, including pharmaceuticals and pharmaceutical intermediates, foods, dietary supplements, and cosmetics • In Japan, conditions in the health food industry were sluggish in the year under review, including demand for beverages containing amino acids • Nevertheless, interest in health maintenance and improvement continues to heighten around the world • Also, demand for amino acids for use as pharmaceutical ingredients for parenteral and enteral nutrition preparations, pharmaceutical intermediates, and cosmetics is strong • Key trends in the year under review included markedly higher prices for raw materials and fuel • In addition, food safety and product quality were subjects of growing attention • To maximize customer value, we will further increase efficiency in production and bolster our quality assurance systems to provide safe, high-quality products.

• In the year under review, robust capital investment and firm consumer spending provided the backdrop for a tone of recovery in the domestic economy, and business conditions also improved in global markets • In the petrochemical industry, demand was generally firm in Japan and overseas • With crude oil prices spiraling upward, the prices of raw materials and fuel continued to rise; however, the sales prices of many major products were increased substantially, and exports were favorable, centered on sales of chemical products to China and other Asian markets • As a result, petrochemical companies generally recorded favorable results • However, in the future, the demand structure is expected to change dramatically and global competition to intensify as a series of highly competitive large-scale production facilities for ethylene and its derivatives come on stream in the Middle East and China.

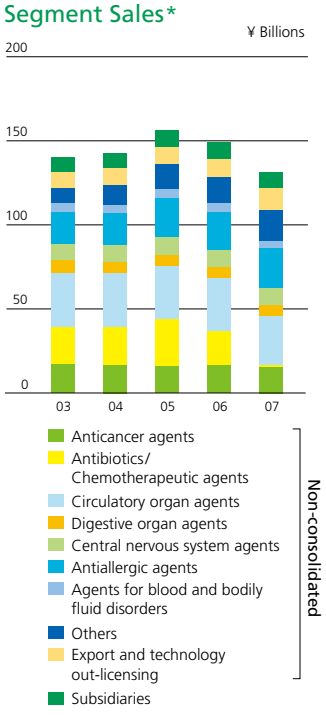
• In the food industry, in an environment marked by maturing markets and higher prices for raw materials, prices continue to decline and competition among companies is intensifying • In the face of escalating competition, companies are implementing selection and concentration in their operations while taking steps to bolster their core businesses, such as strengthening R&D and increasing alliances, including M&A activities • With food markets maturing, over the medium-to-long term, the food service markets are expected to record solid growth, and the number of companies entering these markets is rising • Moreover, we anticipate growing demand for seasonings and confectionery and bakery ingredients that offer not only flavor but also safety, quality, and reasonable prices • The development of original products and the establishment of quality control systems will be key issues for every company in the industry.

Pharmaceuticals

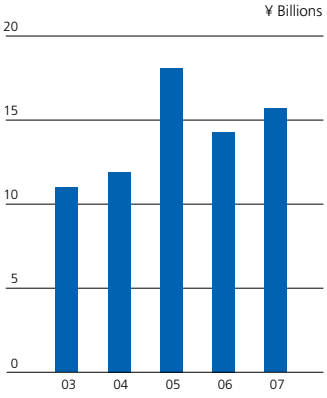
We will bolster our domestic operations and advance the POC Fast strategy for R&D, with a focus on moving rapidly from drug discovery to POC, as well as expand our overseas operations.

Yoshito Imai
President of Pharmaceuticals Business Unit
Executive Vice President

Segment Sales*



Segment Operating Income*



* Including inter-segment transactions / Reflecting the restatements of fiscal 2004 and 2006 figures due to the reclassifications of business segments effective from fiscal 2005 and fiscal 2007, respectively

OPERATIONAL STRATEGY

In Pharmaceuticals, we have three strategic objectives. First, we will bolster our domestic operations. To this end, we have implemented the SMART (Sales and Marketing Transformation) Project. The results of the SMART Project can already be seen in such core products as Coniel®, an agent for treating hypertension and angina pectoris; Allelock®, an antiallergic agent; and Durotep® Patch, an analgesic for consistent cancer pain. We will step up the implementation of the SMART project and expand domestic pharmaceutical sales.

Second, we will advance the POC Fast strategy for R&D, with a focus on moving rapidly from drug discovery to POC. Once we have obtained POC for new drugs, we will consider timing and success rate and choose from a broad range of options, including joint research, out-licensing, and other alliances. This strategy will maximize the value of new drugs by enhancing speed to market.

Third, we will expand our overseas operations. Through U.S. subsidiary BioWa, Inc., we are developing our operations based on Potelligent®, a high ADCC antibody production technology that is expected to generate innovative results in the development of therapeutic antibodies. With the acquisition of another patent that extends the scope of U.S. patent protection to all antibodies with fucose-free complex-type sugar chains and the additional launch of the succeeding technology, Complegent™, we are taking steps to ensure profitable business development. In addition, we are taking steps to build our presence in overseas markets. These steps will include launching KW-6002, an antiparkinson agent, as soon as possible in the United States and Europe and expanding our operations in China through such efforts as increased sales of Coniel® and the launch of Allelock®.

OVERVIEW

In Pharmaceuticals, net sales declined 11.7% from the previous year, to ¥131.5 billion. Sales of our mainstay ethical drugs increased on a volume basis, but the April 2006 revision of official ethical drug prices and the termination of a distribution agreement for the oral antifungal agent Itrizole® had an adverse influence, and sales of these products declined on a value basis. Operating income rose 10.4%, to ¥15.7 billion, due to increased technology out-licensing revenues and efforts to reduce personnel and other expenses.

Ethical Drugs As a result of efforts to secure new customers, we were able to maintain sales of Coniel®, an agent for treating hypertension and angina pectoris, at the same level as in the previous year on a volume basis, despite the market entry of generics. Despite low levels of airborne pollen in the year under review, Allelock® (olopatadine hydrochloride), an antiallergic agent, steadily expanded its market share, and Durotep® Patch, an analgesic for persistent cancer pain, consolidated its position as the top brand. For both of these products, the effect of higher unit sales offset the influence of reductions in official drug prices, and sales rose on a value basis as well. Navelbine®, an anticancer agent, also recorded increased sales. Patanol® antiallergic eye drops, which were launched in October 2006, were well accepted in the marketplace and contributed to sales. On the other hand, due to the termination of a distribution agreement with Janssen Pharmaceutical K.K. for Itrizole®, an antifungal agent, sales of ethical drugs were down overall.

In exports and technology out-licensing, sales of olopatadine hydrochloride, an antiallergic agent, were favorable. Kyowa Hakko licenses out olopatadine hydrochloride to Alcon Laboratories, Inc., of the United States, and the Alcon Group markets it around the world in an eye drop formulation.

Billions of Yen

Principal Drug Sales	Indication	2007	2006	2005
Coniel	Cardiovascular (hypertension and angina pectoris)	¥26.3	¥28.1	¥28.1
Allelock	Antiallergic	21.0	19.9	18.8
Celtect	Antiallergic	4.8	5.4	6.9
Itrizole	Antifungal	—	21.5	29.8
Depakene	Antiepileptic	10.2	10.2	10.1
Adriacin + Farmorubicin	Anticancer	8.6	9.5	9.1
Nauzelin	Gastrointestinal	6.5	6.6	6.9
5-FU	Anticancer	3.3	3.3	3.5
Neu-up	Recombinant human G-CSF derivative	4.5	4.6	4.7
Durotep Patch	Transdermal analgesic	14.1	13.5	12.6
Navelbine	Anticancer	2.8	2.3	1.5
Patanol	Antiallergic eye drops	2.3	—	—
Exports and Technology Out-Licensing		12.8	10.6	10.1

Kyowa Hakko President Yuzuru Matsuda and Alcon Japan Ltd. President Scott Manning at the signing ceremony for the Patanol® joint promotion agreement.

Diagnostic Reagents Subsidiary Kyowa Medex Co., Ltd., handles the manufacture and sale of diagnostic reagents. In the year under review, sales of clinical chemistry diagnostic reagents were down due to intensified competition, but sales of immunological reagents increased. Overall, sales of reagents were up from the previous fiscal year.

New Drug Development In Japan, we received approval in April 2006 for Bothdel, an oral MRI contrast medium for the gastrointestinal tract, and we commenced sales in September 2006. An application has been filed for KW-6485, an antiepileptic, and is now under review by a regulatory agency. KW-6002, an antiparkinson agent, and KW-2246, an analgesic for cancer pain, are in phase II clinical trials. KW-0761, a therapeutic antibody that uses Potelligent®, a high ADCC antibody production technology, is in phase I trials for hematologic tumors. In addition, in January 2007 we concluded a joint development and marketing agreement with Zeria Pharmaceutical Co., Ltd., for Asacol®, an agent for treating inflammatory bowel disease that is currently in phase III trials.

Overseas, we completed phase III clinical trials for the antiparkinson disease indications of KW-6002 in the United States and Europe, and in April 2007 an NDA was filed in the United States. Also, in North America, the anticancer agent KW-2449 is in phase I trials, and in Europe the therapeutic antibody KW-0761 is in phase I trials for allergic rhinitis. In China, phase III clinical trials are under way for Allelock® as well as Coniel®, for which we are targeting an additional indication for angina pectoris.

Therapeutic antibodies for which BioWa has conducted clinical development include BIW-8405, an agent for treating asthma to which Potelligent® is applied. Phase I trials began in the United States in October 2006, and in December 2006 we decided to license it to MedImmune, Inc., a leading U.S. biopharmaceutical company. We are prepared for the development of therapeutic antibodies following BIW-8405, and BioWa will continue to implement rapid clinical trials for therapeutic antibodies. At the same time, we will push ahead with a strategy for maximizing the speed of development of therapeutic antibodies using Potelligent® technology, including joint development efforts with companies that have licensed this technology.

Pharmaceuticals Pipeline

As of June 2007

Code Name *Generic Name* (Product Name)	Indication *Formulation*	Country (Area)	Stage PC P1 P2a P2b P3 ND AP LC	Remarks
ANTICANCER				
KW-2246 *Fentanyl citrate*	Cancer pain *Sublingual tablet*	Japan	PC P1 P2a	• Licensed from Orexo
KW-0761[1]	Anticancer (Hematologic tumor) *Injection*	Japan	PC P1	• Humanized monoclonal antibody (Potelligent® technology applied)
KW-2449	Anticancer *Oral*	U.S.	PC P1	
ANTIALLERGIC				
KW-4679 *Olopatadine hydrochloride* (Allelock)	Antiallergic *Oral*	China	PC P1 P2a P2b P3	• Prescribed in Japan as Allelock®
KW-0761[1]	Antiallergic *Injection*	Europe	PC P1	• Humanized monoclonal antibody (Potelligent® technology applied)
CENTRAL NERVOUS SYSTEM				
KW-6485 *Topiramate*	Antiepileptic *Oral*	Japan	PC P1 P2a P2b P3 ND (Filed in July 2004)	• Licensed from Cilag
KW-6002[2, 3] *Istradefylline*	Parkinson's disease (Adjunct therapy) *Oral*	Japan U.S.	PC P1 P2a P2b PC P1 P2a P2b P3 ND (Filed in April 2007)	• Monotherapy in Japan is in phase IIa
KW-6500 *Apomorphine hydrochloride*	Parkinson's disease *Injection*	Japan	PC P1	• Licensed from Britannia Pharmaceuticals
CARDIOVASCULAR				
KW-3049[4] *Benidipine Hydrochloride* (Coniel)	Angina pectoris *Oral*	China	PC P1 P2a P2b P3	• Prescribed in China from December 2004 as Coniel® (Indication: hypertension)
OTHER				
Z-206 *Mesalazine* (Asacol)	Inflammatory bowel disease (Crohn's disease) *Oral*	Japan	PC P1 P2a P2b P3	• Licensed from and jointly developed with Zeria Pharmaceutical

PC Preclinical
P1 Phase I
P2a Phase IIa
P2b Phase IIb
P3 Phase III
ND NDA filed
AP Approved
LC Launched

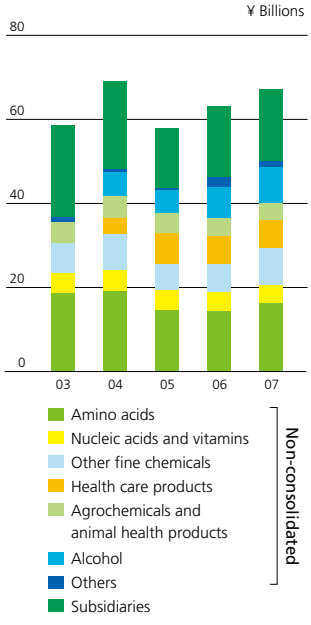
1. KW-0761 is under development as both an antiallergic agent and an anticancer agent.
2. The development program for KW-6002 for the treatment of restless legs syndrome in the United States for an additional indication was discontinued in January 2007 due to a lack of significant efficacy in the phase IIa clinical study.
3. The development program for KW-6002 (phase IIa clinical trials) as monotherapy in the United States was discontinued in April 2007 due to the high investment risk and poor cost-benefit performance.
4. For additional indication
5. In-house developed antibody KW-2871 targeting malignant melanoma cells was licensed to Life Science Pharmaceuticals in the United States, on February 28, 2007. The clinical development of KW-2871 will be continued at the Ludwig Institute for Cancer Research in collaboration with Life Science Pharmaceuticals.

Bio-Chemicals

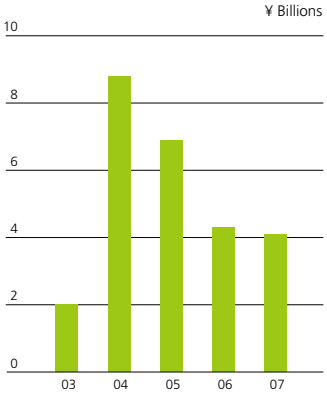
We are enhancing our market position by increasing our cost-competitiveness in amino acids, strengthening our health care operations, and creating new businesses that will be drivers of future earnings.

Yukinobu Kotani
President of Bio-Chemicals Business Unit
Executive Managing Officer

Segment Sales*



Segment Operating Income*



* Including inter-segment transactions / Reflecting the restatements of fiscal 2004 and 2006 figures due to the reclassifications of business segments effective from fiscal 2005 and fiscal 2007, respectively

OPERATIONAL STRATEGY

In Bio-Chemicals, we are pursuing three strategic objectives aimed at differentiating our lineups and achieving growth in the health care market on a foundation of amino acids and other fermented bulk products. Our first objective is to enhance our market position by increasing our cost-competitiveness in amino acids. Kyowa Hakko and Ajinomoto Co., Inc., are the world's two largest manufacturers of amino acids for pharmaceuticals, foods, and industrial applications. In recent years, however, Chinese and South Korean manufacturers have used low-pricing strategies to enter the market. In response, Kyowa Hakko is taking steps to reinforce its three-pronged production system in Japan, the United States, and China, including measures to increase production capacity in China. At the same time, we are increasing our cost-competitiveness in amino acids by boosting productivity through streamlining and production process innovations. Our second objective is to strengthen our health care operations, a field in which we anticipate further growth. For example, we are using our Healthcare Products Development Center to expand our mail-order and OEM businesses by identifying consumer needs, developing products, and conducting planning and proposals. In addition, we are enhancing our marketing capabilities in the U.S. health care market. Our third objective is to create new businesses that will be drivers of future earnings. Dipeptides and sugar chains, for which we have developed groundbreaking manufacturing processes, are candidates to become future earnings mainstays. Moreover, we will work to create derivatives and new compounds using our fermented materials as the starting point and provide new products to customers. To this end, we will start working to combine fermentation and synthesis processes.

OVERVIEW

Bio-Chemicals registered year-on-year gains of 6.1% in net sales, to ¥67.1 billion, while operating income declined 5.3% from the previous year, to ¥4.1 billion. Amino acids for bulk pharmaceuticals and raw materials for generic pharmaceutical products enjoyed robust demand and recorded higher sales. On the other hand, price competition in amino acids for health foods and dietary supplements remained fierce, and domestic demand for amino acids for beverages was sluggish. In addition, raw material and fuel prices increased. Operating income was approximately level with the previous year.

Fine Chemicals Raw materials for pharmaceuticals and industrial use — centered on amino acids, nucleic acids, and related compounds — recorded a substantial gain in sales, as demand increased overseas and domestic sales of raw materials for generic pharmaceutical products increased.

Health Care Products Sales of health care products were up from the previous fiscal year. Although domestic sales of raw materials for health foods were slack due to sluggish conditions in the domestic health foods market, sales of amino acids for use in dietary supplements grew in overseas markets and domestic mail-order sales of the Remake® series of products expanded.

Biokyowa Inc.

Agrochemicals and Livestock and Fisheries Products Overall, sales in this category decreased from the previous fiscal year. This decline was principally attributable to our withdrawal from fertilizer operations, intensified competition in overseas agrochemicals markets, and sluggish market conditions in the livestock and fisheries industries.

Alcohol Sales of raw material alcohol for use in alcoholic beverages remained sluggish, however, sales of industrial-use alcohol, which was deregulated, recorded substantial growth on a volume basis. Prices were revised to partially offset higher raw material prices, and overall sales of alcohol increased.

R&D In Bio-Chemicals operations, we are continuing to research methods to increase efficiency in fermentation production processes to significantly reduce production costs for our mainstay amino acids. We are also continuing projects to discover functions and develop applications for a wide range of amino acids, nucleic acids, and related compounds.

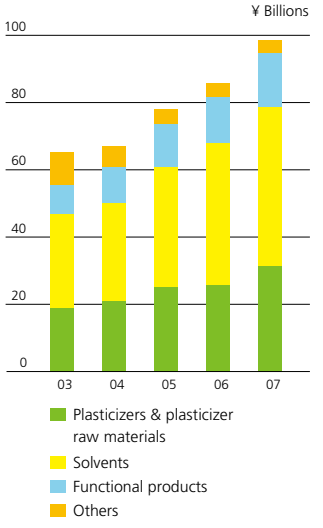
Shanghai Kyowa Amino Acid Co., Ltd.

Chemicals

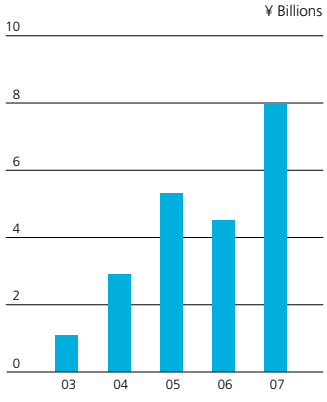
To bolster our operational foundation, we will enhance the market positions and cost-competitiveness of core products through alliances and implement measures to further cultivate the market for and expand sales of specialty chemicals.

Makoto Kikkawa
President and Chief Executive Officer of Kyowa Hakko Chemical Co., Ltd.
Managing Officer

Segment Sales*



Segment Operating Income*



* Including inter-segment transactions

OPERATIONAL STRATEGY

With the objective of shifting to a corporate constitution that is less susceptible to the influences of the operating environment, such as continued dramatic fluctuations in raw material and fuel prices, we will implement the following measures to achieve our strategic objectives.

To bolster our operational foundation, we will step up cost-cutting measures, including the low-cost, stable procurement of raw materials and fuel as well as reductions in production facilities and distribution expenses. We will target capital expenditures at such efforts as the improvement of aging plants and the enhancement of infrastructure. In existing operations, our strategy for such basic chemicals as solvents and raw materials for plasticizers is to enhance the market positions and cost-competitiveness of core products through alliances and other efforts. We will also implement measures to further cultivate the market for and expand sales of specialty chemicals, where we expect future market growth, mainly focusing on environment-friendly and IT-related products.

To develop and expand new product operations, we will reinforce our R&D system. In addition to capital investment in research facilities and measures to prepare the internal systems needed to conduct efficient R&D, we will aggressively work with universities and external research organizations and steadily lay the foundations for future growth and development.

OVERVIEW

In Chemicals, market demand was strong in Japan and overseas. While raw materials and fuel prices continued to rise, we implemented price revisions for core products in Japan, and the prices of exports remained high due to strong market conditions for our mainstay basic chemical products. Kyowa Hakko Chemical recorded a 14.9% year-on-year increase in net sales, to ¥98.7 billion, and operating income rose 77.2%, to ¥8.0 billion.

Basic Chemicals Domestic sales in basic chemicals operations registered a significant year-on-year increase that resulted from upward revisions of mainstay product prices against a background of hikes in raw material and fuel prices. In exports, high prices for mainstay raw materials for plasticizers and solvents lifted export revenues despite a decline in shipment volumes from the previous fiscal year.

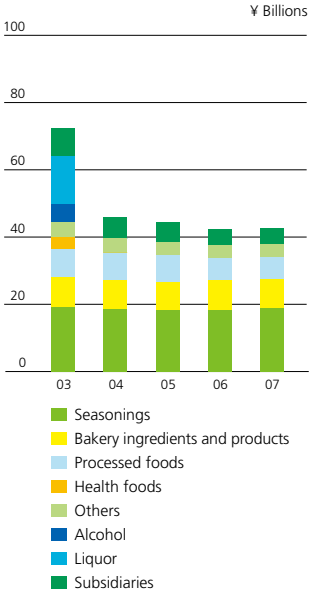
Specialty Chemicals In specialty chemicals, domestic and export sales grew in terms of both volume and value. Sales of high-purity solvents for the IT industry expanded, and favorable sales growth was recorded by raw materials for lubricants in air-conditioning and refrigeration equipment that uses chlorofluorocarbon (CFC) substitutes, which are refrigerants that do not damage the ozone layer.

Food

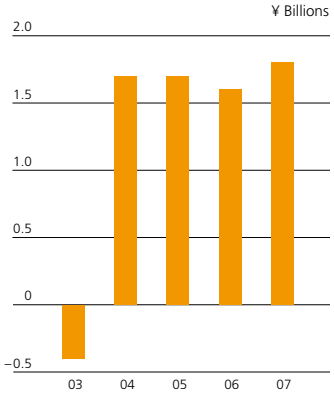
We will draw on our original technologies to develop differentiated food ingredients, implement new initiatives with reinforced links between development and marketing, and work to develop new markets through solutions-based marketing activities.

Takeyuki Yoshida
President and Chief Executive Officer of
Kyowa Hakko Food Specialties Co., Ltd.
Managing Officer

Segment Sales*



Segment Operating Income*



* Including inter-segment transactions / Reflecting the restatement of fiscal 2004 figures due to the reclassification of business segments effective from fiscal 2005 / Liquor operations were sold in September 2002

OPERATIONAL STRATEGY

The mission of Kyowa Hakko Food Specialties Co., Ltd., is to earn the trust of customers by providing safe, high-quality products that contribute to better health and diets. We are drawing on our original technologies — including fermentation and cooking-reactions technologies — to develop differentiated food ingredients. By establishing a marketing system that integrates R&D and sales activities and strengthening our quality assurance system, we will work to open up new markets through solutions-based marketing activities. Targeting the expanding food service industries, we will implement new initiatives with reinforced links between development and marketing and work to develop new markets.

In seasonings, one of our core product areas, we aim to be a leader in the field of natural seasonings, which includes extract, amino acid, and brewed seasonings. In bakery products and ingredients, another core area, we will enhance our relationships with major bread companies by offering unique products, such as flavor enhancers and bread improvers.

Currently, we operate plants in China for the manufacture of natural seasonings and freeze-dried food ingredients. We are taking steps to bolster our marketing capabilities and open up new markets in China.

OVERVIEW

Food operations face the challenge of responding to rapid changes in market structures driven by diversifying consumer preferences. In the fiscal year under review, net sales were up 0.4% from the previous fiscal year, to ¥42.6 billion, and operating income increased 14.4%, to ¥1.8 billion.

Seasonings In natural seasonings, higher sales were recorded by brewed seasonings for home-meal replacement products and food service products, and sales of *Umami* seasonings rose on a volume basis. Overall, sales of seasonings expanded from the previous fiscal year.

Bakery Products and Ingredients Sales of core products, such as yeast, flavor enhancers, and bread improvers, increased, but sales of bread premixes and milk preparations declined. Overall, sales of bakery products and ingredients were down from the previous fiscal year.

Processed Foods In processed foods, higher sales were recorded by ingredients for instant noodles and by soup bases. Overall, sales of processed foods increased from the previous year.

BASIC POLICIES REGARDING INTELLECTUAL PROPERTY

Kyowa Hakko is an R&D-based company and considers intellectual property (IP) to be one of its key management resources. In particular, the Company aggressively pursues wide-ranging, robust, and effective rights to the IP that underpins its business strategies. Also, we respect the rights of third parties and refrain from infringing on them. This enables us to not only ensure compliance but also maintain a high degree of freedom in our research and business activities, which in turn contributes to the achievement of maximum value in each individual business.

To this end, the Company is strengthening its systems to conduct such activities as acquiring and protecting IP rights, managing licensing, and monitoring third parties' rights from a global perspective. For example, in its main business of pharmaceutical product development, the Company protects core technologies and prolongs the life of products through the strategic filing of relevant patents.

FUNCTIONS OF THE INTELLECTUAL PROPERTY DEPARTMENT

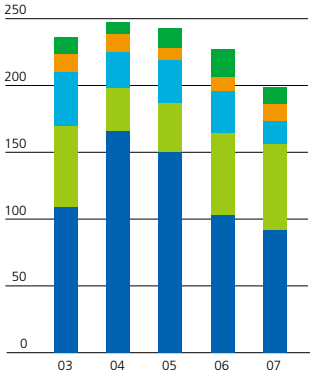
The Intellectual Property Department has Companywide functions based on the principle of centralized management across Kyowa Hakko's business divisions and major subsidiaries. This structure is intended to make operations more efficient and reinforce risk management with regard to IP. As part of the Company's efforts to increase its capabilities in terms of IP, the previously independent Technological Information Division was merged with the Intellectual Property Department in April 2005, and in April 2007 the Pharmaceutical Patent Information Division and certain contract-related functions of the Legal Department were merged into the Intellectual Property Department, thereby enhancing the department's capabilities to investigate, evaluate, and utilize information.

In recent years, Kyowa Hakko has recognized that integrating business and IP strategies is an important Companywide issue. The Intellectual Property Department is strengthening its coordination with the head office of each business division and research laboratories by holding regular meetings as well as exchanging information and consulting with research laboratories more frequently. Moreover, we recognize the necessity of being familiar with the IP environment at each important stage of research and business decision making. Members of the Intellectual Property Department therefore participate in major projects related to development themes, existing products, licensing, and other issues.

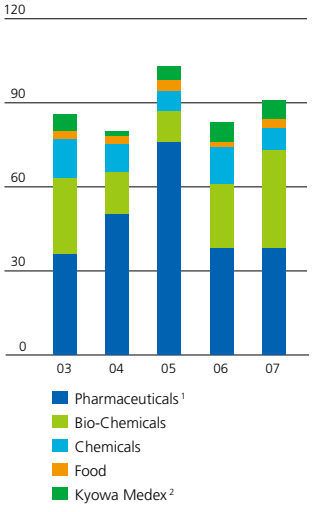
Another important function of the Intellectual Property Department is the education of employees on IP rights. The department sends employees on overseas training courses while upgrading its in-house employee training programs, which include orientation for new recruits and programs for specific fields or groups of employees. Also, the Company has close relationships with lawyers and patent attorneys with expertise in related fields in Japan or overseas to appropriately address highly specialized issues.

.

Number of Patent Applications (Japan)



Number of Patent Applications (Overseas)



1. Pharmaceuticals excludes Kyowa Medex Co., Ltd.
2. Kyowa Medex manufactures and sells diagnostic reagents.

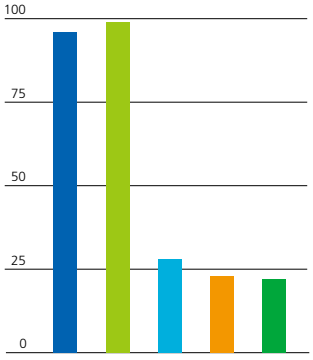
CONTRIBUTIONS TO LICENSING ACTIVITIES

As it is becoming increasingly difficult to continue to independently develop new products, the Company's Pharmaceuticals operations actively out-license products developed in-house based on the POC Fast strategy. At the same time, additional attention is being paid to in-licensing activities, which in turn has raised the importance of the evaluation of IP issues related to in-licensed candidates. The Company established a Strategy and Legal Affairs Group within the Intellectual Property Department in June 2007 to facilitate closer cooperation among IP staff, legal staff, and various business divisions, which is vital in the management of important licensing-related issues.

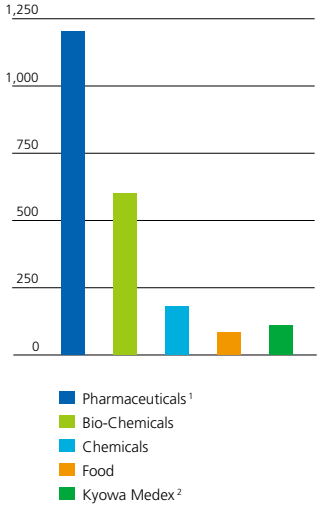
In recent years, opportunities have expanded in Pharmaceuticals operations, in particular, to license R&D achievements to other companies. For example, the Company's proprietary antiallergic agent, olopatadine hydrochloride, has become a mainstay of technology-licensing revenue. Also, in the previous fiscal year we successfully out-licensed the therapeutic antibody KW-2871 and other compounds. As a result, technology-licensing fees are accounting for a larger share of operating income, and further gains are expected.

Kyowa Hakko has accumulated numerous core technologies in the process of pursuing R&D activities that are underpinned by unique and innovative research and technology. One of these technologies is the Company's proprietary Potelligent® technology, which dramatically enhances the antibody-dependent cellular cytotoxicity (ADCC) of antibodies. While working to acquire multifaceted patent rights for this technology, the Company is actively out-licensing this technology to major U.S. and European pharmaceutical companies that develop antibodies through its U.S. subsidiary, BioWa, Inc. During the fiscal year under review, the anti-IL-5R antibody BIW-8405 and other compounds were out-licensed, which are expected to make solid profit gains as well as strengthen the Company's reputation for innovative technological capabilities. Moreover, the Company has multiple core technologies related to drug formulation, which are contributing to its profits under the protection by IP rights.

Number of Patents Owned (Japan)



Number of Patents Owned (Overseas)



1. Pharmaceuticals excludes Kyowa Medex Co., Ltd.
2. Kyowa Medex manufactures and sells diagnostic reagents.

POLICIES RELATED TO THE IP PORTFOLIO

Kyowa Hakko generally engages employees to create initial basic inventions and aggressively apply for patents based on such inventions. Nevertheless, the timing of overseas applications and examination requests as well as post-registration operations, management, and other activities are evaluated in terms of technology, business operations, and rights. Each issue or project is prioritized by taking into account the additional factor of cost effectiveness, and decisions are made to maintain only those rights deemed necessary. This makes it possible to concentrate internal resources related to IP on significant issues. In Pharmaceuticals, for instance, the heads of relevant departments meet regularly to make decisions for which technologies and in which countries the applications are to be prepared. Meetings are held when necessary to discuss the need to maintain patents in light of changes in strategic direction to make maximum use of patent rights. Each business division works to build an IP portfolio that is consistent with its business strategy, taking into account the position of individual projects under the strategy as well as the position of each IP right within the project. In addition, given the particular importance of IP strategies in Pharmaceuticals, a Portfolio Committee meets regularly to decide major issues related to R&D as part of a structure for analyzing and evaluating IP-related issues as a whole or as individual projects.

As stated in its management guidelines, Kyowa Hakko considers environmental safety, quality assurance, and social contribution activities to be important management issues. Leadership by top management provides an example that is followed by everyone at Kyowa Hakko.

ENVIRONMENTAL SAFETY

Management Systems

Our environmental and safety management system ensures continuous improvement in environmental safety and preservation, disaster prevention, and product safety through the integration of the ISO 14001 environmental management system with the Occupational Safety and Health Management System (OSHMS) and the implementation of our Plan, Do, Check, and Act (PDCA) cycle. In addition to complying with environmental safety-related laws and regulations, we have set targets that are even higher. Compliance with laws and regulations is monitored at the head office. Moreover, we have fully adopted Responsible Care (RC) activities.

Performance

Through the Companywide Kyowa Eco-Project, we have once again worked to reduce the environmental burden of our operations during the fiscal year under review, focusing on energy saving, resource saving, and zero emissions. As a result, the Company has achieved its stringent targets for zero emissions, which include the thorough control of emissions and the recycling of industrial waste, for the third consecutive year. We are also working aggressively to reduce greenhouse gas emissions by investing in energy-saving equipment and moving to alternative fuels, including a shift from heavy oil to gas.

Furthermore, the entire Group is engaged in green office plan activities, which focus on the promotion of a green supply chain along with saving energy and promoting recycling in administrative departments.

In terms of safety, we continue to rank at the top of our industry, with an accident rate of zero at Kyowa Hakko, Kyowa Hakko Food Specialties, Kyowa Hakko Chemical, and Kyowa Medex. In addition, the Group did not experience any serious incidents involving fires or leakages during the fiscal year under review.

Communication

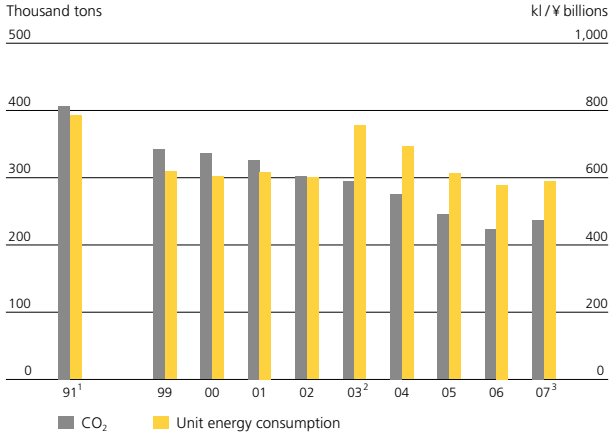
Our annual Sustainability Report provides information related to environmental safety, and we are enhancing the reliability of this report through third-party verification. As part of our RC activities, we interact with local residents near our workplaces, and such interactions lead to improvements in terms of safety and the environment.

Development of Technologies and Products for Environmental Safety

Kyowa Hakko is actively engaged in the development of environmental safety technologies and products as well as resource-saving technologies. Our raw materials for lubricants in air-conditioning and refrigeration equipment that uses CFC substitutes contribute to environmental preservation. Also,we produce raw materials for water-based coatings, which help prevent atmospheric pollution by curbing the environmental emissions of organic solvents. Furthermore, we participate in national projects in the field of biotechnology by developing core technologies with the aim of raising efficiency in low-environmental-impact bioprocesses.

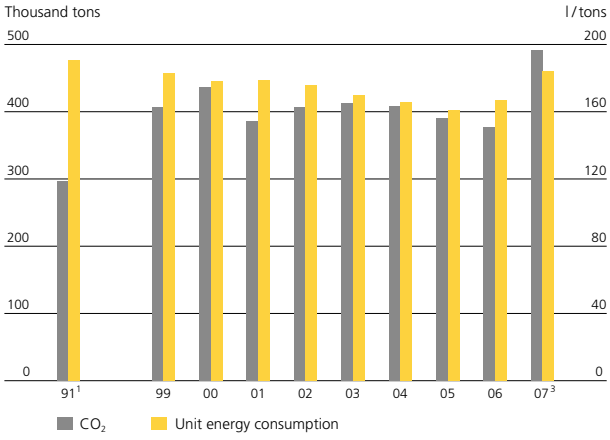
Yearly Changes in Unit Energy Consumption

Kyowa Hakko, except Kyowa Hakko Chemical



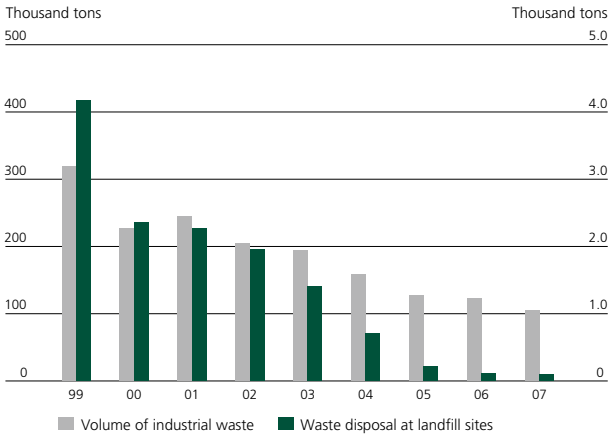
Yearly Changes in Unit Energy Consumption

Kyowa Hakko Chemical



Yearly Changes in Volume of Industrial Waste

Kyowa Hakko



1. Fiscal 1991 figures are the reference values for numerical targets spelled out in the Kyoto Protocol, which determined emission reduction obligations for CO2 and other greenhouse gases.
2. Due to the transfer of the alcoholic beverage operations, unit energy consumption increased in 2003.
3. Following the revision of the law in 2006, CO_2 equivalent units and the areas for which energy are calculated have been revised.

QUALITY ASSURANCE

The Kyowa Hakko Group has formulated a Quality Assurance Action Policy to raise the awareness of quality assurance and is actively promoting this policy throughout the Group, including overseas locations.

Our goal is to gain the trust and satisfaction of customers by providing products and services that are superior in terms of quality and function. With this in mind, the Group strives to enhance quality and function across all divisions, from R&D to purchasing, manufacturing, distribution, and sales.

Furthermore, we actively gather such information as customers' requests and complaints to improve our response times. Information regarding complaints is quickly passed on to relevant departments; the entire Company is involved in responding to customers to gain their satisfaction. In addition, we strive to further raise product quality assurance through highly reliable manufacturing and quality control by addressing new laws, including the revised Pharmaceutical Affairs Law, and implementing and continuously improving GMP, ISO 9001, and other quality assurance systems at all our plants.

In Pharmaceuticals operations, programs are in place for manufacturing control, quality control, and post-marketing safety monitoring that are in accordance with the revised Pharmaceutical Affairs Law, while global quality assurance systems have been set up for new products. In addition, the Medical Information Center responds to direct customer inquiries as a means of raising customer satisfaction.

The Medical Information Center

CORPORATE CITIZENSHIP

One of the management guidelines of Kyowa Hakko for the achievement of its fundamental policy is to ensure that management is open to society and international standards are fully adopted in management practices. Furthermore, the keys to achieving this guideline are to maintain open lines of communication with local communities and earn society's understanding and trust through exchanges of information, good corporate citizenship, and social contribution activities.

"Science for a Happier 21st Century" Essay Competition

The increasing complexity of science is causing Japan's younger generation to lose interest in this important field. In response, Kyowa Hakko aims to offer the kinds of opportunities that will spur young students toward a greater interest in science and, to this end, holds an annual scientific essay competition that is open to junior and senior high school students throughout Japan. The competition, which began in 1999, is cosponsored by The Mainichi Newspapers and supported by Japan's Ministry of Education, Culture, Sports, Science and Technology. It will be held for the ninth time in summer 2007.

Local Science Experiment Classrooms

The BioAdventure vehicle is a mobile classroom equipped with microscopes and other scientific equipment that is operated by BioFrontier Laboratories, in Machida, Tokyo. Kyowa Hakko's researchers teach science to elementary and junior and senior high school students and assist the students in conducting experiments. Other local activities include the Children's Science Experiment Classroom, situated at the Fuji Plant, in Shizuoka Prefecture, for local elementary school students, and the Junior Science Classroom, located at the Ube Plant, in Yamaguchi Prefecture, for elementary and junior high school students.

Asahi Young Session

In cooperation with The Asahi Shimbun Company and with the support of the Ministry of Education, Culture, Sports, Science and Technology, Kyowa Hakko has sponsored the Asahi Young Session since 1988. This annual lecture series for young people, primarily high school students, introduces a new theme each year with an overlying message of the importance of future directions, dreams, and a desire for life. The 19th session was held in March 2007 and featured a presentation by immunologist Dr. Kimishige Ishizaka, who discovered immunoglobulin E and, together with his wife Teruko, has clarified mechanisms that trigger allergies. The subject of his talk was "Solving the Riddle of Allergies." Printed transcripts of Dr. Ishizaka's presentation are available on request.

Kato Memorial Bioscience Foundation

Established in 1988 in commemoration of Kyowa Hakko's founder, Dr. Benzaburo Kato, the Kato Memorial Bioscience Foundation supports creative bioscience research through the provision of research and financial assistance to young researchers.

Free Braille Calendars for Schools for the Blind Nationwide

Kyowa Hakko has created a Braille calendar for people with visual disabilities every year since 1994 and distributed it free to schools for the blind all over Japan. Approximately 4,000 calendars were distributed to 71 schools in 2006.

FUNDAMENTAL APPROACH

Kyowa Hakko operates its business 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 advances in life sciences and technology." Our basic pursuit in corporate governance is to frame responsibilities and duties of the management organization and ensure the policies we have in place are complied with and are leading toward the realization of the Company's philosophy. We recognize the importance of increasing management transparency and reinforcing oversight functions and make efforts to enhance corporate governance to continually raise corporate value.

FUNDAMENTAL STRUCTURE

Kyowa Hakko uses a corporate auditor system, with the General Shareholders' Meeting as the highest decision-making body. The corporate governance structure is based on the Board of Directors and the Board of Auditors, which carry out the functions stipulated under the Corporation Law.

Directors and Board of Directors

The Board of Directors convenes once a month in principle and had six members, including one outside director, as of June 20, 2007. The Board of Directors performs critical Groupwide management functions, including strategic planning, decision making, and the monitoring of operational execution. In its performance of these functions, the Board of Directors met 14 times during the fiscal year ended March 31, 2007.

Corporate Auditors and Board of Auditors

The Board of Auditors comprised four members, including three outside auditors, as of June 20, 2007. Based on the audit policies set forth by the board, auditors attend important meetings, including those of the Board of Directors; inspect operations and assets; and audit the work of directors. In its performance of these duties, the Board of Auditors met 14 times during the fiscal year ended March 31, 2007.

Note: There are no personal, capital, or transactional interests between the Company and its outside directors or outside auditors. The Company has concluded contracts with its outside directors and outside auditors limiting their liability for damages as stipulated under the Corporation Law. Based on these contracts, the maximum liability for damages is the higher of either ¥5 million or the legal minimum liability limit.

Management Meeting, Executive Officer System, and Advisory Board

The Management Meeting, comprising directors and executive officers, has been established as a decision-making body to make accurate and effective management decisions from a strategic viewpoint. The Management Meeting deliberates important and fundamental issues related to the Group's management policies and operational execution and met 16 times during the fiscal year.

In addition, an Executive Officer System has been introduced to facilitate swift decision making and strengthen operational execution.

Also, Kyowa Hakko has established an Advisory Board to the Board of Directors to bolster management and ensure transparency and soundness. The Board provides an outside management perspective on various management-related issues for the entire Group. The Advisory Board is made up of the Company's two representative directors and four outside advisors and, in principle, meets twice a year. The Advisory Board met twice during the fiscal year ended March 31, 2007.

Outside Advisor	Company	Title
Eiko Kono	Recruit Co., Ltd.	Senior Advisor
Masatoshi Shigefuchi	TOTO LTD.	Chairman of the Board
Tomio Tsutsumi	Mitsubishi Corporation	Director
Tomijiro Morita	The Dai-ichi Mutual Life Insurance Company	Chairman of the Board

In-House Committees

To address the variety of risks inherent in management issues, seven in-house committees have been established to strengthen risk management and enhance corporate governance. These committees regularly report on their activities to the Board of Directors and also seek advice as necessary from such third parties as corporate lawyers and tax accountants. The Information Disclosure Committee is chaired by President Yuzuru Matsuda, and the Risk Management Committee, Environmental Safety Committee, Quality Assurance Committee, Corporate Ethics Committee, and Information Security Committee are chaired by Director and Senior Executive Managing Officer Tomonori Yuji. The Financial Management Committee is chaired by Director and Senior Executive Managing Officer Kazuhiko Yamanoe.

INTERNAL CONTROL SYSTEM

A policy for the establishment of a structure for internal control to ensure the integrity of operations was approved by the Board of Directors on May 22, 2006, and this structure is currently under development based on that resolution.

Compliance

Kyowa Hakko views regulatory compliance as one of its most important management issues and has established guidelines under the Kyowa Hakko Code of Ethics and Kyowa Hakko Standards of Ethical Conduct. A dedicated organization has been created to promote corporate ethics and familiarize all employees throughout the Group with Kyowa Hakko's corporate ethics policies. Also, an internal reporting system is in place, and when necessary advice is sought from lawyers and other third parties.

Internal Audit

The Audit Department has been established as a dedicated internal audit organization that is independent of the operating organization. In addition to examining and reporting on the status of the Company's operations from the perspectives of legal and internal compliance and effective management, the Audit Department offers advice and makes proposals to enhance operations and improve efficiency.

Risk Management

The Risk Management Committee is the risk management structure for the entire Group, centrally overseeing the activities in each section or department associated with potential risks that may arise in the Company's business operations. (Please refer to "Risk Factors" on pages 48–49 for details of these risks.)

Structure for Reporting to Auditors

Directors and employees are obligated to report to auditors any violations of laws, internal regulations, resolutions of the Board of Directors, or other rules under the internal reporting structure. Auditors may attend important management meetings, including those of the Board of Directors, as well as examine meeting minutes and other documents and carry out other audits in cooperation with the dedicated internal audit department.

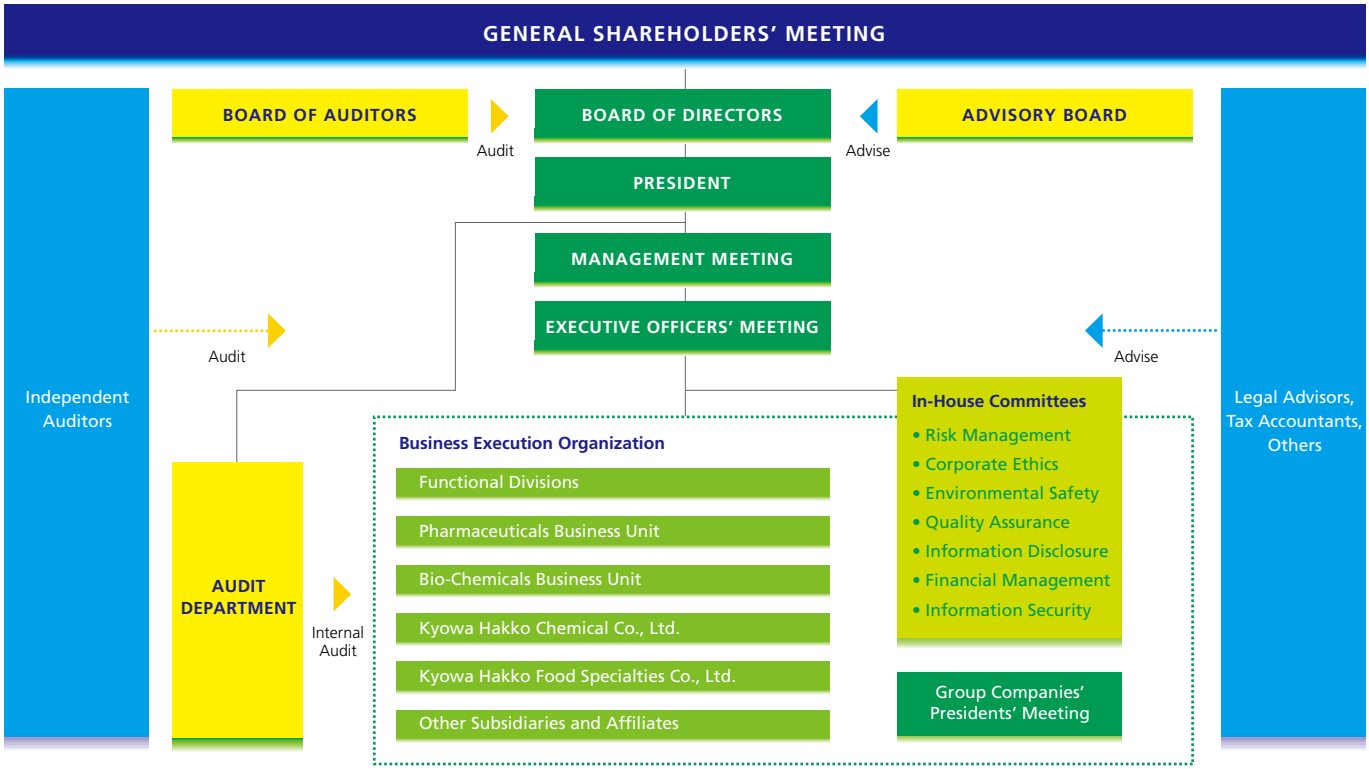
INDEPENDENT AUDITOR

The Company's previous independent auditor, ChuoAoyama Audit Corporation (presently Misuzu Audit Corporation), received a suspension of its business activities from the Financial Services Agency on May 10, 2006, for the period from July 1, 2006, to August 31, 2006. As a result, ChuoAoyama ceased to qualify as an independent auditor and resigned as the Company's independent auditor. To avoid a vacancy in the position of independent auditor, on July 3, 2006, the Board of Auditors appointed Ernst & Young ShinNihon as the Company's temporary independent auditor. The Company's auditors and the independent auditor regularly discuss audit plans, audit policy, and the status of audits and exchange opinions whenever necessary. In addition, the Company's auditors read the audit reports prepared by the independent auditor and, when necessary, meet with their auditors and attend reviews to study the status of such audits. Furthermore, Ernst & Young ShinNihon was appointed as the Company's independent auditor at the 84th Annual General Shareholders' Meeting, which was held on June 20, 2007.

COMPENSATION TO DIRECTORS AND AUDITORS

Executive compensation to directors and auditors during the fiscal year under review totaled ¥324 million, of which ¥251 million was compensation to directors and ¥72 million was to auditors. The Company introduced a performance-based compensation system for its directors and executive officers. Furthermore, a stock option scheme for a stock-linked compensation plan has been offered in place of the discontinued retirement benefit system and the compensation to directors shown above included stock options in the amount of ¥31 million. In addition, ¥56 million in audit fees were paid to the independent auditor, including ¥41 million for the audit certification based on the audit contract.

Corporate Governance Structure



MEMBERS OF THE BOARD

Directors

President

Yuzuru Matsuda*

Yoshito Imai*
Tomonori Yuji
Kazuhiko Yamanoe
Yukinobu Kotani
Kozo Fujita
Outside Director, Lawyer,
Former Corporate Auditor

* Representative Director

Front row, from left:
Yoshito Imai,
Yuzuru Matsuda,
Tomonori Yuji

Back row, from left:
Yukinobu Kotani,
Kazuhiko Yamanoe,
Kozo Fujita

Corporate Auditors

Takeshi Asaoka
Outside Corporate Auditor

Akira Taniguchi
Outside Corporate Auditor

Nobuo Kanda
Former Director and Senior
Executive Managing Officer

Hiroyuki Takahashi
Outside Corporate Auditor

From left:
Nobuo Kanda
Takeshi Asaoka
Akira Taniguchi
Hiroyuki Takahashi

MANAGING OFFICERS

President and Chief Executive Officer

Yuzuru Matsuda

Executive Vice President

Yoshito Imai
President of Pharmaceuticals Business Unit

Senior Executive Managing Officers

Tomonori Yuji
Kazuhiko Yamanoe

Executive Managing Officers

Yukinobu Kotani
President of Bio-Chemicals Business Unit
Yutaka Yoshida
Fumio Norimatsu

Managing Officers

Takeyuki Yoshida
President and Chief Executive Officer,
Kyowa Hakko Food Specialties Co., Ltd.
Makoto Kikkawa
President and Chief Executive Officer,
Kyowa Hakko Chemical Co., Ltd.
Yoshiki Tsunekane
Mitsuru Takahashi
Akio Ozaki
Kazuyoshi Tachibana
Nobuo Hanai
Akira Karasawa
Manabu Suzuki
Shuichi Ishino
Fumihiro Nishino
Takao Miyamoto
Masau Takayanagi

Financial Section

40 Eleven-Year Selected Financial Data
42 Management's Discussion and Analysis
48 Risk Factors
50 Consolidated Balance Sheets
52 Consolidated Statements of Income
53 Consolidated Statements of Changes in Net Assets
54 Consolidated Statements of Cash Flows
55 Notes to the Consolidated Financial Statements
76 Report of Independent Auditors

ELEVEN-YEAR SELECTED FINANCIAL DATA

KYOWA HAKKO KOGYO CO., LTD. AND ITS CONSOLIDATED SUBSIDIARIES
For the years ended March 31

	2007	2006	2005	2004
For the Year:				
Net sales	**¥354,274**	¥353,440	¥358,963	¥348,838
Gross profit	**131,425**	126,983	132,113	129,507
Selling, general and administrative expenses	**100,726**	101,448	98,606	102,671
Operating income	**30,699**	25,535	33,507	26,836
Net income	**12,694**	16,273	17,932	10,017
Capital expenditures	**14,498**	10,859	7,647	9,041
Depreciation and amortization	**10,006**	9,789	10,565	11,358
R&D expenses	**33,342**	32,876	28,762	29,206
Cash Flows:				
Net cash provided by operating activities	**23,381**	14,303	30,104	34,264
Net cash (used in) provided by investing activities	**(8,494)**	(1,796)	(8,104)	10,477
Net cash used in financing activities	**(24,417)**	(5,139)	(9,116)	(44,226)
Cash and cash equivalents at the end of the year	**36,614**	45,820	37,818	24,911
At Year-End:				
Current assets	**214,352**	212,985	210,341	194,062
Total assets	**378,871**	384,381	374,493	361,096
Current liabilities	**106,566**	94,148	103,489	98,914
Interest-bearing debt	**13,137**	12,216	12,193	13,358
Total net assets	**244,082**	257,491	—	—
Total shareholders' equity [2]	**220,427**	232,621	235,439	225,042
Number of employees [4]	**5,756**	5,800	5,960	6,294
Per Share Data:				
Net income — basic [3]	**¥ 31.3**	¥ 38.4	¥ 41.7	¥ 23.0
Total net assets	**607.5**	604.9	556.3	522.6
Cash dividends	**10.0**	10.0	10.0	7.5
Common Stock Price Range (Per share):				
High	**1,154**	946	864	719
Low	**722**	656	661	495
Stock Information (Thousands of shares):				
Number of common stock issued	**399,244**	434,244	434,244	434,244
Weighted average number of common stock issued	**405,270**	422,920	427,636	431,497
Financial Ratios:				
Return on assets (ROA)	**3.33**	4.29	4.88	2.74
Operating return on assets	**8.04**	6.73	9.11	7.35
Return on equity (ROE)	**5.10**	6.63	7.79	4.51
Equity ratio	**63.80**	66.55	62.87	62.32
Debt/equity ratio	**5.43**	4.78	5.18	5.94

1. U.S. dollar amounts are translated from Japanese yen, for convenience only, at the rate of ¥118.09=US$1, the approximate exchange rate at March 31, 2007.
2. Due to a change in accounting standards, figures for total shareholders' equity in the years ended March 31, 2007 and 2006, have been restated.
3. 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.
4. Figures for number of employees prior to the year ended March 31, 2000, were only available in nonconsolidated basis.

	Millions of Yen						Thousands of U.S. Dollars[1]
2003	2002	2001	2000	1999	1998	1997	2007
¥359,285	¥378,668	¥375,610	¥374,910	¥384,671	¥397,361	¥397,629	**$3,000,034**
126,328	128,744	123,945	126,872	127,864	144,191	144,248	**1,887,112**
110,239	108,387	106,233	105,216	104,407	109,448	110,320	**852,959**
16,089	20,357	17,712	21,656	23,457	34,743	33,928	**259,963**
8,485	5,535	9,395	11,274	6,143	13,528	12,339	**107,494**
11,791	11,454	17,092	21,053	24,408	24,555	19,132	**122,771**
14,768	17,819	18,502	19,153	17,673	17,113	16,701	**84,732**
31,438	29,294	28,921	25,888	24,083	25,358	22,882	**282,344**
18,193	16,955	28,789	32,737	—	—	—	**197,993**
2,586	8,377	(1,991)	23,422	—	—	—	**(71,928)**
(38,748)	(16,843)	(20,871)	(50,077)	—	—	—	**(206,766)**
24,588	41,908	32,600	26,215	—	—	—	**310,052**
195,878	244,410	237,852	223,353	270,499	235,697	236,337	**1,815,158**
368,772	430,113	431,410	433,958	477,729	437,271	431,774	**3,208,324**
95,046	162,508	169,821	158,542	211,376	181,554	182,648	**902,412**
51,969	74,354	87,624	102,870	151,489	98,282	97,786	**111,246**
—	—	—	—	—	—	—	**2,066,915**
219,047	211,652	194,692	195,039	185,766	188,645	180,391	**1,866,601**
6,749	7,299	7,766	7,866	5,044	5,134	5,174	**—**
	Yen						U.S. Dollars[1]
¥ 19.4	¥ 12.7	¥ 21.6	¥ 26.0	¥ 13.9	¥ 30.3	¥ 27.6	**$0.265**
505.4	487.5	448.3	449.1	427.8	422.6	404.2	**5.144**
7.5	7.5	7.5	10.0	7.5	7.5	7.5	**0.085**
780	899	1,225	1,581	694	888	1,080	**9.772**
411	587	701	610	485	492	720	**6,114**
434,244	434,244	434,244	434,244	434,244	446,343	446,343	
433,748	434,244	434,244	434,244	441,906	446,343	446,343	
	%						
2.12	1.28	2.17	2.47	1.34	3.11	2.90	
4.03	4.73	4.09	4.75	5.13	8.00	7.98	
3.94	2.72	4.82	5.92	3.28	7.33	6.96	
59.40	49.21	45.13	44.94	38.89	43.14	41.78	
23.73	35.13	45.01	52.74	81.55	52.10	54.21	

OPERATING ENVIRONMENT AND OVERVIEW

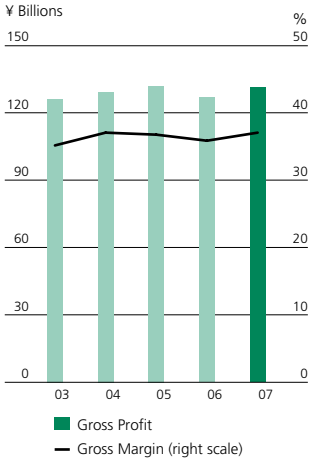
Despite weak consumer spending, the underlying tone of recovery continued in the Japanese economy during fiscal 2007, ended March 31, 2007, in an environment of increased capital investment and an improved employment situation against a backdrop of higher corporate earnings.

Regarding the operating environment for the Kyowa Hakko Group, Pharmaceuticals operations were faced with industrywide average reductions of 6.7% in NHI official drug prices, which were implemented in April 2006. In addition, global competition among companies increased further in the areas of pharmaceutical sales and new drug development, including a more aggressive stance by European and U.S. pharmaceutical companies and the growth of the generic drug market. Conditions remained challenging for Bio-Chemicals operations, which experienced a jump in raw material and fuel prices, while price competition intensified further, both in Japan and overseas. Chemicals operations were affected by the rise in crude oil prices, and domestic and overseas product prices generally remained high. Food operations were faced with the challenge of quickly responding to changes in the structure of the market associated with the diversification of consumers' dietary preferences.

Against this backdrop, the Kyowa Hakko Group made aggressive forward-looking investments based on its Ninth Medium-Term Management Plan, which spans a three-year period, and its fundamental management policy of growth and development. At the same time, efforts were made to strategically increase sales and carry out comprehensive cost reductions, as the Group worked to enhance the competitive strengths of its businesses.

As a result of these efforts, both net sales and operating income registered gains from the previous fiscal year, while net income declined on the booking of an extraordinary loss.

Gross Profit



SG&A Expenses

PROFIT AND LOSS

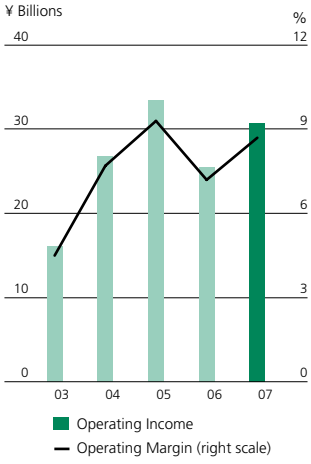
Sales

Net sales during fiscal 2007 edged up 0.2%, to ¥354.3 billion. Mainstay Pharmaceuticals operations recorded a decrease in sales from the oral antifungal agent Itrizole® due to the termination of a distribution agreement and NHI drug price revisions; however, Bio-Chemicals operations recorded higher sales, thanks to increased demand for pharmaceutical and industrial raw materials, both in Japan and overseas. In Chemicals operations, as product price revisions were carried out in response to higher prices for fuel and raw materials, revenues grew, resulting in a slight overall increase in net sales.

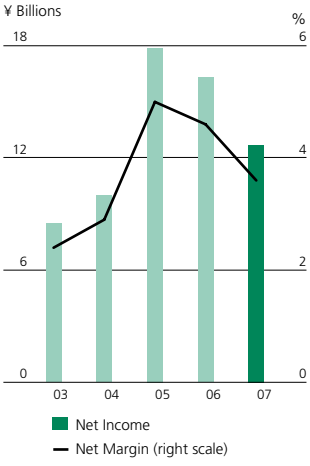
Cost of Sales and SG&A Expenses

The cost of sales declined 1.6%, to ¥222.8 billion, while the cost of sales ratio improved 1.2 percentage points, to 62.9%. Gross profit grew 3.5%, to ¥131.4 billion, with a 1.2 percentage point rise in the gross margin, to 37.1%. Selling, general and administrative (SG&A) expenses edged down 0.7%, to ¥100.7 billion, and SG&A expenses as a percentage of net sales was 0.3 percentage point lower, at 28.4%. Despite increases in R&D and sales promotion expenses, lower personnel and other expenses contributed to an overall decline.

Operating Income



Net Income



Operating Income

Operating income for the year grew 20.2%, to ¥30.7 billion, leading to a 1.5 percentage point rise in the operating margin, to 8.7%. Although revenue growth was minimal, the improvement in the gross margin and a reduction in SG&A expenses resulted in a large increase in operating income.

Other Revenue (Expenses)

Net other expenses grew significantly, to ¥7.2 billion, from the previous year's ¥0.7 billion. Although expenses on support for employees' early retirement declined to ¥0.4 billion from the previous year's ¥4.6 billion, no equity in gain of anonymous association was recorded, compared with a ¥2.2 billion gain in the previous year. The gain on sale of property, plant and equipment fell approximately ¥1.0 billion from the previous year. In addition, a ¥2.6 billion loss on sale of investments in affiliated companies was recorded, and the loss on impairment of fixed assets increased ¥1.3 billion.

As a result, income before income taxes and minority interests declined 5.4%, to ¥23.5 billion.

Income Taxes

Current and deferred income taxes totaled ¥10.9 billion, a 28.0% increase from the previous year. As a percentage of pretax net income, the effective tax rate was 46.2%, up from 34.1% in the previous year.

Net Income

Consequently, net income fell 22.0%, to ¥12.7 billion, while the net margin declined 1.0 percentage point, to 3.6%.

PERFORMANCE BY INDUSTRY SEGMENT

Sales, operating expenses, and operating income by industry segment are shown in the table on the following page. Segment performance figures include inter-segment transactions.

Pharmaceuticals

During the year, sales in this segment fell 11.7%, to ¥131.5 billion, and the business accounted for 33.9% of total net sales. Operating expenses were reduced 14.0%, to ¥115.8 billion, absorbing the decline in sales and resulting in a 10.4% increase in operating income, to ¥15.7 billion. Although a significant impact was evident following the termination of a distribution agreement for Itrizole® at the end of March 2006 and NHI drug price revisions that took effect in April 2006, sales volumes grew for high-margin main products, including the antiallergic agent Allelock®, and personnel expenses declined.

Bio-Chemicals

Sales from Bio-Chemicals operations rose 6.1%, to ¥67.1 billion, accounting for 17.3% of total sales. Operating expenses grew 7.0%, to ¥63.0 billion, for a 5.3% decrease in operating income, to ¥4.1 billion. Solid demand for pharmaceutical and industrial raw materials both in Japan and overseas contributed to these business results.

Chemicals

Sales rose 14.9%, to ¥98.7 billion, representing 25.4% of total sales. Operating expenses were 11.5% higher, at ¥90.7 billion, and operating income expanded 77.2%, to ¥8.0 billion. In addition to sales price revisions, the segment saw solid demand in Japan and overseas.

Food

Food sales edged up 0.4%, to ¥42.6 billion, and accounted for 11.0% of total sales. Operating expenses were 0.2% lower, at ¥40.8 billion, resulting in a 14.4% increase in operating income, to ¥1.8 billion. In addition to a contribution from higher sales of seasonings, processed foods performed well.

Other

The Group's Other segment registered increases in sales of 5.5%, to ¥48.5 billion, which represented 12.4% of total sales. Operating expenses rose 5.0%, to ¥47.5 billion, for a 36.1% increase in operating income, to ¥1.0 billion. The Other segment includes wholesale and transportation operations at subsidiaries.

	Millions of Yen						Thousands of U.S. Dollars[1]
	2007	2006	2005	2004	2003	2002	**2007**
Sales by Industry Segment:							
Pharmaceuticals	**¥131,526**	¥148,939	¥156,426	¥142,881	¥140,594	¥142,297	**$1,113,778**
Bio-Chemicals	**67,120**	63,241	57,767	69,195	58,525	55,496	**568,380**
Chemicals	**98,650**	85,835	77,983	66,899	65,158	60,410	**835,380**
Food[2]	**42,589**	42,440	44,500	45,912	72,322	103,531	**360,649**
Other	**48,480**	45,950	57,784	62,906	63,485	59,777	**410,534**
Corporate, elimination and other	**(34,091)**	(32,965)	(35,497)	(38,955)	(40,799)	(42,843)	**(288,687)**
Total	**¥354,274**	¥353,440	¥358,963	¥348,838	¥359,285	¥378,668	**$3,000,034**
Operating Income (Loss) by Industry Segment:							
Pharmaceuticals	**¥15,746**	¥14,268	¥18,100	¥11,943	¥11,014	¥18,959	**$133,339**
Bio-Chemicals	**4,112**	4,341	6,887	8,847	1,975	1,268	**34,821**
Chemicals	**7,974**	4,501	5,339	2,893	1,100	(1,174)	**67,525**
Food[2]	**1,832**	1,602	1,662	1,654	(368)	(440)	**15,514**
Other	**968**	711	1,634	1,767	2,597	1,756	**8,197**
Corporate, elimination and other	**67**	112	(115)	(268)	(229)	(12)	**567**
Total	**¥30,699**	¥25,535	¥33,507	¥26,836	¥16,089	¥20,357	**$259,963**

1. U.S. dollar amounts are translated from Japanese yen, for convenience only, at the rate of ¥118.09=US$1, the approximate exchange rate at March 31, 2007.
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.
3. Due to the reclassification of business segments effective from fiscal 2005, segment information for fiscal 2004 has been restated. However, segment information for years prior to fiscal 2004 has not been restated.
4. Due to the reclassification of the Other Segment effective from fiscal 2007, segment information for the Pharmaceuticals, Bio-Chemicals, and Other segments for fiscal 2006 has been restated. However, segment information for years prior to fiscal 2006 has not been restated.

CASH FLOWS

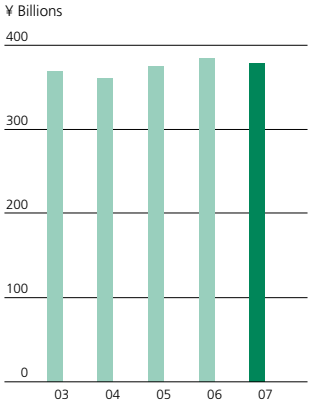
Net cash provided by operating activities in the year under review totaled ¥23.4 billion, for a ¥9.1 billion increase from the previous year. This rise was primarily because of lower income tax payments, despite a decline in income before income taxes and minority interests.

Net cash used in investing activities amounted to ¥8.5 billion, which was ¥6.7 billion higher than in the previous year. Proceeds from sale of investments in securities generated ¥4.0 billion in revenue; however, outlays for the acquisition of property, plant and equipment — the main expense item — came to ¥13.0 billion.

Net cash used in financing activities rose ¥19.3 billion from the previous year, to ¥24.4 billion. This was primarily because of a ¥20.5 billion increase in outlays for the acquisition of treasury stock.

As a result, cash and cash equivalents outstanding at the end of the year stood at ¥36.6 billion, marking a ¥9.2 billion decline from the previous fiscal year-end.

Total Assets



FINANCIAL POSITION

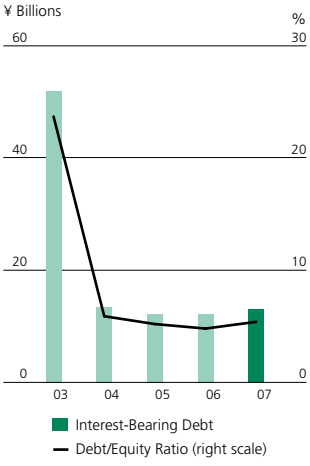
Assets

Current assets totaled ¥214.4 billion, a 0.6% increase from the previous fiscal year-end. With the July 2006 acquisition of treasury stock in the aggregate amount of ¥20.4 billion, declines were registered in the outstanding amounts of short-term commercial paper, which is included under marketable securities, and beneficiary rights for receivables in investment trusts, which is included under other current assets. However, because the last day of the fiscal year fell on a Saturday, the amount of accounts and notes receivable – trade was inflated.

Investments and other assets decreased 13.8% from the previous fiscal year-end, to ¥70.2 billion, primarily because of declines in investments in securities stemming from lower share prices of listed securities held and investments in and advances to unconsolidated subsidiaries and affiliates as a result of sales of affiliates' shares. With an increase in capital expenditures, property, plant and equipment grew 3.5%, to ¥91.2 billion.

As a result, total assets edged down 1.4%, to ¥378.9 billion.

Interest-Bearing Debt



Liabilities

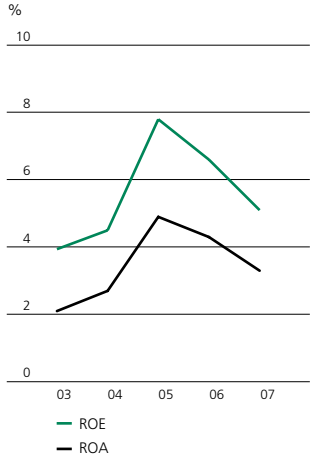
Current liabilities expanded 13.2% from the previous year-end, to ¥106.6 billion, with the increase primarily stemming from growth in accounts and notes payable and income taxes payable.

Long-term liabilities declined 13.8%, to ¥28.2 billion, mainly because of a 24.2% fall in deferred tax liabilities, to ¥5.6 billion, and a 12.7% reduction in the reserve for retirement benefits–employees, to ¥21.4 billion.

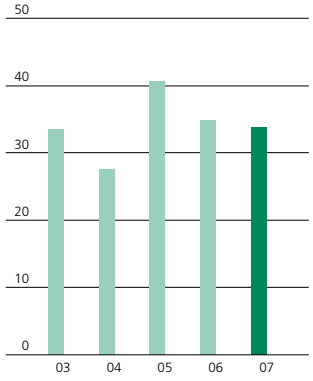
As a result, total liabilities rose 6.2%, to ¥134.8 billion.

Interest-bearing debt increased 7.5% from the previous year-end, to ¥13.1 billion, partly due to new additions to the scope of consolidation. Nevertheless, cash and deposits continued to be significantly larger than borrowings.

ROE and ROA



EBITDA



NET ASSETS

Net assets[1] shrank 5.2%, to ¥244.1 billion, primarily because of a decline in retained earnings associated with the acquisition and retirement of treasury stock.

As a result, the equity ratio decreased 2.8 percentage points, to 63.8%, from 66.6% at the previous fiscal year-end, while the debt / equity ratio[2] rose 0.6 percentage point, to 5.4%, from 4.8%. Nevertheless, we consider this level to be sufficiently safe.

MANAGEMENT INDEXES

Return on equity (ROE) declined to 5.10%, from 6.63% in the previous year, while return on assets (ROA) slid to 3.33%, from 4.29%, both reflecting lower net income. On the other hand, operating return on assets improved, from 6.73% to 8.04%, largely because of the significant growth in operating income.

The Ninth Medium-Term Management Plan emphasizes operating return on invested capital (ROIC)[3] as a key management index and sets a target of 12.0% for fiscal 2008. This index showed a major improvement during the year under review, rising to 11.1% at the fiscal year-end from the previous year's 9.2% and suggesting that fiscal 2008's target is achievable. EBITDA[4] for the term was 3.1% lower than in the previous year, at ¥33.8 billion.

CAPITAL EXPENDITURES

Capital expenditures in fiscal 2007 rose 33.5%, to ¥14.5 billion. Based on the Ninth Medium-Term Management Plan, which represents a "period of investment to build a foundation for future growth," the Group aggressively invested in plant and equipment for the future. This included the construction of a new production facility for the coenzyme Q10 in Bio-Chemicals operations and the expansion of production facilities for specialty chemicals in Chemicals operations, resulting in an increase in capital expenditures from the previous year.

At the same time, depreciation and amortization edged up 2.2%, to ¥10.0 billion. Capital expenditures surpassed depreciation by a wide margin, but this was fully covered with internal reserves.

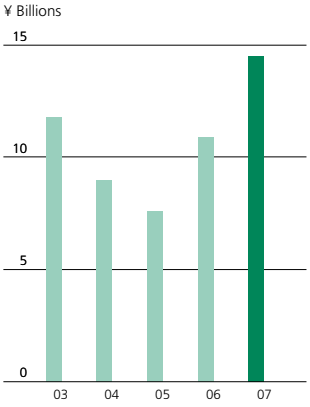
The breakdown of capital expenditures and depreciation and amortization are shown below.

Millions of Yen

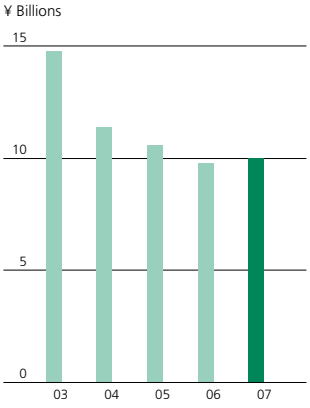
	Capital Expenditures			Depreciation and Amortization		
	2007	2006	2005	**2007**	2006	2005
Pharmaceuticals	**¥ 3,681**	¥3,898	¥2,733	**¥ 3,606**	¥3,913	¥4,371
Bio-Chemicals	**6,628**	2,317	2,216	**3,181**	2,642	2,684
Chemicals	**3,623**	3,407	1,622	**2,302**	2,283	2,344
Food	**886**	1,216	491	**799**	806	1,075
Other	**30**	32	586	**130**	159	110
Corporate, elimination and other	**(350)**	(11)	(1)	**(12)**	(14)	(19)
Total	**¥14,498**	¥10,859	¥7,647	**¥10,006**	¥9,789	¥10,565

1. Due to a change in accounting standards, effective from the year ended March 31, 2007, shareholders' equity has been changed to net assets, which includes shareholders' equity as well as minority interests in consolidated subsidiaries, share subscription rights, and net deferred profits on hedges. The figures for the previous year have been restated in conformity with this change.
2. Debt/equity ratio = Interest-bearing debt (short-term borrowings + current portion of long-term debt + long-term debt) / total shareholders' equity
3. ROIC = Operating income / total fixed assets + (accounts receivable + inventories – trade payables)
4. EBITDA = Income before income taxes and minority interests + interest expenses + depreciation and amortization

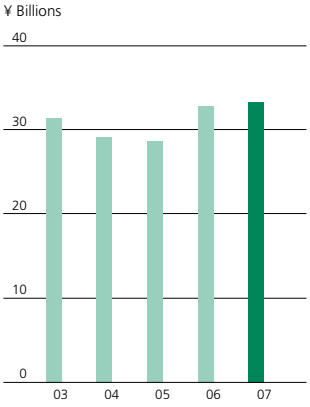
Capital Expenditures



Depreciation and Amortization



R&D Expenses



R&D EXPENSES

R&D expenses, which are included in production expenses and SG&A expenses, rose 1.4% for the year, to ¥33.3 billion. This was equivalent to 9.4% of consolidated net sales, marginally higher than the 9.3% recorded in the previous year. Although a decline was registered following the conclusion of phase III clinical trials for the Parkinson's treatment KW-6002 in Europe and the United States, expenses arose from the licensing-in of the inflammatory bowel disease treatment Asacol® from Zeria Pharmaceutical Co., Ltd., leading to growth in overall expenses. Pharmaceuticals operations accounted for 85.6% of R&D expenses, at ¥28.5 billion, which represented 21.7% of Pharmaceuticals sales — up from the previous year's level of 18.8%.

PER SHARE DATA

Net income per share — basic declined to ¥31.3 in fiscal 2007, from the previous year's amount of ¥38.4 per share, while net assets per share grew from ¥604.9 per share to ¥607.5 per share. Cash dividends per share were unchanged from the previous year, at ¥10.0 per share, which included an interim dividend of ¥5.0 per share.

DISTRIBUTION OF PROFITS

Kyowa Hakko considers returns to shareholders to be one of its most important management issues. The Company's basic policy on dividends calls for the enrichment of retained earnings to lay the foundations for future business development while making stable, continuous dividend payments, with comprehensive consideration given to consolidated results, the dividend payout ratio, and the dividends-on-equity ratio. In light of this policy and despite a decline in net income, the previous year's interim and year-end dividends of ¥5.0 per share, respectively, were maintained, for a full-year dividend of ¥10.0 per share. As a result, the dividend payout ratio for the year rose to 31.9%, from 26.1%.

The Company has earmarked retained earnings for investments in new growth, including investments in R&D and facilities, with a view toward future gains in corporate value.

TREASURY STOCK

Kyowa Hakko intends to raise capital efficiency by maintaining its flexible approach to the acquisition of treasury stock. During fiscal 2007, the Company spent a net ¥20.8 billion to purchase 24,999,638 shares. The total number of treasury stock shares declined 35,096,027, which included the retirement of 35,000,000 shares, resulting in 1,351,220 outstanding treasury stock shares at the fiscal year-end.

In the analysis of Kyowa Hakko's business performance and financial position, the major risks that could have a significant influence on the judgment of investors include those outlined below. The Group recognizes that these risk events may occur and uses a risk management system to prevent the occurrence of risk events that it is able to control. At the same time, the Company will do its utmost to respond to risk events if and when they were to occur. Matters in this section dealing with future events represent the judgment of the Kyowa Hakko Group as of March 31, 2007 – the end of the fiscal year under review.

RISKS INHERENT IN THE DOMESTIC PHARMACEUTICAL INDUSTRY'S OPERATING ENVIRONMENT

The Company's mainstay Pharmaceuticals operations face periodical reductions to the official prices of the majority of ethical drugs under the domestic public drug pricing system. As a result, the Company is unable to avoid reductions in the selling prices of its drugs.

RISK OF NON-RECOVERY OF SUBSTANTIAL R&D INVESTMENTS

The Company makes substantial R&D investments in the course of its development of new products and technologies, the improvement of existing products, and the development of new applications for existing products. However, there is no guarantee that all these investments will successfully bear fruit. For example, the development of new ethical drugs requires long periods of time and substantial R&D expenditures. Therefore, there may be instances in which the Company is unable to recover R&D investments for reasons including the cancellation of development if the expected efficacy is not recognized, lackluster sales after a product is launched, or the termination of sales because of the appearance of serious side effects.

RISKS RELATED TO INTELLECTUAL PROPERTY RIGHTS

The creation of new products and new technologies through R&D is a fundamental management strategy for Kyowa Hakko. The Company endeavors to accumulate technologies and acquire intellectual property (IP) rights to differentiate itself from other companies. Furthermore, the Group is strengthening its information control systems to prevent external leakages of its proprietary technologies and expertise. Although the Company strives to ensure that it does not infringe on the IP rights of others, there could be an adverse impact on the Group's market competitiveness in the event it is unable to appropriately protect or control such IP rights.

LEGAL RISKS

In the course of carrying out operations in Japan and overseas, statutory regulations must be observed. To ensure that it does not violate relevant statutory regulations in the course of its operations, the Company emphasizes compliance and works to bolster internal control functions through programs that include administrative oversight. However, the possibility that the Company could inadvertently fail to comply with statutory regulations cannot be entirely eliminated, and the failure to comply with statutory regulations could lead to a loss of public trust in the Company.

RISKS RELATED TO DEFECTIVE PRODUCTS

Kyowa Hakko manufactures a variety of products at plants in the countries in which it operates, in compliance with locally recognized quality control and other standards. Furthermore, the Company requires that the products it purchases for sale conform to the same quality and standards required of Kyowa Hakko products. However, there is no guarantee that all products will be free of defects. Therefore, the possibility of product defects leading to large-scale product recalls or product liability claims cannot be ruled out.

RISKS RELATED TO DISASTERS AND ACCIDENTS

To minimize the negative effects of interruptions in manufacturing line activities, the Company conducts regular disaster prevention tests and inspections of all its production facilities. Nevertheless, no guarantee exists that the Company will be able to completely prevent events that interrupt production, including accidents, electrical outages, and boiler stoppages. Furthermore, the Company handles flammable materials, including petrochemical products and raw material alcohol, as well as substances that are subject to an array of statutory regulations and guidelines. The handling of these materials is strictly controlled, but if a fire, natural disaster, or some other event were to occur surrounding areas could suffer damage. Such an accident or disaster could not only result in large payments for damages but also adversely affect the public's trust in the Group.

RISKS RELATED TO THE STRENGTHENING OF ENVIRONMENTAL REGULATIONS ON PRODUCTION ACTIVITIES

The Company processes and disposes of waste fluid generated from its fermentation production processes in accordance with the environmental regulations of the countries in which plants are situated. Furthermore, the Company is endeavoring to shift to raw materials that minimize the toll on the environment and improve its waste fluid treatment technology. However, given the trend of environmental regulations becoming more stringent each year, it is possible that regulatory changes could lead to restrictions on the Company's production activities or increased production costs.

RISKS INHERENT IN OVERSEAS BUSINESS ACTIVITIES

The Company operates in the United States and various countries throughout Europe and Asia. The development of operations in overseas markets entails a number of potential risks, which are outlined below.

- Unforeseeable laws and regulations or disadvantageous changes in tax systems
- The occurrence of disadvantageous political or economic factors
- Difficulty in recruiting and maintaining personnel
- Social unrest resulting from terrorism, war, or other factors

The occurrence of one or more of these potential risk events could prevent the Company from operating effectively in the affected country.

RISK OF DROPS IN PRODUCT PRICES FROM FLUCTUATIONS IN THE SUPPLY-DEMAND BALANCE

Market prices for some of the Company's products, including solvents and raw materials for plasticizers in Chemicals operations and seasonings in Food operations, fluctuate significantly in response to the worldwide balance of supply and demand. It is therefore possible that a situation of excess supply could result in substantial declines in sales prices for these products.

RISK OF DECLINES IN PROFITABILITY FROM MAJOR FLUCTUATIONS IN CRUDE OIL PRICES

The primary raw materials for the products of the Company's Chemicals operations include ethylene and propylene, which are made from naphtha, refined from crude oil. The prices of these raw materials are significantly affected by fluctuations in the price of crude oil, which can be triggered by a variety of unpredictable factors, including the worldwide balance of supply and demand, weather conditions, war, and terrorism. In some cases, the Company may not be able to factor fluctuations in raw materials prices into product prices, or offset fluctuations through cost reductions, in a timely manner.

CONSOLIDATED BALANCE SHEETS

KYOWA HAKKO KOGYO CO., LTD. AND ITS CONSOLIDATED SUBSIDIARIES
As at March 31, 2007 and 2006

ASSETS	Millions of Yen 2007	2006	Thousands of U.S. Dollars (Note 3) 2007
Current Assets:			
Cash and bank deposits	¥ 28,896	¥ 26,019	$ 244,695
Marketable securities	6,998	15,494	59,260
Accounts and notes receivable:			
Trade	99,026	90,991	838,564
Unconsolidated subsidiaries and affiliates	10,354	8,376	87,679
Other	2,098	2,436	17,766
	111,478	101,803	944,009
Inventories	56,015	55,486	474,342
Deferred tax assets (Note 7)	5,803	6,366	49,140
Other current assets	5,262	8,006	44,559
Less: allowance for doubtful accounts	(100)	(189)	(847)
Total Current Assets	214,352	212,985	1,815,158
Property, Plant and Equipment (Notes 6 and 11):			
Land	20,364	20,268	172,445
Buildings and structures	116,681	118,568	988,068
Machinery and equipment	214,699	211,619	1,818,097
Construction in progress	5,123	2,782	43,382
	356,867	353,237	3,021,992
Less: accumulated depreciation	(265,619)	(265,049)	(2,249,293)
	91,248	88,188	772,699
Investments and Other Assets:			
Investments in securities (Note 4)	54,489	58,447	461,419
Investments in and advances to unconsolidated subsidiaries and affiliates (Note 4)	10,518	18,764	89,068
Long-term loans to employees, mostly for housing	33	36	279
Long-term loans and other investments	6,158	5,848	52,147
Less: reserve for write-down of investments in securities	—	(449)	—
Less: allowance for doubtful accounts	(980)	(1,160)	(8,299)
	70,218	81,486	594,614
Deferred Tax Assets (Note 7)	313	343	2,651
Other Assets	2,740	1,379	23,202
Total Assets	¥ 378,871	¥ 384,381	$3,208,324

The accompanying notes are an integral part of the statements.

LIABILITIES AND NET ASSETS	Millions of Yen 2007	2006	Thousands of U.S. Dollars (Note 3) 2007
Current Liabilities:			
Short-term borrowings (Note 5)	¥ 12,887	¥ 12,204	$ 109,129
Accounts and notes payable:			
Trade (Note 4)	46,884	42,269	397,019
Unconsolidated subsidiaries and affiliates	6,489	5,223	54,950
Construction and acquisition of properties	4,589	3,389	38,860
Other	13,004	12,802	110,119
	70,966	63,683	600,948
Income taxes payable	7,080	3,828	59,954
Reserve for accrued sales returns	44	39	373
Reserve for accrued sales rebates	948	1,072	8,028
Reserve for accrued sales promotion expenses	717	718	6,072
Accrued bonuses	3,141	3,304	26,598
Reserve for periodic repairs	968	—	8,197
Guarantee deposits from customers	6,561	7,120	55,559
Other current liabilities	3,254	2,180	27,554
Total Current Liabilities	106,566	94,148	902,412
Long-Term Debt (Note 5)	250	12	2,117
Deferred Tax Liabilities (Note 7)	5,593	7,382	47,362
Reserve for Retirement Benefits:			
Employees (Note 9)	21,402	24,517	181,235
Directors and corporate auditors	108	92	915
Other Non-Current Liabilities	870	739	7,368
Total Long-Term Liabilities	28,223	32,742	238,997
Total Liabilities	134,789	126,890	1,141,409
Commitments and Contingent Liabilities (Notes 6 and 11)			
Net Assets:			
Shareholders' Equity (Note13)			
Common stock:			
Authorized: 987,900,000 shares at March 31, 2007 and 2006			
Issued: 399,243,555 shares at March 31, 2007			
434,243,555 shares at March 31, 2006	26,745	26,745	226,480
Additional paid-in capital	43,180	43,186	365,653
Retained earnings	151,565	170,718	1,283,470
Treasury stock, at cost 1,351,220 shares at March 31, 2007	(1,063)	(8,028)	(9,002)
Total Shareholders' Equity	220,427	232,621	1,866,601
Valuation, Translation Adjustments and Others			
Unrealized gains on available-for-sale securities (Note 4)	21,785	24,338	184,478
Net deferred profits on hedges	6	—	51
Translation adjustments	(502)	(1,152)	(4,251)
Total Valuation, Translation Adjustments and Others	21,289	23,186	180,278
Share Subscription Rights	66	—	559
Minority Interests in Consolidated Subsidiaries	2,300	1,684	19,477
Total Net Assets	244,082	257,491	2,066,915
Total Liabilities and Net Assets	¥378,871	¥384,381	$3,208,324

CONSOLIDATED STATEMENTS OF INCOME

KYOWA HAKKO KOGYO CO., LTD. AND ITS CONSOLIDATED SUBSIDIARIES
For the years ended March 31, 2007, 2006 and 2005

	Millions of Yen			Thousands of U.S. Dollars (Note 3)
	2007	2006	2005	2007
Net Sales (Note 16)	¥354,274	¥353,440	¥358,963	$3,000,034
Cost of Sales (Notes 6, 9 and 11)	222,849	226,457	226,850	1,887,112
Gross Profit	131,425	126,983	132,113	1,112,922
Selling, General and Administrative Expenses (Notes 6, 9 and 11)	100,726	101,448	98,606	852,959
Operating Income (Note 16)	30,699	25,535	33,507	259,963
Other Revenue (Expenses):				
Interest and dividend income	1,167	995	686	9,882
Interest expenses	(240)	(186)	(240)	(2,032)
Gain on sale of investments in securities	89	97	131	754
Foreign exchange gain	350	454	202	2,964
Insurance premium received	298	359	380	2,523
Equity in earnings of affiliates	832	680	564	7,045
Gain on sale of property, plant and equipment	680	1,667	155	5,758
Loss on disposal of inventory assets	(1,047)	(402)	(2,029)	(8,866)
Loss on impairment of fixed assets (Note 11)	(2,406)	(1,061)	—	(20,374)
Expenses on support for employees' early retirement	(390)	(4,640)	—	(3,303)
Loss on sale of investments in affiliated companies	(2,626)	—	—	(22,237)
Retroactive provision of reserve for periodic repairs	(1,016)	—	—	(8,604)
Industrial water obligation fee	(777)	—	—	(6,580)
Restructuring costs for affiliated companies	(267)	—	—	(2,261)
Reversal of reserve for cost of disposal of fixed assets	—	587	—	—
Equity in gain of anonymous association	—	2,222	304	—
Other, net	(1,820)	(1,435)	(3,757)	(15,411)
	(7,173)	(663)	(3,604)	(60,742)
Income before Income Taxes and Minority Interests	23,526	24,872	29,903	199,221
Income Taxes (Note 7):				
Current	10,456	6,887	11,334	88,543
Deferred	414	1,603	569	3,506
	10,870	8,490	11,903	92,049
	12,656	16,382	18,000	107,172
Minority Interests in Losses (Earnings) of Consolidated Subsidiaries	38	(109)	(68)	322
Net Income	¥ 12,694	¥ 16,273	¥ 17,932	$ 107,494

	Yen			U.S. Dollars (Note 3)
Per Share Data (Note 17):				
Net income — basic	¥31.3	¥38.4	¥41.7	$0.265
Net income — diluted (*)	31.3	38.3	—	0.265
Cash dividends	10.0	10.0	10.0	0.085
Weighted Average Number of Shares (Thousands of shares)	405,270	422,920	427,636	

* Diluted net income per share for fiscal 2005 is not disclosed because there were no residual securities.
The accompanying notes are an integral part of the statements.

CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS

KYOWA HAKKO KOGYO CO., LTD. AND ITS CONSOLIDATED SUBSIDIARIES

For the years ended March 31, 2007, 2006 and 2005

	Millions of Yen								
	Common stock	Additional paid-in capital	Retained earnings	Treasury stock, at cost	Net unrealized gains on available-for sale securities	Net deferred profits on hedges	Translation adjustment	Share subscription rights	Minority interests in consolidated subsidiaries
Balance at March 31, 2004	¥26,745	¥43,182	¥144,927	¥ (2,313)	¥14,637	¥—	¥(2,135)	¥—	¥1,389
Net income for the year ended March 31, 2005			17,932						
Cash dividends			(3,228)						
Directors' and corporate auditors' bonuses			(83)						
Increase due to subsidiaries newly included in consolidation			40						
Purchases of treasury stock				(5,525)					
Gain on sale of treasury stock		3		17					
Net changes during the year					670		571		69
Balance at March 31, 2005	26,745	43,185	159,588	(7,821)	15,307	—	(1,564)	—	1,458
Net income for the year ended March 31, 2006			16,273						
Cash dividends			(4,760)						
Directors' and corporate auditors' bonuses			(99)						
Decrease due to initial consolidation of subsidiaries			(284)						
Purchases of treasury stock				(239)					
Gain on sale of treasury stock		1		32					
Net changes during the year					9,031		412		226
Balance at March 31, 2006	26,745	43,186	170,718	(8,028)	24,338	—	(1,152)	—	1,684
Net income for the year ended March 31, 2007			12,694						
Cash dividends			(4,105)						
Directors' and corporate auditors' bonuses			(41)						
Decrease due to initial consolidation of subsidiaries			(25)						
Purchases of treasury stock				(20,755)					
Loss on sale of treasury stock		(6)	(5)	29					
Retirement of treasury stock			(27,671)	27,671					
Decrease due to exclusion of subsidiary accounted for by the equity method				20					
Net changes during the year					(2,553)	6	650	66	616
Balance at March 31, 2007	¥26,745	¥43,180	¥151,565	¥ (1,063)	¥21,785	¥6	¥ (502)	¥66	¥2,300

	Thousands of U.S. Dollars (Note 3)								
	Common stock	Additional paid-in capital	Retained earnings	Treasury stock, at cost	Net unrealized gains on available-for sale securities	Net deferred profits on hedges	Translation adjustment	Share subscription rights	Minority interests in consolidated subsidiaries
Balance at March 31, 2006	$226,480	$365,704	$1,445,660	$ (67,982)	$206,097	$ —	$(9,755)	$ —	$14,260
Net income for the year ended March 31, 2007			107,494						
Cash dividends			(34,762)						
Directors' and corporate auditors' bonuses			(347)						
Decrease due to initial consolidation of subsidiaries			(212)						
Purchases of treasury stock				(175,756)					
Loss on sale of treasury stock		(51)	(42)	246					
Retirement of treasury stock			(234,321)	234,321					
Decrease due to exclusion of subsidiary accounted for by the equity method				169					
Net changes during the year					(21,619)	51	5,504	559	5,217
Balance at March 31, 2007	$226,480	$365,653	$1,283,470	$ (9,002)	$184,478	$51	$(4,251)	$559	$19,477

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, 2007, 2006 and 2005

	Millions of Yen			Thousands of U.S. Dollars (Note 3)
	2007	2006	2005	2007
Cash Flows from Operating Activities:				
Income before income taxes and minority interests	¥23,526	¥ 24,872	¥ 29,903	$ 199,221
Adjustments to reconcile income before income taxes and minority interests to net cash provided by operating activities:				
Loss on impairment of fixed assets	2,406	1,061	—	20,374
Depreciation and amortization	10,006	9,789	10,565	84,732
(Decrease) in reserve for retirement benefits	(3,123)	(6,053)	(3,201)	(26,446)
(Decrease) increase in accrued bonuses	(163)	3,304	—	(1,380)
(Decrease) in reserve for cost of disposal of fixed assets	—	(1,308)	(518)	—
(Decrease) increase in allowance for doubtful accounts	(274)	(23)	474	(2,320)
Interest and dividend income	(1,167)	(995)	(686)	(9,882)
Interest expenses	240	186	240	2,032
Equity in earnings of affiliates	(832)	(680)	(564)	(7,045)
Equity in gain of anonymous association	—	(2,222)	(304)	—
(Gain) loss on disposal of property, plant and equipment	(82)	(959)	780	(694)
Increase in reserve for guarantee of liabilities	—	—	17	—
Increase in reserve for loss on investment	—	—	255	—
Increase in reserve for loss on liquidation of business	—	—	1,224	—
Loss (gain) on sale of securities	2,538	(97)	(131)	21,492
Loss on sale of investment in consolidated subsidiary	—	—	266	—
Expenses on support for employees' early retirement	390	4,640	—	3,303
(Increase) decrease in trade receivables	(9,274)	8,665	(361)	(78,533)
Decrease (increase) in inventories	38	(4,641)	(374)	322
Increase (decrease) in trade payables	4,689	(3,176)	2,176	39,707
Others	749	(6,170)	4,164	6,341
	29,667	26,193	43,925	251,224
Interest and dividend received	1,470	1,303	772	12,448
Interest expenses paid	(220)	(169)	(242)	(1,863)
Dividend of anonymous association received	—	2,590	—	—
Compensation payment incurred in connection with recalling products	—	—	(1,897)	—
Payment of expenses on support for employees' early retirement	(529)	(4,318)	—	(4,480)
Income taxes paid	(7,007)	(11,296)	(12,454)	(59,336)
Net Cash Provided by Operating Activities	23,381	14,303	30,104	197,993
Cash Flows from Investing Activities:				
Acquisition of property, plant and equipment	(13,040)	(9,001)	(7,265)	(110,424)
Proceeds from sale of property, plant and equipment	1,632	3,216	371	13,820
Acquisition of investments in securities	(68)	(63)	(138)	(576)
Proceeds from sale of investments in securities	3,951	4,117	179	33,458
Proceeds from sale of investments in consolidated subsidiaries	—	1,183	794	—
Net (increase) in short-term loans receivable	(117)	(439)	(260)	(991)
Increase in long-term loans receivable	—	(169)	—	—
Decrease in long-term loans receivable	23	332	65	195
Others	(875)	(972)	(1,850)	(7,410)
Net Cash (Used in) Investing Activities	(8,494)	(1,796)	(8,104)	(71,928)
Cash Flows from Financing Activities:				
Increase (decrease) in short-term debt	169	(141)	(319)	1,432
Increase in long-term debt	282	—	—	2,388
Repayment of long-term debt	(8)	(11)	(45)	(68)
Acquisition of treasury stock	(20,755)	(234)	(5,525)	(175,756)
Proceeds from sale of treasury stock	18	16	20	152
Dividends paid	(4,105)	(4,755)	(3,233)	(34,762)
Dividends paid to minority	(18)	(14)	(14)	(152)
Net Cash (Used in) Financing Activities	(24,417)	(5,139)	(9,116)	(206,766)
Effect of Exchanges on Cash and Cash Equivalents	238	381	14	2,015
(Decrease) Increase in Cash and Cash Equivalents	(9,292)	7,749	12,898	(78,686)
Cash and Cash Equivalents at the Beginning of the Year	45,820	37,818	24,911	388,010
Increase in Cash and Cash Equivalents Due to Consolidation of Certain Subsidiary	86	253	9	728
Cash and Cash Equivalents at the End of the Year	¥ 36,614	¥ 45,820	¥ 37,818	$ 310,052

Relation between cash and cash equivalents at year-end and the account booked in the balance sheets				
Cash and bank deposits	¥28,896	¥26,019	¥36,139	$244,695
Time deposits whose maturity periods exceed three months	(281)	(293)	(320)	(2,380)
Marketable securities with original maturities of three months or less	6,998	15,494	999	59,260
Investments in accounts receivable securitization	1,001	4,600	1,000	8,477
Cash and Cash Equivalents	¥36,614	¥45,820	¥37,818	$310,052

The accompanying notes are an integral part of the statements.

Note 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 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 the 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 2007" began on April 1, 2006 and ended on March 31, 2007.

Note 2

Summary of Significant Accounting Policies

(1) Principles of Consolidation

The Company had 41 subsidiaries as at March 31, 2007 (43 as at March 31, 2006). The consolidated financial statements include the accounts of the Company and 22 subsidiaries in fiscal 2007 (21 for fiscal 2006).

The remaining 19 (22 as at March 31, 2006) 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 financial statements of 8 (7 as at March 31, 2006) overseas consolidated subsidiaries prepare their financial statements on a calendar year basis. For all domestic consolidated subsidiaries, have adopted 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.

Any differences 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, have 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.

Major subsidiaries are as follows:

Name of company	Direct and indirect equity ownership percentage	Capital stock (Millions)
Domestic subsidiaries:		
Kyowa Hakko Chemical Co., Ltd.	100.0%	¥5,300
Kyowa Hakko Food Specialties Co., Ltd.	100.0	3,000
Kyowa Medex Co., Ltd.	100.0	450
Kyowa Wellness Co., Ltd.	100.0	30
Kyowa F.D. Foods Co., Ltd.	100.0	100
Miyako Kagaku Co., Ltd.	52.9	111
Chiyoda Kaihatsu Co., Ltd.	100.0	113
Overseas subsidiaries:		
BioWa, Inc. (U.S.A.)	100.0	$10
Biokyowa Inc. (U.S.A.)	100.0	$20
Shanghai Kyowa Amino Acid Co., Ltd.	70.0	YUAN156
Kyowa Hakko U.S.A., Inc. (U.S.A.)	100.0	$1
Kyowa Hakko Europe GmbH (Germany)	100.0	EURO1
Kyowa America, Inc. (U.S.A.)	100.0	$58

(2) Accounting for Investments in Unconsolidated Subsidiaries and Affiliates

The Company had 19 (22 at March 31, 2006) unconsolidated subsidiaries and 20 (20 at March 31, 2006) affiliates. The equity method is applied to the investments in 5 (6 at March 31, 2006) significant 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 investments in the remaining unconsolidated subsidiaries and affiliates are stated at cost or less.

(3) Cash and Cash Equivalents

Cash and cash equivalents in the consolidated statements of cash flows comprise cash on hand, bank deposits, which can 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.

(4) Securities Valuation

Held-to-maturity debt securities are valued at amortized 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 4.

(5) Inventories Valuation

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

(6) 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 is principally as follows:

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

Additional Information

For fiscal 2005, based on the Company's inquiry for the cancellation of rental agreements with tenants and prospective use of the property and equipment, the Company changed its useful life of certain rental property and equipment to the period until the tenants' exit, where the property and equipment is expected to be disposed of after the termination of the rental agreement with tenants. As a result, the depreciation of the property and equipment of ¥165 million was accounted for as extraordinary depreciation in "Other expenses."

(7) 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 is expected to be uncollectible due to bad financial condition or insolvency.

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 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 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 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 Periodic Repairs

The Company estimates expenditure needed for periodic repairs of manufacturing equipment in Chemicals operations and recognizes the part of this amount allocated to the year under review.

Accrued Bonuses to Employees

Accrued bonuses to employees are provided for bonuses payable to employees based on the amount expected to be paid at the year-end.

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.

Reserve for Retirement Benefits to Directors and Corporate Auditors

A reserve for retirement benefits to directors and corporate auditors is provided in accordance with the Company's internal rule.

Additional Information

On July 28, 2005, at the shareholders' meeting, the retirement benefits plan to directors and corporate auditors was terminated as a result of a change to the directors' compensation plan as a part of the restructuring plan of management. Prior to June 28, 2005, directors, including executive directors, and corporate auditors were covered by the retirement benefits plan to directors and corporate auditors and a reserve for retirement benefits to directors and corporate auditors was provided in accordance with the Company's internal rule. The benefits granted prior to the termination date of ¥404 million were recorded as "Other non-current liabilities."

(8) 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 "Net assets."

(9) 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 that 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 6.

(10) 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 to reduce the Companies' risk of fluctuation in interest and exchange rates. Therefore, the Companies' purchase of the hedging instruments is limited to, at maximum, the amounts of the hedged items.

The Companies evaluate the effectiveness of their hedging activities with 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.

(11) 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 7 for details of deferred tax assets/liabilities.

(12) Accounting for Consumption Taxes

In Japan, consumption taxes are imposed at a flat rate of five 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 subsequently paid to the national government and the local public body. 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 Corporation Law of Japan (the "Law"), the appropriation of retained earnings with respect to a given financial period is made by resolution of the shareholders at a general meeting held subsequent to the close of such financial period. The accounts for that period do not, therefore, reflect such appropriations. See Note 13.

(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) Amortization of Goodwill and Negative Goodwill

The Company uses the straight-line method to amortize regularly goodwill over an effective period of within 20 years and negative goodwill over an appropriate period of within 20 years based on the circumstances of acquisition. If the amount of goodwill/negative goodwill is immaterial, it is charged to income when incurred.

(16) Reclassification

Certain fiscal 2006 and 2005 figures have been reclassified to conform to the current year representation.

(17) Additional Information

The fiscal year-end of March 31, 2007 fell on a bank holiday. As a result, notes receivable/payable were not accounted for as settled until the date of exchange. Therefore, the following items were included in the accompanying consolidated balance sheets as of March 31, 2007 and remained unsettled.

	Millions of Yen	Thousands of U.S. Dollars
	2007	2007
Notes receivable	¥3,355	$28,411
Notes payable	1,927	16,318
Notes payable for construction included in "Other current liabilities"	51	432

In addition, the following receivable/payable balances, which originally fell due at the fiscal year-end, are included in the accompanying consolidated balance sheets as of March 31, 2007, because those balances are settled in the same way as for notes receivable/payable.

	Millions of Yen	Thousands of U.S. Dollars
	2007	2007
Accounts receivable—trade	¥5,121	$43,365
Accounts payable—trade	5,144	43,560
Accounts payable—other	1,489	12,609

New Accounting Standard

Accounting for impairment of fixed assets

On August 9, 2002, the Business Accounting Council issued a new accounting standard, "Accounting Standard for Impairment of Fixed Assets," and on October 31, 2003 the Accounting Standards Board of Japan issued the Financial Accounting Standards Implementation Guidance No. 6, "Implementation Guidance for Accounting Standard for Impairment of Fixed Assets." The Companies applied the adoption of the new accounting standard for impairment of fixed assets in the fiscal year beginning on April 1, 2005. As a result of adopting the new accounting standard, income before taxes and minority interests for the year ended March 31, 2006 decreased ¥1,061 million. Accumulated impairment losses are deducted directly from related fixed assets.

Accounting standard for presentation of net assets in the balance sheet
For fiscal 2007, the Company adopted the Accounting Standard for Presentation of Net Assets in the Balance Sheet (ASBJ Statement No. 5, December 9, 2005) and Guidance on Accounting Standard for Presentation of Net Assets in the Balance Sheet (ASBJ Guidance No. 8, December 9, 2005). In this connection, the previously reported consolidated balance sheet as of March 31, 2006 and the consolidated statements of shareholders' equity for the years ended March 31, 2006 and 2005 have been restated to conform to the presentation and disclosure of the consolidated financial statements for the year ended March 31, 2007.

Accounting standard for stock options, etc.
For fiscal 2007, the Company adopted Accounting Standard for Share-Based Payment (ASBJ Statement No. 8, December 27, 2005) and Guidance on Accounting Standard for Share-Based Payment (ASBJ Guidance No. 11, May 31, 2006). As a result, operating income and income before income taxes and minority interests for the year ended March 31, 2007 decreased ¥65 million ($550 thousand), respectively.

Reserve for periodic repairs
Previously, expenses for periodic repairs of production facilities in Chemicals operations were charged to income when incurred. However, with effect from fiscal 2007 the Company recognized the part of estimated expenditure allocated to the year under review as reserve for periodic repairs.

In light of the introduction of a quarterly financial reporting system from the year beginning April 1, 2008, the Company made this change to increase the accuracy of periodic income statements and further the soundness of its financial position by allocating expenses to reflect the operational period until the next periodic repairs are needed.

As a result, compared with the previous method, operating income increased ¥230 million ($1,948 thousand), and income before income taxes and minority interests increased ¥786 million ($6,656 thousand) for the year ended March 31, 2007. Further, the effect on segment information is described in Note 16.

Note 3
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 ¥118.09=U.S.$1, the approximate exchange rate at March 31, 2007. 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 ¥118.09=U.S.$1 or at any other rate.

Note 4
Securities

a) Available-for-sale securities for which market value is available as of March 31, 2007 and 2006 are as follows:

	2007		
	Millions of Yen		
	Historical cost	Fair market value	Unrealized gain (loss)
Securities with unrealized gain:			
Shares	¥7,245	¥44,351	¥37,106
Securities with unrealized loss:			
Shares	331	315	(16)

	2007		
	Thousands of U.S. Dollars		
	Historical cost	Fair market value	Unrealized gain (loss)
Securities with unrealized gain:			
Shares	$61,352	$375,569	$314,217
Securities with unrealized loss:			
Shares	2,803	2,667	(136)

	2006		
	Millions of Yen		
	Historical cost	Fair market value	Unrealized gain (loss)
Securities with unrealized gain:			
Shares	¥7,533	¥48,572	¥41,039
Securities with unrealized loss:			
Shares	16	14	(2)

b) The details of investments in securities without market quotation in 2007 and 2006 are as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	2007
Held-to-maturity debt securities:			
Commercial paper	**¥6,998**	¥15,494	**$59,260**
Available-for-sale securities:			
Unlisted shares	**8,819**	8,855	**74,680**
Other securities	**1,004**	1,006	**8,502**

c) The maturity schedule of available-for-sale securities with scheduled maturity as at March 31, 2007 is as follows:

	Millions of Yen
	2007
Less than one year	**¥6,998**
More than one year, less than five years	**4**
More than five years, less than ten years	**—**
Thereafter	**—**

	Thousands of U.S. Dollars
	2007
Less than one year	**$59,260**
More than one year, less than five years	**34**
More than five years, less than ten years	**—**
Thereafter	**—**

d) Assets pledged as collateral and relevant debt as at March 31, 2007 and 2006 consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	2007
Investments in securities	**¥914**	¥642	**$7,740**
Accounts and notes payable — trade	**793**	619	**6,715**

e) Investments in unconsolidated subsidiaries and affiliates as at March 31, 2007 and 2006 were:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	2007
Investments in shares	**¥7,899**	¥13,797	**$66,890**
Participations	**2,009**	3,716	**17,012**

Note 5

Short-Term and Long-Term Debt

Short-term debt consisted principally of bank overdrafts bearing interest of 1.41% and 0.76%, which was the weighted-average interest rate on outstanding balances as at March 31, 2007 and 2006, respectively. It is a normal business custom in Japan for short-term bank loans to be rolled over each year.

Short-term borrowings as at March 31, 2007 and 2006 are summarized as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	**2007**
Short-term bank loans	¥12,822	¥12,198	$108,579
Current portion of long-term borrowings	65	6	550
	¥12,887	¥12,204	$109,129

Long-term debt as at March 31, 2007 and 2006 consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	**2007**
Loans from banks, other financial institutions, etc., due from 2008 to 2012 with mortgage and collateral (Remarks 1 and 2)	**¥250**	¥12	**$2,117**

Remarks: 1. The weighted-average interest rate on outstanding balances of long-term loans (excluding current portion) from banks at the year-end was 5.51%.

2. 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 interest on the bond.
See Note 12 for underlying obligations of the Company.

Annual maturities of long-term debt subsequent to March 31, 2007, except for bonds, are as follows:

	Millions of Yen	Thousands of U.S. Dollars
Within one year	¥ 65	$ 550
More than one year, less than two years	63	534
More than two years, less than three years	63	533
More than three years, less than four years	62	525
More than four years, less than five years	62	525
More than five years	—	—
	¥315	$2,667

Note 6

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, 2007 and 2006 is as follows.

The acquisition cost, accumulated depreciation and net book value of leased assets at March 31, 2007 and 2006 were as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	**2007**
Acquisition cost	**¥1,515**	¥1,882	**$12,829**
Accumulated depreciation	**776**	1,032	**6,571**
Net book value	**¥ 739**	¥ 850	**$ 6,258**

Lease payments for the years ended March 31, 2007 and 2006 were ¥315 million ($2,667 thousand) and ¥378 million, respectively.

Depreciation equivalents for the years ended March 31, 2007 and 2006 were ¥315 million ($2,667 thousand) and ¥378 million, respectively.

Depreciation equivalent 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, 2007 and 2006 were as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	2007
Due within one year	¥268	¥323	$2,269
Due over one year	471	527	3,989
	¥739	¥850	$6,258

(2) Operating Leases

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	2007
Due within one year	¥0	¥3	$0
Due over one year	—	0	—
	¥0	¥3	$0

Note 7

Income Taxes

The tax effects of temporary differences that give rise to significant portions of deferred tax assets and liabilities as of March 31, 2007 and 2006 are as follows:

	March 31, 2007	
	Millions of Yen	Thousands of U.S. Dollars
Deferred tax assets:		
Non-deductible portion of reserve for retirement benefits to employees	¥ 8,071	$ 68,346
Non-deductible portion of depreciation of property, plant and equipment	2,146	18,173
Reserve for bonuses	1,275	10,797
Deferred assets for tax purposes	1,234	10,450
Prepaid expense for tax purposes	1,215	10,289
Others	9,338	79,074
Sub-total	23,279	197,129
Valuation allowance	(5,318)	(45,033)
Total deferred tax assets	¥ 17,961	$ 152,096
Deferred tax liabilities:		
Deferred gain, mainly related to expropriation of fixed assets	¥ (2,086)	$ (17,664)
Unrealized gains on available-for-sale securities	(15,050)	(127,445)
Others	(302)	(2,558)
Total deferred tax liabilities	(17,438)	(147,667)
Deferred tax assets, net	¥ 523	$ 4,429

The classification of "Deferred tax assets, net" on the consolidated balance sheets as of March 31, 2007 is as follows:

Balance sheet item		Millions of Yen	Thousands of U.S. Dollars
Current assets	Deferred tax assets	¥ 5,803	$ 49,140
Non-current assets	Deferred tax assets	313	2,651
Non-current liabilities	Deferred tax liabilities	(5,593)	(47,362)
		¥ 523	$ 4,429

Remark: 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.

	March 31, 2006
	Millions of Yen
Deferred tax assets:	
Reserve for bonuses	¥ 1,343
Non-deductible portion of reserve for retirement benefits to employees	9,983
Prepaid expense for tax purposes	1,840
Non-deductible portion of depreciation of property, plant and equipment	1,224
Loss on write-down of fixed assets held by overseas subsidiaries	955
Others	8,252
Sub-total	23,597
Valuation allowance	(5,000)
Total deferred tax assets	¥ 18,597
Deferred tax liabilities:	
Deferred gain, mainly related to expropriation of fixed assets	¥ (2,188)
Unrealized gains on available-for-sale securities	(16,653)
Others	(429)
Total deferred tax liabilities	(19,270)
Deferred tax assets, net	¥ (673)

Classification of "Deferred tax assets, net" on the consolidated balance sheets as of March 31, 2006 is as follows:

Balance sheet item		Millions of Yen
Current assets	Deferred tax assets	¥6,366
Non-current assets	Deferred tax assets	343
Non-current liabilities	Deferred tax liabilities	(7,382)
		¥ (673)

Remark: 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, 2007 and 2006 is as follows:

	2007	2006
Statutory tax rate	**40.7%**	40.7%
Permanent differences:		
Non-deductible expenses, such as entertainment expenses	**5.6**	5.8
Loss on sale of equity method affiliates' shares	**4.5**	—
Future tax benefits deemed not to be realized	**3.7**	(5.2)
Equity in earnings of affiliates	**(1.4)**	(1.1)
Non-taxable income, such as dividend income	**(1.5)**	(0.9)
Special corporate tax credit	**(5.1)**	(3.5)
Others	**(0.3)**	(1.7)
Effective tax rate	**46.2%**	34.1%

Note 8

Stock Option Plans

a) The following table summarizes the contents of stock options as of March 31, 2007.

	2007 Plan	2006 Plan
Grantees' position	Directors and Executive Officers	Directors and Executive Officers
Number of grantees	18	19
Type of stock	Common stock	Common stock
Date of grant	June 29, 2006	June 28, 2005
Vesting condition	No provisions	No provisions
Applicable period of service	No provisions	No provisions
Exercisable period	June 30, 2006 – June 28, 2026	June 29, 2005 – June 28, 2025

b) The following table summarizes scale and movement of stock options as of March 31, 2007.

	2007 Plan	2006 Plan
Non-vested (number of shares):		
Stock options outstanding at April 1, 2006	—	—
Granted during the year	111,000	—
Forfeited during the year	—	—
Vested during the year	111,000	—
Stock options outstanding at March 31, 2007	—	—
Vested (number of shares):		
Stock options outstanding at April 1, 2006	—	133,000
Vested during the year	111,000	—
Exercised during the year	—	19,000
Forfeited during the year	—	—
Stock options outstanding at March 31, 2007	111,000	114,000

c) The following tables summarize the price information of stock options as of March 31, 2007.

	2007 Plan	2006 Plan
Exercise price (yen)	¥ 1	¥ 1
Average market price of the stock at the time of exercise (yen)	—	775
Fair valuation price (date of grant) (yen)	705	—

d) Method of estimating the fair value of stock options

① Valuation method used: Black-Scholes model

② Principal basic numeric values and estimation methods

	2007 Plan
Share price variability (Remark 1)	6%
Projected remaining period (Remark 2)	5 years
Projected dividends (yen) (Remark 3)	¥10/per share
Risk-free interest rate (Remark 4)	0.58%

Remarks:
1. Calculated based on share price results over five years (from June 2001 to May 2006).
2. Calculated by subtracting the average years of service of present office holders from the average years of service of retirees over the past five years.
3. Based on dividends for the year ended March 2006.
4. The rate of return on government bonds over the projected remaining period.

e) Method of estimating number of stock option vestings

In principle, because reasonable estimations of future expirations are problematic, a method reflecting actual expirations is used.

Note 9

Reserve for Retirement Benefits to Employees

The Company and its domestic consolidated subsidiaries operate various defined benefit plans, including a corporate pension plan (the so-called cash-balanced plan), a group contributory plan, a tax-qualified pension plan and a severance payment plan.

a) The reserve for retirement benefits as of March 31, 2007 and 2006 is analyzed as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	**2007**
Projected benefit obligations	**¥(62,221)**	¥(61,680)	**$(526,895)**
Plan assets	**42,888**	38,157	**363,181**
Unfunded benefit obligations	**(19,333)**	(23,523)	**(163,714)**
Unrecognized actuarial differences	**1,660**	2,578	**14,057**
Unrecognized prior service costs	**(2,350)**	(3,572)	**(19,900)**
Prepaid pension cost	**(1,379)**	—	**(11,678)**
	¥(21,402)	¥(24,517)	**$(181,235)**

Remark: Reserve for certain subsidiaries calculate the projected benefit obligation by the simplified method permitted under the accounting standards generally accepted in Japan.

b) The net periodic pension expense related to the retirement benefits for fiscal 2007, 2006 and 2005 is as follows:

	Millions of Yen			Thousands of U.S. Dollars
	2007	2006	2005	**2007**
Service cost (Remark)	**¥(2,445)**	¥(2,595)	¥(2,650)	**$(20,705)**
Interest cost	**1,518**	1,575	1,583	**12,855**
Expected return on plan assets	**(1,136)**	(1,011)	(736)	**(9,620)**
Amortization of unrecognized actuarial differences	**1,158**	1,457	1,628	**9,806**
Amortization of unrecognized prior service costs	**(1,222)**	(1,432)	(1,431)	**(10,348)**
Special severance payment	**202**	4,364	—	**1,771**
	¥ 2,965	¥ 7,548	¥ 3,694	**$ 25,109**

Remark: Includes net periodic pension expense incurred by the subsidiaries that apply the simplified method.

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

	As of March 31, 2007	As of March 31, 2006	As of March 31, 2005
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	3.0%	3.3%	2.8%

Note 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 swap, foreign exchange contract and interest rate swap and cap agreements.

All such instruments involve risk, including the credit risk of non-performance by counterparties. However, at March 31, 2007, 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

The Companies have the following derivatives contracts outstanding at March 31, 2007 and 2006:

		Millions of Yen					
		2007			2006		
Classification	Type of transaction	Contract amount	Fair value	Unrealized gain (loss)	Contract amount	Fair value	Unrealized gain (loss)
Non-market transactions	Foreign exchange forward contracts						
	Buying U.S. dollar	¥2,310	¥2,341	¥31	¥—	¥—	¥—
	Buying Euro	2,095	2,086	(9)	—	—	—
		¥4,405	¥4,427	¥22	¥—	¥ —	¥—

		Thousands of U.S. Dollars		
		2007		
Classification	Type of transaction	Contract amount	Fair value	Unrealized gain (loss)
Non-market transactions	Foreign exchange forward contracts			
	Buying U.S. dollar	$19,561	$19,824	$263
	Buying Euro	17,741	17,664	(77)
		$37,302	$37,488	$186

Remarks: 1. Fare value is determined based on the foreign currency forward exchange market rates.
2. Derivative transactions utilized by the Companies other than above are applied by hedge accounting and are not included in the above.

Note 11

Supplementary Statements of Income

a) The significant elements of selling, general and administrative expenses for each of the three years in the period ended March 31, 2007, 2006 and 2005 are as follows:

	Millions of Yen			Thousands of U.S. Dollars
	2007	2006	2005	2007
Research and development expenses	¥32,687	¥32,318	¥28,325	$276,797
Salaries	16,888	17,018	17,342	143,010
Sales promotion	8,475	8,186	7,016	71,767
Bonuses to employees	5,523	5,980	7,786	46,769
Transportation expense	3,948	4,061	4,677	33,432
Provision for accrued bonuses	1,735	1,896	—	14,692

b) Loss on impairment of fixed assets

The Companies have made a group of fixed assets for impairment testing by the management accounting unit. However, the Company classifies certain assets as a separate unit for impairment testing. The assets include assets held for lease, idle assets and assets held for sale or disposition.

For the fiscal year ended March 31, 2007, the Companies recognized impairment loss for the following group of assets:

Location	Description	Classification	Millions of Yen	Thousands of U.S. Dollars
Five locations, including a pharmaceutical distribution center in Tokyo (Itabashi-ku, Tokyo, etc.)	Assets scheduled for disposal	Buildings and equipment	¥1,310	$11,093
Hofu Plant and other two locations (Hofu City, Yamaguchi Prefecture, etc.)	Idle assets	Buildings and equipment	1,095	9,273

The Companies wrote down the book value to recovery value and accounted for its diminution in "Loss on impairment of fixed assets." The reason was that assets scheduled for disposal in five locations are scheduled for sale or disposal, and idle assets in two locations are idle or expected to halt operations or their future use has not been decided. Further, the recovery value was measured by the net sales value. The idle assets which would be difficult to dispose of and assets scheduled for disposal were measured at one yen.

For the fiscal year ended March 31, 2006, the Companies recognized impairment loss for the following group of assets.

Location	Description	Classification	Millions of Yen
Six locations, including Houki Town, Saihaku County, Tottori Prefecture	Idle assets	Land	¥187
Toxicological Research Laboratories	Idle assets	Buildings	551
Company housing of Kyowa Hakko Chemical Co., Ltd.	Assets scheduled for disposal	Buildings, other	323

The Companies wrote down the book value to recovery value and accounted for its diminution in "Loss on impairment of fixed assets." The reason was that the market price of idle land in six locations fell significantly, a part of the buildings of the Toxicological Research Laboratories had been idle, and its purpose for future use had not been determined, and the Company's housing of Kyowa Hakko Chemical Co., Ltd. was determined to be disposed of. The recovery value was measured by the net sales value. The idle land was valued by the adjusted assessed value of fixed assets based on the valuation for property taxes. The idle building which would be difficult to dispose of and assets scheduled for disposal were measured at one yen.

c) Industrial water obligation fee
Industrial water obligation fee (compensation) arose from the return in part of the fee under the industrial water-supply contract between the Company's Hofu Plant and Yamaguchi Prefecture.

Note 12

Contingent Liabilities

a) The Company and its consolidated subsidiaries had contingent liabilities arising from notes discounted by banks in the amount of ¥62 million ($525 thousand) at March 31, 2007.

The Company and its consolidated subsidiaries are contingently liable for guarantees of loans borrowed by Kyowa Hakko Pharmaceuticals (Suzhou) Co., Ltd. and others in the amounts of ¥700 million ($5,928 thousand) and ¥460 million ($3,895 thousand), respectively, at March 31, 2007.

b) Contingent liabilities under a debt assumption contract totaled ¥33,000 million ($279,448 thousand).

Note 13

Supplementary Information for Shareholders' Equity

(1) Type and number of outstanding shares

		Number of shares Fiscal 2007
Common stock:		
Balance at beginning of the year		434,243,555
Increase in shares during the year		—
Decrease in shares during the year	(Remark 1)	35,000,000
Balance at end of the year		399,243,555
Treasury stock:		
Balance at beginning of the year		11,447,609
Increase in shares during the year	(Remark 2)	24,999,638
Decrease in shares during the year	(Remark 3)	35,096,027
Balance at end of the year		1,351,220

Remarks: 1. Outstanding shares of common stock decreased by 35,000,000 shares due to the retirement of treasury stock.
2. Treasury stock increased by 24,999,638 shares due to the purchases of treasury stock based on the resolution of board of directors by 24,626,000 shares and the repurchase of shares less than one unit by 373,638 shares.
3. Treasury stock decreased by 35,096,027 shares due to the retirement of treasury stock by 35,000,000 shares, the decrease due to sales of equity method affiliates' shares by 55,670 shares, the stock options exercised by 19,000 shares and the sale of shares less than one unit by 21,357 shares.

(2) Share subscription rights

			Number of Shares			Balance at March 31, 2007		
Company	Description	Type of shares	At the end of the prior fiscal year	Increase	Decrease	At the end of the prior fiscal year	Millions of Yen	Thousands of U.S. Dollars
Parent company	Subscription rights as stock options	—					¥66	$559

(3) Dividends

a) Dividends paid to shareholders

Date of approval	Resolution approved by	Type of shares	Amount (Millions of Yen)	Amount (Thousands of U.S. dollars)	Per share (Yen)	Per share (U.S. dollars)	Shareholders' cut-off date	Effective date
June 28, 2006	Annual general meeting of shareholders	Common stock	¥2,114	$17,902	¥5	$0.042	March 31, 2006	June 29, 2006
October 30, 2006	Board of directors	Common stock	1,991	16,860	5	0.042	September 30, 2006	December 1, 2006

b) Dividends with a shareholders' cut-off date during the current fiscal year but an effective date subsequent to the current year.

Date of approval	Resolution approved by	Type of shares	Amount (Millions of Yen)	Amount (Thousands of U.S. dollars)	Per share (Yen)	Per share (U.S. dollars)	Shareholders' cut-off date	Effective date
June 20, 2007	Annual general meeting of shareholders	Common stock	¥1,989	$16,843	¥5	$0.042	March 31, 2007	June 21, 2007

Note 14

Related Party Transactions

The Company discloses significant 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 for the years ended March 31.

Also, the Company discloses significant balances and transactions with related companies where such balances and transactions, including the related amounts in the footnote, represent more than one 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 2007, 2006 or 2005.

Significant transactions and balances of the Company with its related individuals, including shareholders and directors, representing more than ¥1 million shall be disclosed, however no such transactions and balances were noted for the years ended March 31, 2007, 2006 and 2005.

Note 15

Cash Flow Information

(1) Summary of assets and liabilities excluded following the transfer of Agroferm:

	Millions of Yen
	2005
Current assets	¥2,144
Fixed assets	941
Total assets	¥3,085
Current liabilities	¥ 399
Non-current liabilities	—
Total liabilities	¥ 399

Note 16

Segment Information

(1) Industry Segment Information

The Companies operate principally in the following five industry segments:

Industry segments:	Major products:
(1) Pharmaceuticals Division	Ethical drugs and diagnostic reagents
(2) Bio-Chemicals Division	Pharmaceutical and industrial use raw materials, health care products, agrochemicals, products for livestock and fisheries industries and alcohol
(3) Chemicals Division	Solvents, raw materials of plasticizers and specialty chemicals
(4) Food Division	Seasonings, baking products and ingredients and processed foods
(5) Other Division	Transportation and facilities

Millions of Yen

Year ended March 31, 2007	Industry segment						Corporate, elimination and other	Consolidated total
	Pharmaceuticals	Bio-Chemicals	Chemicals	Food	Other	Total		
I. Sales and Operating Income:								
Sales:								
Sales to outside customers	¥130,879	¥57,055	¥92,099	¥38,447	¥35,794	¥354,274	¥ —	¥354,274
Inter-segment sales/transfers	647	10,065	6,551	4,142	12,686	34,091	(34,091)	—
Total sales	131,526	67,120	98,650	42,589	48,480	388,365	(34,091)	354,274
Operating expenses	115,780	63,008	90,676	40,757	47,512	357,733	(34,158)	323,575
Operating income	¥ 15,746	¥ 4,112	¥ 7,974	¥ 1,832	¥ 968	¥ 30,632	¥ 67	¥ 30,699
II. Assets, Depreciation and Amortization, Loss on Impairment of Fixed Assets and Capital Expenditures:								
Assets	¥117,778	¥85,871	¥83,523	¥34,775	¥22,632	¥344,579	¥34,292	¥378,871
Depreciation and amortization	3,606	3,181	2,302	799	130	10,018	(12)	10,006
Loss on impairment of fixed assets	815	940	138	513	—	2,406	—	2,406
Capital expenditures	3,681	6,628	3,623	886	30	14,848	(350)	14,498

Thousands of U.S. Dollars

Year ended March 31, 2007	Industry segment						Corporate, elimination and other	Consolidated total
	Pharmaceuticals	Bio-Chemicals	Chemicals	Food	Other	Total		
I. Sales and Operating Income:								
Sales:								
Sales to outside customers	$1,108,299	$483,148	$779,905	$325,574	$303,108	$3,000,034	$ —	$3,000,034
Inter-segment sales/transfers	5,479	85,232	55,475	35,075	107,426	288,687	(288,687)	—
Total sales	1,113,778	568,380	835,380	360,649	410,534	3,288,721	(288,687)	3,000,034
Operating expenses	980,439	533,559	767,855	345,135	402,337	3,029,325	(289,254)	2,740,071
Operating income	$ 133,339	$ 34,821	$ 67,525	$ 15,514	$ 8,197	$ 259,396	$ 567	$ 259,963
II. Assets, Depreciation and Amortization, Loss on Impairment of Fixed Assets and Capital Expenditures:								
Assets	$997,358	$727,166	$707,283	$294,479	$191,649	$2,917,935	$290,389	$3,208,324
Depreciation and amortization	30,536	26,937	19,494	6,766	1,101	84,834	(102)	84,732
Loss on impairment of fixed assets	6,902	7,960	1,169	4,343	—	20,374	—	20,374
Capital expenditures	31,171	56,127	30,680	7,503	254	125,735	(2,964)	122,771

For fiscal 2007, the Company recognized part of estimated expenditure allocated to the year under review as reserve for periodic repairs. As a result, compared with the previous method, operating income increased ¥230 million ($1,948 thousand) in "Chemicals" segment.

The Company reviewed the operations of some consolidated subsidiaries in Pharmaceuticals operations and other operations and changed the division of the Group's managerial control. As a result, the Company included these consolidated subsidiaries in Bio-Chemicals operations from fiscal 2007.

The industry segment information for fiscal 2006 has been restated accordingly. (However, the industry segment Information for fiscal 2005 has not been restated.)

Millions of Yen

Year ended March 31, 2006	Industry segment						Corporate, elimination and other	Consolidated total
	Pharmaceuticals	Bio-Chemicals	Chemicals	Food	Other	Total		
I. Sales and Operating Income:								
Sales:								
Sales to outside customers	¥148,593	¥52,740	¥80,231	¥37,930	¥33,946	¥353,440	¥ —	¥353,440
Inter-segment sales/transfers	346	10,501	5,604	4,510	12,004	32,965	(32,965)	—
Total sales	148,939	63,241	85,835	42,440	45,950	386,405	(32,965)	353,440
Operating expenses	134,671	58,900	81,334	40,838	45,239	360,982	(33,077)	327,905
Operating income	¥ 14,268	¥ 4,341	¥ 4,501	¥ 1,602	¥ 711	¥ 25,423	¥ 112	¥ 25,535
II. Assets, Depreciation and Amortization, Loss on Impairment of Fixed Assets and Capital Expenditures:								
Assets	¥118,800	¥82,423	¥73,381	¥31,962	¥27,547	¥334,113	¥ 50,268	¥384,381
Depreciation and amortization	3,913	2,642	2,283	806	159	9,803	(14)	9,789
Loss on impairment of fixed assets	738	—	323	—	—	1,061	—	1,061
Capital expenditures	3,898	2,317	3,407	1,216	32	10,870	(11)	10,859

Millions of Yen

Year ended March 31, 2005	Industry segment						Corporate, elimination and other	Consolidated total
	Pharmaceuticals	Bio-Chemicals	Chemicals	Food	Other	Total		
I. Sales and Operating Income:								
Sales:								
Sales to outside customers	¥155,870	¥50,354	¥73,148	¥39,266	¥40,325	¥358,963	¥ —	¥358,963
Inter-segment sales/transfers	556	7,413	4,835	5,234	17,459	35,497	(35,497)	—
Total sales	156,426	57,767	77,983	44,500	57,784	394,460	(35,497)	358,963
Operating expenses	138,326	50,880	72,644	42,838	56,150	360,838	(35,382)	325,456
Operating income	¥ 18,100	¥ 6,887	¥ 5,339	¥ 1,662	¥ 1,634	¥ 33,622	¥ (115)	¥ 33,507
II. Assets, Depreciation and Amortization and Capital Expenditures:								
Assets	¥128,723	¥75,862	¥66,976	¥33,188	¥37,839	¥342,588	¥ 31,905	¥374,493
Depreciation and amortization	4,371	2,684	2,344	1,075	110	10,584	(19)	10,565
Capital expenditures	2,733	2,216	1,622	491	586	7,648	(1)	7,647

(2) Geographic Segment Information

For fiscal 2007, 2006 and 2005, geographic segment information has been omitted because both domestic sales and assets located in Japan were more than 90% of those for all segments.

(3) Overseas Sales

The classification of overseas sales is as follows:

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

Millions of Yen

Year ended March 31, 2007	Americas	Europe	Asia	Other areas	Total
I. Overseas sales	¥19,364	¥15,789	¥28,618	¥424	¥ 64,196
II. Consolidated net sales					354,274
III. Ratio of overseas sales to consolidated net sales	5.5%	4.5%	8.1%	0.1%	18.1%

Thousands of U.S. Dollars

Year ended March 31, 2007	Americas	Europe	Asia	Other areas	Total
I. Overseas sales	$163,977	$133,712	$242,341	$3,589	$ 543,619
II. Consolidated net sales					3,000,034
III. Ratio of overseas sales to consolidated net sales	5.5%	4.5%	8.1%	0.1%	18.1%

Millions of Yen

Year ended March 31, 2006	Americas	Europe	Asia	Other areas	Total
I. Overseas sales	¥15,138	¥13,608	¥25,548	¥644	¥ 54,938
II. Consolidated net sales					353,440
III. Ratio of overseas sales to consolidated net sales	4.3%	3.9%	7.2%	0.2%	15.6%

Millions of Yen

Year ended March 31, 2005	Americas	Europe	Asia	Other areas	Total
I. Overseas sales	¥12,883	¥16,563	¥23,655	¥925	¥ 54,026
II. Consolidated net sales					358,963
III. Ratio of overseas sales to consolidated net sales	3.6%	4.6%	6.6%	0.3%	15.1%

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

Note 17

Per Share Data

	Yen			U.S. Dollars
	2007	2006	2005	2007
Net assets per share	¥607.5	¥604.9	¥556.3	$5.144
Net income—basic	31.3	38.4	41.7	0.265
Net income—diluted (*)	31.3	38.3	—	0.265

* Diluted net income per share information for fiscal 2005 is not disclosed because there were no residual securities.

a) The basis for the calculation of net income per share data is as follows:

	Millions of Yen			Thousands of U.S. Dollars
	2007	2006	2005	2007
Net income	¥12,694	¥16,273	¥17,932	$107,494
Less: Components not pertaining to common shareholders				
Bonuses to directors and corporate auditors	—	(51)	(109)	—
Net income pertaining to common shareholders	¥12,694	¥16,222	¥17,823	$107,494

	2007	2006	2005
Average outstanding shares of common stock	405,270,297	422,919,680	427,635,631 shares

b) The basis for the calculation of net assets per share data is as follows:

	Millions of Yen	Thousands of U.S. Dollars
	2007	2007
Net assets	¥244,082	$2,066,915
Less: Share subscription rights	(66)	(559)
Less: Minority interests in consolidated subsidiaries	(2,300)	(19,477)
Net assets pertaining to common shareholders	¥241,716	$2,046,879

	2007
Number of shares of common stock at year-end (number of shares outstanding)	397,892,335 shares

Note 18

Subsequent Event

On June 1, 2007, the Company acquired all the outstanding shares of DAIICHI FINE CHEMICAL CO., LTD., formerly a wholly owned subsidiary of DAIICHI SANKYO COMPANY, LIMITED, and made it into a subsidiary.

a) Aim of share acquisition

The Company decided to acquire the shares of DAIICHI FINE CHEMICAL because the Company will be able to further heighten the value of its existing operations by organically linking DAIICHI FINE CHEMICAL's outstanding capabilities in synthesis technologies with the Company's capabilities in fermentation technologies. At the same time, the Company looks forward to significant synergies based on mutually complementary products and commercial distribution.

b) Name of counterpart company in acquisition of shares . . . . DAIICHI SANKYO COMPANY, LIMITED

c) Overview of acquired company

①Name	DAIICHI FINE CHEMICAL CO., LTD.	
②Location	Takaoka City, Toyama Prefecture	
③Name of Representative	President Shunya Tamai	
④Financial results (as of March 31, 2007)		
Net sales:	¥16,418 million	($139,030 thousand)
Operating income:	¥1,948 million	($16,496 thousand)
Capital:	¥2,276 million	($19,273 thousand)

⑤Description of operations

Production (import) and sale of pharmaceuticals, veterinary medicines, food additives, feed additives, cosmetics ingredients, in vitro diagnostic reagents, and intermediaries for chemical products.

d) Date of share acquisition . . . . . June 1, 2007

e) Number of shares acquired and percentage of ownership held upon acquisition

①Number of shares acquired	1,449,160 shares
②Percentage of ownership held upon acquisition	100%

f) Source of financing and payment plan

The Company appropriated the funds needed to acquire the above shares from its own funds and paid the amount for the acquisition of the shares on the day of the transference of stock certificates, on June 1, 2007.

ERNST & YOUNG SHINNIHON

■ Certified Public Accountants
Hibiya Kokusai Bldg.
2-2-3, Uchisaiwai-cho
Chiyoda-ku, Tokyo, Japan 100-0011
C.P.O. Box 1196, Tokyo, Japan 100-8641

■ Tel: 03 3503 1100
Fax: 03 3503 1197

Report of Independent Auditors

The Board of Directors
KYOWA HAKKO KOGYO CO., LTD.

We have audited the accompanying consolidated balance sheets of KYOWA HAKKO KOGYO CO., LTD. and consolidated subsidiaries as of March 31, 2007, and the related consolidated statements of income, changes in net assets, and cash flows for the year ended March 31, 2007, all expressed in yen. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. The consolidated financial statements of KYOWA HAKKO KOGYO CO., LTD. and consolidated subsidiaries for the years ended March 31, 2006, and 2005, were audited by other auditors whose report dated June 28, 2006, expressed an unqualified opinion on those financial statements.

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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of KYOWA HAKKO KOGYO CO., LTD. and consolidated subsidiaries at March 31, 2007 and the consolidated results of their operations and their cash flows for the year ended March 31, 2007 in conformity with accounting principles generally accepted in Japan.

Supplemental Information:

As described in Note 18, the Company acquired all outstanding shares of DAIICHI FINE CHEMICALS. CO., LTD., a wholly-owned subsidiary of DAIICHI SANKYO COMPANY, LIMITED and made this company its subsidiary on June 1, 2007.

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended March 31, 2007 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 3.

Ernst & Young ShinNihon

June 20, 2007

PRINCIPAL SUBSIDIARIES AND AFFILIATES

As of March 31, 2007

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
BioWa, Inc.[1]	100.0	$10	Licensing of antibody technology, development of therapeutic antibodies
Kyowa Medical Promotion Co., Ltd.[1]	100.0	¥50	Sales promotion of pharmaceuticals
Kyowa Warehouse & Transportation Co., Ltd.[3]	100.0	¥70	Warehousing and transportation
Bio-Chemicals			
Biokyowa Inc. (U.S.A.)[1]	100.0	$20	Manufacture and sale of amino acids
Shanghai Kyowa Amino Acid Co., Ltd.[1]	70.0	$18	Manufacture and sale of amino acids
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, and chemicals
Kyowa Italiana Farmaceutici S.R.L. (Italy)[1]	100.0	Euro1	Sale of pharmaceuticals and fine chemicals
Kyowa Hakko (H.K.) Co., Ltd. (Hong Kong)[1]	100.0	HK$1	Sale of pharmaceuticals and amino acids
Kyowa Wellness Co., Ltd.[1]	100.0	¥30	Sale of health care products
Shinwa Pharmaceutical Co., Ltd.[1]	100.0	¥95	Manufacture and sale of herbal medicines and health foods
Kyowa Engineering Co., Ltd.[1]	100.0	¥70	Design and installation of equipment and facilities
Chemicals			
Kyowa Hakko Chemical Co., Ltd.[1]	100.0	¥5,300	Manufacture and sale of chemicals
J-PLUS Co., Ltd.[2]	50.0	¥480	Manufacture and sale of plasticizers
Kurogane Kasei Co., Ltd.[2]	40.0	¥90	Manufacture and sale of chemicals
Food			
Kyowa Hakko Food Specialties Co., Ltd.[1]	100.0	¥3,000	Manufacture and sale of seasonings and bakery products and ingredients
Kyowa F.D. Foods Co., Ltd.[1]	100.0	¥100	Manufacture and sale of freeze-dried foods
Ohland Foods Co., Ltd.[1]	100.0	¥50	Manufacture and sale of foods
Riken Kagaku Co., Ltd.[1]	100.0	¥30	Manufacture and sale of seasonings and health foods
Kyowa HiFoods Co., Ltd.[1]	100.0	¥60	Import and 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 seasonings
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 America, Inc. (U.S.A.)[1]	100.0	$58	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

1. Consolidated subsidiary
2. Affiliate accounted for by the equity method
3. Kyowa Warehouse & Transportation Co., Ltd., is in the process of being liquidated.

As of June 30, 2007

AMERICAS

Kyowa America, Inc.
Princeton Commerce Center,
29 Emmons Drive, Suite C-10,
Princeton, NJ 08540, U.S.A.
TEL: 1-609-734-3420
FAX: 1-609-734-3455

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.
Princeton Commerce Center,
29 Emmons Drive, Suite C-10,
Princeton, NJ 08540, U.S.A.
TEL: 1-609-734-3420
FAX: 1-609-734-3455

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

ASIA

Kyowa Hakko Industry (S) Pte Ltd.
260 Orchard Road, #12-04,
The Heeren, Singapore 238855
TEL: 65-6733-4948
FAX: 65-6733-0819

Kyowa Hakko (Malaysia) SDN BHD.
20, Jalan SS 19/5, 47500 Subang Jaya,
Selangor, Darul Ehsan, Malaysia
TEL: 60-3-5634-0669
FAX: 60-3-5634-0990

Kyowa Hakko Kogyo Co., Ltd.
Mumbai Liaison Office
Suite 701-A, MMTC House C-22,
Bandra Kurla Complex, Bandra (East),
Mumbai 400051, India
TEL: 91-22-6725-3457
FAX: 91-22-6725-3458

Kyowa Hakko Kogyo Co., Ltd.
Beijing Representative Office
Room 701, No. 5, Beijing Fortune Bldg.,
Dong San Huan Bei Lu,
Chao Yang District, Beijing 100004,
People's Republic of China
TEL: 86-10-6590-8515
FAX: 86-10-6590-8517

Kyowa Hakko Kogyo Co., Ltd.
Shanghai Representative Office
Room 1712,
205 Maoming Nan lu Ruijin Bridge,
Shanghai 200020,
People's Republic of China
TEL: 86-21-6466-1222
FAX: 86-21-6415-6022

Kyowa Hakko Kogyo Co., Ltd.
Guangzhou Representative Office
Room 701, No. 33, Yi An Plaza,
Jianshe 6 Ma Lu, Guangzhou 510060,
People's Republic of China
TEL: 86-20-8364-4123
FAX: 86-20-8364-4131

Shanghai Kyowa Amino Acid Co., Ltd.
No. 158, Xintuan Road,
Qingpu Industrial Zone, Shanghai 201700,
People's Republic of China
TEL: 86-21-5970-1988
FAX: 86-21-5970-1135

Kyowa Hakko (H.K.) Co., Ltd.
Room 1908, Hang Lung Centre,
2-20 Paterson Street, Causeway Bay,
Hong Kong, People's Republic of China
TEL: 852-2895-6795
FAX: 852-2576-6142
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

Kyowa Pharmaceutical (H.K.) Co., Ltd.
Room 1908, Hang Lung Centre,
2-20 Paterson Street, Causeway Bay,
Hong Kong, People's Republic of China
TEL: 852-2881-7459
FAX: 852-2576-6142

Kyowa Hakko Pharmaceuticals (Suzhou) Co., Ltd.
No. 115, Qingqju Street,
Suzhou Industrial Park, Jiangsu 215021,
People's Republic of China
TEL: 86-512-6283-1082
FAX: 86-512-6283-1083

Kyowa Foods (Jiangyin) Co., Ltd.
Huangtang Industrial Park,
Xiake Zhen, Jiangyin, Jiangsu 214407,
People's Republic of China
TEL: 86-510-8653-0599
FAX: 86-510-8653-0505

Wuxi Xiehe Food Co., Ltd.
Huangtang Industrial Park,
Xiake Zhen, Jiangyin, Jiangsu 214407,
People's Republic of China
TEL: 86-510-8653-0599
FAX: 86-510-8653-0505

Qingdao Kyowa Wanfu Foods Co., Ltd.
East of Shenzhen Road,
Laixi Qingdao 266600,
People's Republic of China
TEL: 86-532-8187-1217
FAX: 86-532-8840-7606

PHARMACEUTICALS

Antibiotics
Pasetocin®, Fortimicin®, Sagamicin®

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

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

Cardiovascular Agents
Meditrans® Tape, Inovan®, Apiracohl®, Coniel®, Pre Dopa®, Dobupum®

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

Antiallergic Agents
Allelock®, Celtect®

Sensory Organ Agents
Patanol®

Hormones
Desmopressin, Hysron®

Other Metabolic Agents
Gludiase®, ATP Kyowa, Activacin®

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

Ointment
Propaderm®

Transdermal Analgesic Agent
Durotep® Patch

Contrast Medium
Bothdel

Diagnostic Medical Devices
Clinical Chemistry Diagnostic Reagents (Determiner® L HDL-C, MetaboRead® RemL-C), Immunological Reagents (Determiner® HbA1c, Chemilumi series), Reagent strips for urinanalysis (Uropiece® S), Controls (Accurun series Infectrol), Full Auto Micro Plate EIA Analyzer (AP series), Fecal Occult Blood Test Analyzer (HM-JACK® series), Diabetes Mellitus Test Analyzer (DM-JACK® series)

BIO-CHEMICALS

Fine Chemicals for Pharmaceutical and Industrial Use
Amino Acids (L-Alanine, L-Arginine, L-Glutamine, 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, Ubidecarenone (Coenzyme Q10)

Health Care Products
Amino Acids, Vitamins, Minerals, Carotenoids, Probiotics, Peptides, Remake® series, Enguard® series

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

Agrochemicals
Plant Growth Regulators (Gibberellin, Fulmet®)

Livestock and Fisheries Products
Nanaomycin, Polyup®, Atomolate®, Benesal®, Lysozyme Chloride for Aquaculture, Fantacin® for Aquaculture, Ampicirin for Aquaculture

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

Alcohol
For use in refined sake, food preservatives, and disinfectants

CHEMICALS

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

Raw Materials for Plasticizers
2-Ethylhexyl Alcohol, Oxocol® 900 (Isononyl Alcohol), Decanol

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

Diols
1-3 Butylene Glycol, 2,4-DiEthyl-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

Processed Foods
Instant egg-drop soup, Various food materials

CORPORATE DATA

As of March 31, 2007

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
5,756 (Parent Company: 3,644)

Date of Foundation
July 1, 1949

Paid-in Capital
¥26,745 million

Principal Plants
Domestic
Hofu, Ube, Sakai, Fuji,
Kyowa Hakko Chemical Co., Ltd. (Yokkaichi, Chiba),
Kyowa Hakko Food Specialties Co., Ltd. (Tsuchiura),
Kyowa Medex Co., Ltd. (Fuji)

Overseas
Biokyowa Inc. (U.S.A.),
Shanghai Kyowa Amino Acid Co., Ltd. (China)

Principal Laboratories
BioFrontier Laboratories
Pharmaceutical Research Center
Technical Research Laboratories
Healthcare Products Development Center
Kyowa Hakko Chemical Co., Ltd., Yokkaichi Research Laboratories
Kyowa Hakko Food Specialties Co., Ltd., Food Creation Center
Kyowa Medex Co., Ltd., Research Laboratories

Stock Price
Stock Price Range
(Yen)

INVESTOR INFORMATION

As of March 31, 2007

Stock Listing
Tokyo

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

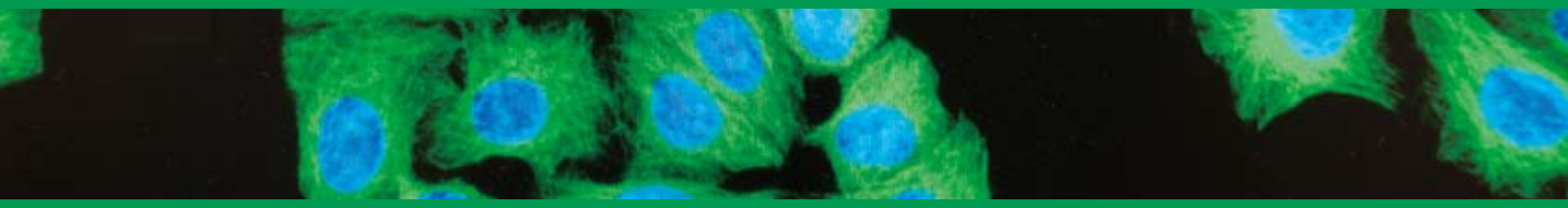
Number of Shares of Common Stock
Authorized: 987,900,000
Issued: 399,243,555

Number of Shareholders
61,247

Principal Shareholders

	Number of Shares Held (Thousands)	Percentage of Total Shares Issued
The Master Trust Bank of Japan, Ltd. (Trust account)	25,306	6.35%
The Dai-ichi Life Mutual Insurance Co.	24,661	6.19
Japan Trustee Services Bank, Ltd. (Trust account)	22,386	5.62
The Norinchukin Bank	18,083	4.54
Mizuho Trust & Banking Co., Ltd. (Retirement Benefit Trust for Mizuho Bank, Ltd.)	8,075	2.02
Mizuho Bank, Ltd.	7,126	1.79
Japan Trustee Service Bank, Ltd. (Trust account 4)	6,056	1.52
NIPPONKOA Insurance Company, Limited	5,483	1.37
SOMPO JAPAN INSURANCE INC.	5,296	1.33
Kyowa Fund	5,279	1.32

Note: The Company had 1,324 thousand shares (non-consolidated) of treasury stock as of March 31, 2007, which are not included in the above list.



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

www.kyowa.co.jp

Waterless Printing Naturally

Vegetable INK for waterless printing
Non Volatile Organic Compounds

FSC Mixed Sources
Product group from well-managed forests and other controlled sources
www.fsc.org Cert no. SA-COC-1210
© 1996 Forest Stewardship Council

This report is printed on FSC-certified paper using the waterless printing process with non-VOC (non-volatile organic compound).

Printed in Japan
July 2007