ANNUAL REPORT 2007

Year Ended March 31, 2007

KOBAYASHI PHARMACEUTICAL CO., LTD.

Profile

Something New, Something Different

Kobayashi Pharmaceutical Co., Ltd. has grown steadily since its founding in 1886 through the tireless pursuit of a management policy that defines the Company's mission as providing people and society with comfort through "Creativity and Innovation." The Company will continue to seek growth by developing a unique identity in its three principal businesses: Consumer Products Operation, its core business, and Wholesale Operation and Medical Devices Operation.

As a pioneer in new markets, Kobayashi Pharmaceutical has a trailblazing record of bringing consumers a stream of diverse new products, merchandise and services, and of developing new approaches to business that give form to our management policy of "Something New, Something Different." Today, our sales network spans the globe, covering all important markets, including the U.K., the U.S., China, Hong Kong and Germany.

Unfettered by tradition and hidebound thinking, and leveraging the unique strengths of a speedy development system, we will continue to work toward realizing the concept of our brand charter, "You make a wish and we make it real," while creating new markets and differentiating our brand.

あったらいいなをカタチにする

"You make a wish and we make it real."

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Forward-looking Statements

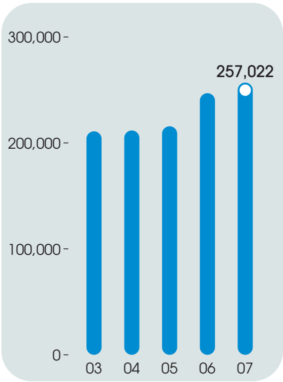
Plans, strategies, beliefs and other statements concerning future business operations of Kobayashi Pharmaceutical Co., Ltd. included in this annual report are forward-looking statements based not on historical facts but on management's assumptions and beliefs in light of information currently available. These forward-looking statements include risks, known and unknown, and uncertainties. Actual management achievements and business results may therefore differ significantly from forecasts in this annual report.

Consolidated Financial Highlights
Years ended March 31

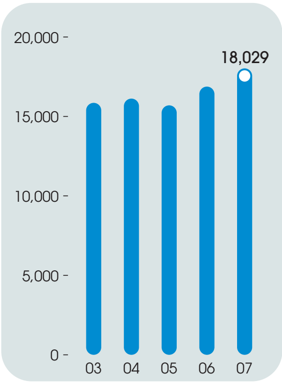
	Millions of yen			
	2005	2006	**2007**	(% Change)
For the Year				
Net Sales	¥ 215,708	¥ 246,853	¥ 257,022	4.1
Operating Income	15,699	16,880	18,029	6.8
Net Income	6,731	7,475	8,298	11.0
Per Share Data (Yen)				
Net Income	160.64	179.17	200.77	12.1
Equity	1,443.30	1,617.10	1,799.87	11.3
Cash Dividends	33.00	38.00	50.00	31.6
At Year-end				
Total Assets	134,629	151,945	164,556	8.3
Equity	60,116	66,812	74,429	11.4
				Change
Ratios (%)				
ROA	5.0	5.2	5.0	(0.2)
ROE	11.7	11.8	11.7	(0.1)
Equity	44.7	44.0	45.2	1.2

Note: Presented as Shareholders' Equity until fiscal 2006. Presented as Equity from fiscal 2007 due to a change in accounting standards.

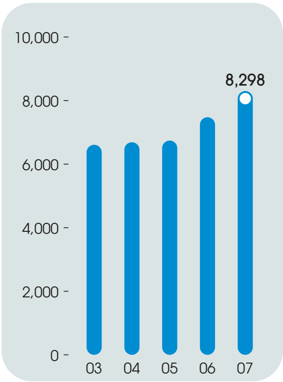
Net Sales (¥ million)



Operating Income (¥ million)



Net Income (¥ million)



To Our Stakeholders

Chairman and Chief Executive Officer
Kazumasa Kobayashi

President and Chief Operating Officer
Yutaka Kobayashi

Net sales up 4.1% and net income up 11.0% for our ninth consecutive year of sales and earnings growth

Kobayashi Pharmaceutical Group Brand Charter

Going beyond merely satisfying our customers' fast-evolving needs, our mission is to create new products that our customers have always wanted. True to our brand slogan of "You make a wish and we make it real," we will deliver these products as early as possible.

Products and services will be developed from the standpoint of customers to the highest standard of quality, in order to live up to the trust placed in us by society and our customers.

Our dream is to share small discoveries from everyday life with people all over the world.

We are committed to being a development-focused company that contributes to society by building lasting relationships with customers and delivering new forms of satisfaction.

In the fiscal year ended March 31, 2007, the trends toward improvement in corporate profits and employment strengthened. However, the recovery in consumer spending remained weak, and the future course of business conditions, including crude oil prices, remained uncertain. In this environment, the Kobayashi Pharmaceutical Group took steps to fully express the spirit of its management philosophy of "Creativity and Innovation." The Group launched new products to seed new markets while activating existing markets by offering new added value. At the same time, we formed partnerships, acquired businesses, and aggressively expanded overseas operations.

As a result, consolidated net sales for the year rose 4.1% year on year, to ¥257,022 million. Operating income rose 6.8%, to ¥18,029 million, as a result of sales growth in product categories with high profit margins and thorough efforts to reduce manufacturing costs. Although there was a decline in equity in earnings of affiliates and an increase in loss on disposal or write-offs of inventories accompanying returns and product renewals, partly due to the absence of a ¥1,656 million loss on impairment of fixed assets recorded in the previous fiscal year, net income for the year under review was up 11.0%, to ¥8,298 million.

Reinforcing existing brands, implementing a growth strategy to expand scope of operations

In the fiscal year ending March 2008, we will mark our 90th anniversary, and Japan's economic recovery is expected to accelerate. To achieve the type of competitiveness that will enable us to be the leader in each of our fields of business, we need to implement strategies for further reinforcing existing brands and businesses at the same time as we take steps to expand operational scope to accelerate growth. In the Consumer Products Operation, in spring 2007, we launched 15 new products targeting emerging customer needs. In addition, to cultivate our brand, we are also implementing aggressive sales initiatives for existing products in accordance with marketing plans formulated for each brand. In overseas operations, meanwhile, we are working to create new markets, centered on body warmers. In the Wholesale Operation, to respond to the increasingly wide areas served by drug stores, our key clients, we are pursuing alliances with other companies to build a sales network that will enable us to expand nationwide. In the Medical Devices Operation, we will introduce new products into our existing markets in Japan and further accelerate the development of our own-brand products. At the same time, having made the Irish ventilator manufacturer eVent Medical Ltd. a subsidiary, we will work to expand our markets through the global sale of ventilators and the development of new products.

In the future, we will continue working not only to create products that consumers trust and support but also to maximize corporate value in order to meet the expectations of shareholders, employees, and all other stakeholders. I would like to ask for your continued support in the years ahead.

August 2007

Kazumasa Kobayashi
Chairman and Chief Executive Officer

Yutaka Kobayashi
President and Chief Operating Officer

Kazumasa Kobayashi

Y. Kobayashi

President and Chief Operating Officer
Yutaka Kobayashi

Q First, how would you evaluate Kobayashi Pharmaceutical's performance in the fiscal year ended March 31, 2007?

A. We faced difficult conditions in the past year with a cool summer and warm winter. However, we have recorded growth in sales and earnings ever since we began to report consolidated results, and the year under review marked our ninth consecutive year of higher sales and profits. We are very pleased with that achievement.

By field, in the Consumer Products Operation, our new products have done well. In particular, strong contributions to our improved performance were made by *Nicitol 85*, a diet pill for reducing abdominal fat; *Cleair*, an air freshener that eliminates unpleasant household odors by releasing ions; and *Araitate Shoshu Shabon*, a deodorizing air freshener that gives rooms a refreshing clean scent.

In the Wholesale Operation, on April 1, 2006, the Company expanded its geographical coverage by acquiring the outstanding shares of KS Tohoku Co., Ltd. (formerly Sowa Co., Ltd.), which was operating in the Tohoku area. KS Tohoku was added to the scope of consolidation, and sales increased by 5.0%.

In the Medical Devices Operation, we transferred all of our shareholdings in the three Shield Healthcare Centers in the U.S. to Dharma Ventures Group, Inc., which was established by the local Shield management team. This was because we did not anticipate future synergies with existing businesses. On the other hand, in November 2006, we followed the principles of selection and concentration by acquiring eVent Medical Ltd., a maker of ventilators.

What challenges does the Company face, even as it continues to record strong results?

A. One challenge we do face is the increase in loss on disposal of products due to the large numbers of new and improved products we have launched. In the past year, for example, we introduced 35 new products. But of course, just launching large numbers of products is not enough to ensure that they will all become hits. It is essential to increase the success rate for new products with advance research and testing. In addition, we need to respond to intensified competition with other brands by continually releasing improved products, but at the same time, I believe the costs and benefits of product renewals must be carefully considered. In wholesale distribution, pressure on prices is intensifying due to the steady advance of retail alliances. In this environment, we need to strengthen the Company so that we can secure reasonable profit margins. In medical devices, we sold the Shield Healthcare Centers, which recorded favorable sales and profits, and acquired a ventilator manufacturer. Future challenges will include enhancing our manufacturing capabilities and targeting growth by putting the principles of selection and concentration into practice.

In the Company's 90th fiscal year, ending March 2008, the Group's overall management policies include advancing growth strategies and strong sales growth. Would you give an overview of your specific strategies?

A. Kobayashi Pharmaceutical has many brands that are well known. I believe that most Japanese consumers know such brands as *Sawaday*, *Bluelet*, *Shoshugen*, *Anmerts*, and *Eyebon*. However, many consumers probably do not know that Kobayashi Pharmaceutical is the company selling those brands. Aligning the product brands and the company brand is important not only to enable consumers to buy products with reassurance but also to enable us to increase our enterprise value.

One initiative to this end is a revision of our marketing strategy. We changed the content of our TV commercials and added our brand slogan and company name at the beginning. Surprisingly, there are hardly any commercials that feature the company name at the beginning. This is a good example of our "Something New, Something Different" management policy.

When we talk about "strong sales growth," we do not mean selling at low prices to increase share, but rather working to expand sales while maintaining a focus on the profitability of both existing products and new products.

When I became president, the Company introduced a new R&D framework called Category Development, which uses a system of six product development categories. We took this step to further increase the speed of new product development. This reorganization has produced results. We have created numerous hit products and increased competition between categories. And we have seen increases in the number and quality of ideas proposed by employees. In regard to profitability, I believe that it is important to focus on pharmaceuticals, which has an especially high profit margin among the six categories.

Overseas, we will leverage the technology of Kiribai Chemical Co., Ltd., which is a global leader in the production and sales of body warmers. We will use Kiribai's technology as a competitive edge in the marketing of body warmers as a global strategic product. Several years ago, when we provided samples of body warmers at the Thanksgiving Day parade near New York's Central Park, consumers were delighted that "such a thing exists!" This shows that, depending on future development, body warmers are an area that has major potential. In China and the U.K., where we are already marketing body warmers, we are getting an excellent market response.

Q In December 2006, the Company announced that it would begin discussions regarding a management integration between Kobashou, Inc. and Paltac Corporation, a consolidated subsidiary of Mediceo Paltac Holdings Co., Ltd. Would you discuss your objectives and the current status of those discussions?

A. Paltac, a Mediceo Paltac Holdings Group company, is a leading wholesale distributor of sundries and cosmetics. Currently, sundries and cosmetics account for about 60% to 70% of the sales of drug stores, while OTC pharmaceutical products contribute about 20%. Accordingly, if we are going to increase our market share, we need to work together with a company that is strong in sundries and cosmetics, rather than pharmaceuticals. Through cooperation between Paltac, which has a leading position in sundries and cosmetics, and Kobashou, which has the number one share in OTC pharmaceuticals, we would be able to create a sales network that could meet the needs of nationwide chains.

Kobayashi Pharmaceutical got its start in the wholesale business, and we remain strongly committed to wholesale operations. However, in consideration of the current operating environment in the wholesale industry, it will be difficult to survive alone, and I believe that we must consider an alliance with another company that will enable the partners to reinforce each other's strengths. With regard to exactly what form this integration will take, we will work to choose the best option based on the understanding that we will "jointly and cooperatively strengthen wholesaling functions from the customer's viewpoint."

Q In the Medical Devices Operation, what results do you expect to see from the acquisition of eVent Medical?

A. The acquisition of eVent Medical was our first M&A transaction in the medical devices field, and we need to ensure that it is successful. eVent Medical is a newly established company that develops "reliable ventilators" that are easy for clinicians to use and trouble free. Ventilators are essential medical devices for hospitals, and the global market for these products is currently about ¥100.0 billion. By combining eVent Medical's development and product capabilities and Kobayashi Pharmaceutical's marketing capabilities, I believe that together we can contribute to further growth in the market for ventilators.

The key to profit growth in the Medical Devices Operation will be a balance between manufacturing and trading. Our objective is to raise the contribution of our own products to 20% as soon as possible. Making eVent Medical a subsidiary offers the prospect of significant synergy effects, including enhanced manufacturing capabilities. In addition to Europe and Asia, where sales are already under way, we will strengthen sales throughout the United States in the near future. Subsequently, we will introduce these products in Japan.

Q What is the Company's policy for providing a return to shareholders?

A. We consider the distribution of profits to shareholders to be one of the most important management priorities, and we will continue to strengthen our focus on this area. Accordingly, the Company intends to promote a dividend policy that reflects consolidated results while maintaining a basic policy of providing ongoing, stable dividend payments. As a result, the ordinary dividend per share for the year was ¥50.00, representing an increase of ¥12.00 compared to the previous year's ¥38.00.

In addition to bolstering returns to shareholders, we take steps to secure adequate internal reserves for investing in operations in order to maintain a high level of growth potential and a robust corporate structure. Internal reserves will be utilized for M&A activities, which are a key focus of our growth strategies, and for aggressive investment in overseas expansion.

Q Finally, what is the outlook for the fiscal year ending March 2008?

A. For the fiscal year ending March 31, 2008, we are targeting year-on-year increases of 3.1% in net sales, 2.6% in operating income, 6.6% in ordinary income, and 5.5% in net income. We will do our utmost to achieve these objectives. We also expect to see a variety of new changes in the fiscal year ending March 2008. I think that we are likely to see substantial changes in the operating environment, such as further alliances in distribution and marked acceleration in industry reorganization. Also, under the influence of global warming, it is possible that the trend toward changeable weather will continue, and our management activities must take that possibility into account. Even in an environment of intensifying competition, we will continue working to meet the expectations of our stakeholders by striving to achieve continued growth in corporate value in accordance with the spirit of our management philosophy of "Creativity and Innovation."

Consumer Products Operation

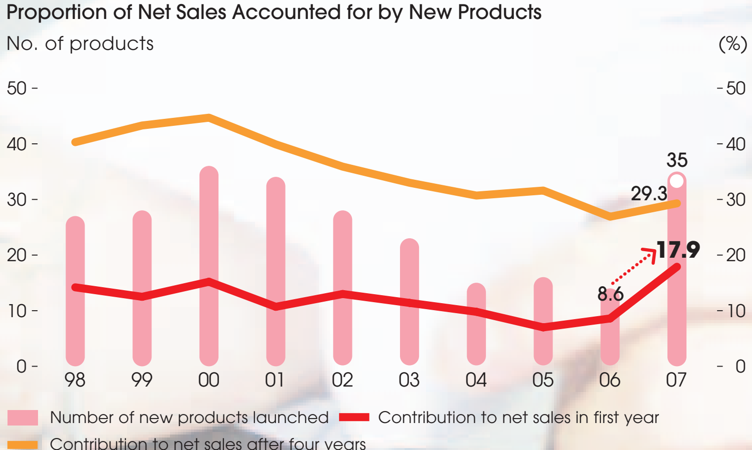
New Product Development Brand Building Strategy

POINT 1 Approximately 30 Products Launched per Year

POINT 2 Sustaining High Profit Margins

POINT 3 Focus on the Healthcare Market

Proportion of Net Sales Accounted for by New Products



Distribution and Overseas Strategies

POINT 1 Approach by Distribution Channel

POINT 2 Overseas Expansion in Body Warmers

POINT 1 Approximately 30 Products Launched per Year

The Company's forte is product development, backed by strong marketing capabilities. Continually working from the customer's perspective, we focus on developing unique products that are easily understood by consumers.

To create products that earn customer support, we polish basic ideas, establish clear concepts, and conduct overlapping R&D and monitoring to commercialize products. At the manufacturing stage, costs and quality are strictly managed, and market rollout is guided by a specific marketing plan. At every stage, it is essential that those in charge of the various functions are able to fully demonstrate their own expertise, while maintaining close cooperation with each other.

We revamped our development framework in April 2005 to facilitate such cooperation. For each product category a team of four people, each with their own functions—a product development manager, a researcher, a technology development manager and a brand manager—is put together to create new products, with presentations made at monthly Idea Meetings. The meetings, at which decisions are made on the ideas presented, comprise five executives: the president, Research and Development Company president, Product Sales Company president, Manufacturing Company president and Marketing Office manager. Management involvement at such an early stage in the decision on whether to proceed with development greatly reduces the period to product commercialization.

Moreover, these monthly idea presentations provide greater opportunity for debate on team ideas, and the individual managers in the team can consider new ideas and compile information along the way. The Kobayashi Group has a system that enables all employees to freely propose new product ideas at any time. This scheme allows the managers to identify the wishes of customers based on the ideas submitted to them, as well as surveys and their own experience.

Product ideas that are approved at the idea presentations proceed to the next stages of product planning, including development, research, and monitoring, followed by commercialization, then market launch and full-scale marketing by the brand manager. Because the individual managers engage in debate from the idea stage, a shared awareness can be maintained throughout the process, from planning and development through sales.

In parallel with this process, we also expand and revamp the existing product lineup. Under an integrated framework encompassing each product category, Kobayashi Pharmaceutical gives each team member a key role in developing new products and cultivating existing products, with the aim of further enhancing its brands.

Category Development Framework

New Product Development System

Integrated organizational structure by category

Drugs/Sanitary Department			Daily Goods Department		
Pharmaceuticals	Oral Care	Foods	Sanitary Products	Deodorizing Air Fresheners	Detergents and Sundries
Brand Manager	Brand Manager	Brand Manager	Brand Manager	Brand Manager	Brand Manager
Product Development Manager	Product Development Manager	Product Development Manager	Product Development Manager	Product Development Manager	Product Development Manager
R&D	R&D	R&D	R&D	R&D	R&D
Technology Development	Technology Development	Technology Development	Technology Development	Technology Development	Technology Development

New products launched in fall 2006 and spring 2007

Brand Management with a Streamlined Portfolio

Our products fall into four types:

1 **Products for Creating New Demand:**
Development of entirely new products, never before seen in the market, and creation of new markets in the process

2 **Products for Expanding Existing Demand:**
Powerful products brought to emerging markets to promote fast expansion

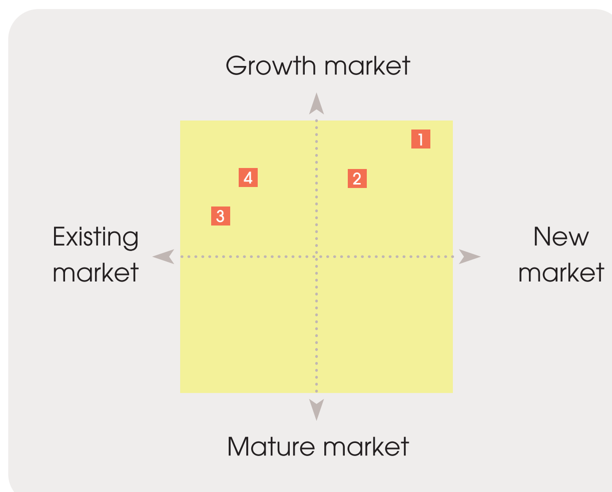
3 **Products for Taking on Competitors:**
Products that protect existing offerings from those of rival companies when new players enter markets we have created

4 **Products for Brand-based Line Extension:**
The addition of value to existing products under a single brand in a way that expands the lineup and further reinforces the brand

In these and other ways, we raise the return on invested capital and execute concentrated sales promotion activities through strategies that clearly and strategically position new products. Brand managers are entirely responsible for overall brand management, including brand development and sales promotion, and for ensuring sales and profit through the timely withdrawal from or renewal of unprofitable products.

Kobayashi Pharmaceutical continues to focus on achieving further growth, with an emphasis on brand building and the development of Products for Creating New Demand and Products for Expanding Existing Demand, the centerpieces of our growth strategy.

Portfolio



"Mother Concept" Development

Another of our product development methods is the "Mother Concept" approach. The idea is to analyze major social trends over the medium and long terms, anticipate consumers' future needs, and then establish themes called "Mother Concepts" that define areas where products should be placed. One such "Mother Concept" is the treatment of menopause-related problems. The acquisition in 2005 of the exclusive sales agency rights to *Inochi No Haha A*, a general-use medication for women's health issues, is positioned as part of this strategy. In addition, we commercialized *Nicitol 85*, an antiobesity drug to address the theme of weight loss.

A *Nicitol 85* project team was inaugurated in 2004. A number of developments were behind our decision to commercialize this drug. Firstly, research had indicated a link between overeating and ill health in the United States, where obesity is a serious social problem. In Japan, meanwhile, interest in losing weight was growing not only among women, but also among men. At the same time, there was increasing demand from customers for traditional Chinese medicine rather than Western pharmaceuticals.

Inochi No Haha A　*Nicitol 85*

POINT ❷ Sustaining High Profit Margins

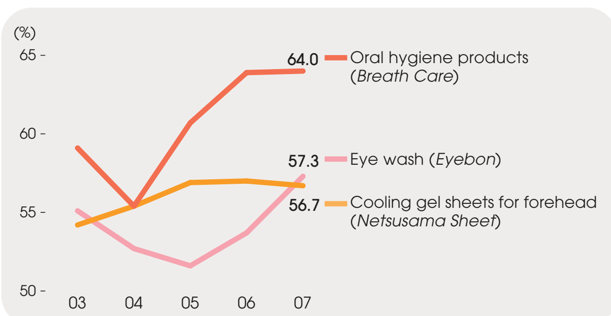
Niche-market Strategy

As the Company's core business, the Consumer Products Operation creates products brimming with originality. We have been first to develop and launch new products in markets where there is a total lack of products that address consumer needs or where products fail to fully satisfy consumer needs. This market cultivation has enabled the Company to establish strong positions in these areas. This approach allows us to avoid price competition and achieve the top market share in markets we have expanded.

Establishing Product Launch and Withdrawal Criteria

By establishing launch criteria based on gross profit margins, we aim to introduce new products that are capable of maintaining stable profitability. At the same time, we are channeling resources into development activities in the home-use pharmaceuticals field, a category offering high gross profit margins. For existing products we have set withdrawal criteria; every six months the criteria are reviewed and we consider which unprofitable products should be withdrawn from the market.

Market shares of principal brands



Breath Care *Eyebon* *Netsusama Sheet*

POINT ❸ Focus on the Healthcare Market

As people have become more health-oriented in recent years, there has been growing interest in healthcare, putting related products in the spotlight. Recognizing that there are still many latent needs, the Kobayashi Group is focusing on the healthcare field with a view to business expansion.

Pursuing M&As

The Kobayashi Pharmaceutical Group aggressively pursues M&As as a strategy for shortening product development and brand-building periods and for boosting investment efficiency. One successful example of this strategy is the *Inochi No Haha A* brand, acquired from Sasaoka Yakuhin Corporation, which is doing well and making substantial contributions to sales growth. We also successively concluded a capital tie-up with Itoh Pharmaceutical Co., Ltd., and a share transfer agreement with Aloe Pharmaceutical Co., Ltd., which have supported expansion of our business domain and marketing area, as well as contributed to a faster pace of growth. Looking ahead, we plan to aggressively pursue M&As while fully considering such impacts as synergies with existing operations.

Mamiya Aloe Ointment

Major Brand Launches

In the fiscal year ended March 31, 2007, metabolic syndrome became a household word, and various media took up the issue of serum triglyceride (neutral fat). These trends had a major impact, resulting in the recognition of our *Nicitol 85* as a major brand. Moreover, in July 2006, sales of *Tochucha* increased substantially amid academic conference and media reports on the effectiveness of Du-Zhong leaf. Going forward, offerings from our competitors and private brands are expected to enter the market for metabolic-related products. However, we believe that the market is capable of even greater growth, and we will therefore further build our brands in this segment.

Tochu Gencha *Tochucha* *Nicitol 85*

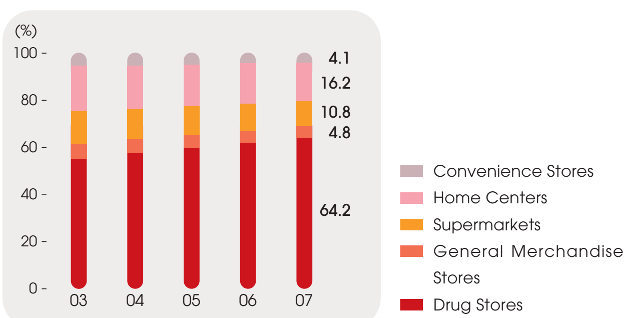
Distribution and Overseas Strategies

POINT ❶ Approach by Distribution Channel

Appointment of In-store Merchandisers for Drugstores

As we have focused product development on the healthcare field, the proportion of sales to drugstores has been increasing annually. Under these conditions, we are working to more accurately grasp the characteristics of retail stores and products, using in-store merchandisers to present even better buying environments, which will allow us to further expand sales in the healthcare field. These in-store merchandisers function as advisors for marketing managers around Japan with regard to 1) the knowledge required to succeed in business negotiations, 2) creation of the buying environment, and 3) effective sales promotion tools. The objective here is to entrench the Company's style of business negotiation in the healthcare field.

Sales Composition by Channel



Product displays in stores

Establishment of Mail-Order Shopping Business Department

Having positioned the mail-order shopping business, which has done well to date, as a growth field, we established the Mail-Order Shopping Business Department in April 2007. The main products handled by the department are 1) nutritional supplements, 2) *Naishidiet*, and 3) *Real Labo*. Regarding nutritional supplements, we already handle 106 products, and will continue aggressively developing supplements that help alleviate the effects of menopause, along with other distinctive products. *Naishidiet* marks the first collaboration between Kobayashi Pharmaceutical and Toyo Shinyaku Co., Ltd. Since April 2007, *Naishidiet* has been sold exclusively through the mail-order channel. In October 2006, we launched *Real Labo*, a high-performance skin-care line that utilizes drug delivery system (DDS) technology. While continuing to pursue the development of revolutionary products, we are exploring trials to induce customers of our nutritional supplement products to try *Real Labo*.

Naishidiet

Real Labo

Online shopping site

The mail-order catalog

Appointment of Dedicated Convenience Store Market Manager

The convenience store market presents attractive sales opportunities, considering the relaxation of regulations on sales of some pharmaceuticals scheduled for 2009 and the considerable number of stores in this segment. To survey the characteristics of customers in the market, in spring 2007, we appointed dedicated convenience store market managers in three departments: marketing, research, and sales. These managers promote the development of products that are sold exclusively through the convenience store channel.

POINT ❷ Overseas Expansion in Body Warmers

The Kobayashi Group is expanding its global presence as part of its growth strategy. Specifically, we have established local subsidiaries in the U.S., China, the U.K., and Hong Kong to pursue sales of our own products.

In October 2006, to bolster our U.S. operations, we made HeatMax, Inc. a consolidated subsidiary. Since its establishment in 1990, HeatMax has dedicated its efforts to developing a body warmer business in the U.S., and now it boasts the No. 1 market share in the U.S. body warmer market. In recent years, in the field of therapeutic body warmers, not only has the company aggressively pursued sales of its own brand, it has done the same for OEM products sold through major drugstore chains and volume retailers. It has built a unique business model in this field that has translated into steady business expansion.

Leveraging HeatMax's distribution network and high profit margins, we aim to further expand the U.S. business and boost corporate value. Additionally, in East Asia, mainly in China, which is experiencing remarkable economic growth, we are working to expand sales, with a particular focus on deodorizing air fresheners and body warmers.


Products sold overseas

Medical Devices Operation

Enhancing Trading Functions

POINT 1 Focusing sales efforts on operating room and orthopedics products

POINT 2 Promoting the introduction of new products

Developing Manufacturing Functions

POINT 1 Promoting Proprietary Brand *Kobamed*

POINT 2 eVent Medical Limited becomes a subsidiary

POINT 3 Bolstering our global sales system

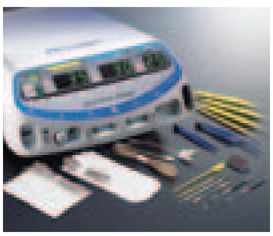
Enhancing Trading Functions

POINT ❶ Focusing sales efforts on operating room and orthopedics products

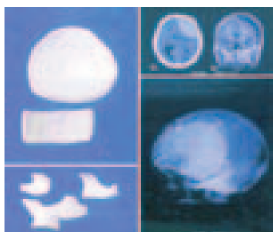
The Medical Devices Operation is guided by the management policy of "providing people and society with comfort." In such fields as surgical and operating room products, respiratory disease, and orthopedics, we import and sell leading-edge medical devices with an emphasis on safety and reassurance, thereby supporting the advancement of medicine in Japan. The operation currently comprises two divisions. One is the Kobayashi Medical Division, which principally handles medical devices in the fields of orthopedics, surgery, anesthesiology, operating room products, pulmonology neurosurgery, and otorhinolaryngology. Based on sales agreements with 21 domestic and overseas manufacturers, the division handles advanced medical devices from around the world, which it imports and sells in the domestic market. The other division is Medicon, Inc., a joint venture with C.R. Bard, Inc. of the U.S. Medicon imports and sells leading-edge medical instruments developed by C.R. Bard, focusing on the urological and gastrointestinal fields, in which there is no competition with Kobayashi Medical Division business. In the urological field in particular, the company has established a position as the market leader.

As the medical field becomes increasing sophisticated and complex, these two divisions will continue to provide "safety and reassurance" at the medical front line by supplying cutting-edge medical devices.

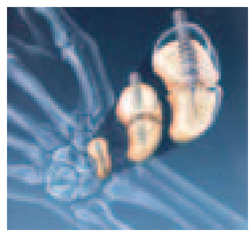
Products Handled by Kobayashi Medical Division



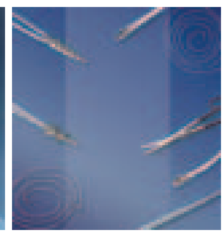
Conmed electric scalpel



NGK Spark Plug *CERATITE* (bone prosthesis)



Acumed ACUTRAK headless compression screw

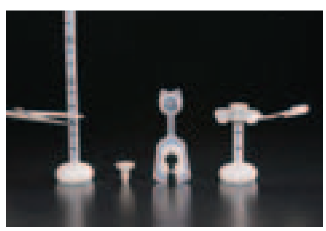


Arthrex Arthroscopy Products

Products Handled by Medicon

BARD I.C. Silver Foley Tray (Complete Care™)

BARD X-Port isp with Groshong 8.0 French Catheter



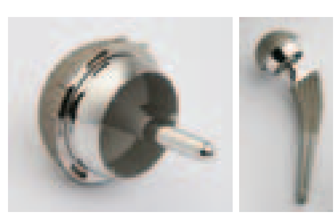
BARD Genie System Ⅱ (PEG type Ⅱ)

POINT ❷ Promoting the introduction of new products

The Kobayashi Medical Division has been concentrating its resources on researching overseas medical device manufacturers in an effort to be first to introduce the most advanced medical devices from overseas into the Japanese market. Moreover, with the orthopedics field expected to expand in line with the graying of society, in April 2003, the division established an orthopedics department. Through this department, the division is concluding distribution agreements with manufacturers in the orthopedic field in Europe and the U.S. to import and market the latest medical devices in Japan.

In October 2006, targeting further development, we concluded a distribution agreement with Corin Group PLC of the U.K., and began to sell their products in April 2007. Corin is a manufacturer of orthopedic implants with distinctive products, especially in knee and hip prosthesis systems, where it boasts highly original development capabilities and expertise in production technologies.

As a result of this tie-up, we will bolster our range of products with the addition of complete artificial joint systems to supplement the osteosynthetic implants we are already marketing such as osteosynthetic bone material and bone-marrow screws. These improvements are aimed at further enhancing our reputation for reliability among medical institutions and increasing our market share.



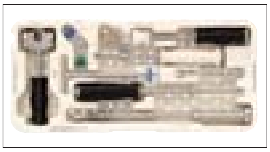
Colin Colmet/Optimum prosthesis system

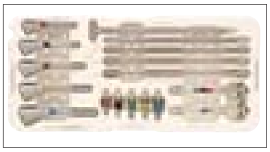
Developing Manufacturing Functions

POINT 1 Promoting Proprietary Brand *Kobamed*

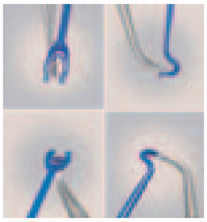
Since its establishment in 1992, the Kobayashi Medical Division has won many accolades from medical professionals for introducing leading-edge medical devices to domestic medical institutions, primarily from Europe and the U.S. Meanwhile, to provide devices that fit the requirements of the Japanese market, we also launched our own brand *Kobamed* to develop proprietary products. We have already started selling products that we developed in-house, such as instruments for minimum incision surgery in the urological field and the *KIAPEX* hip prosthesis system.

Proprietary Products — *Kobamed* Brand





KIAPEX bipolar hip prosthesis



Instruments for minimum incision surgery

Kobamed Epiduroscope System

POINT 2 eVent Medical Limited becomes a subsidiary

In November 2006, we made eVent Medical of Ireland a subsidiary. Since its founding, eVent has worked to develop, manufacture, and sell reliable ventilators that are easy for clinicians to use and trouble-free.

In the Medical Devices Operation, in addition to our existing trading functions, we have also taken on the challenge of developing our manufacturing functions. By making eVent Medical a subsidiary, we have made substantial progress toward that goal.

Development of new products and improvement of existing products

In addition to marketing existing products, eVent Medical will work aggressively to meet medical needs by developing new products and improving existing products. In cooperation with the Kobayashi Medical Division, eVent will also develop products related to ventilators, such as tubes.

Inspiration Infant

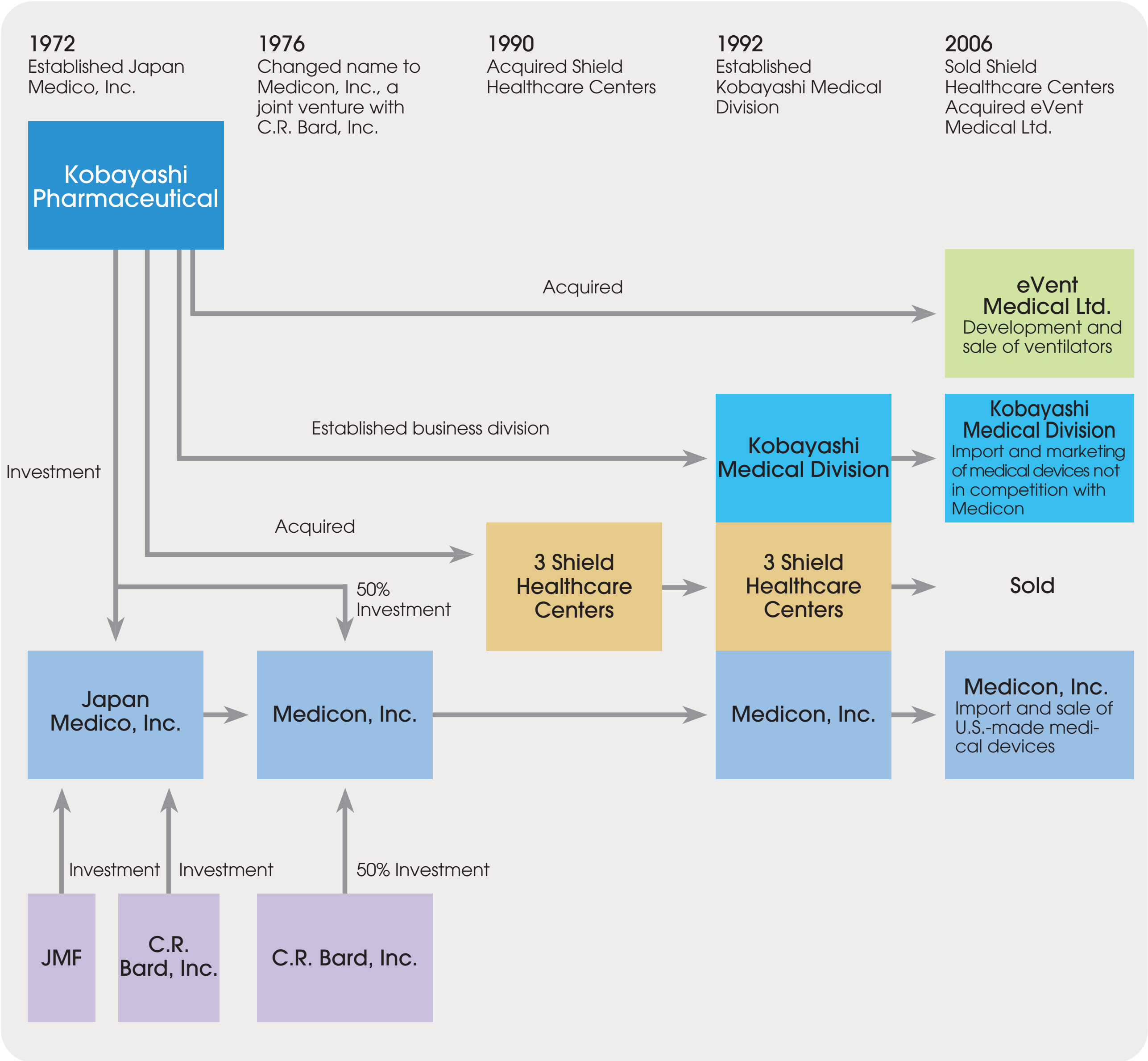
Inspiration LS

POINT 3 Bolstering our global sales system

eVent Medical already has a sales network in Europe and East Asia, and in the near future we will strengthen the sales network in the United States. In spring 2008, we also plan to begin sales in Japan, which is the second largest market in the world for medical devices. Sales will be conducted through the Kobayashi Medical Division. We are already selling ventilator-related products domestically under the *Inspiron* brand name, and with the addition of ventilator products from eVent Medical, we will be able to propose total solutions for respiratory care.

Through this range of measures in Japan and overseas, we aim to achieve an annual profit for eVent Medical in three years' time.

Kobayashi Pharmaceutical's Growing Medical Devices Operation



Withdrawal from home care operations in the United States (Shield Healthcare Centers)

In 1990, we acquired Shield Healthcare Centers, through which we have sold medical devices for patients being cared for at home in the United States. At the time of the acquisition, we anticipated that Shield Healthcare Centers' business model could provide a precedent for future home care-oriented business in Japan. However, due to differences in the health insurance systems in Japan and the United States, we were unable to develop the business model as we had initially planned, and we did not anticipate synergies with our existing businesses. As a result, in November 2006, we transferred all of our shareholdings in the Shield Healthcare Centers to Dharma Ventures Group, Inc., a company that was established by the Shield Healthcare Centers' management team.

Wholesale Operation

Changes in the Wholesale Operation

Reorganization of wholesale operations

Changes in the Wholesale Operation

Kobayashi Pharmaceutical started out as a wholesaler of pharmaceutical products and subsequently expanded to incorporate the three businesses comprising its operations today: consumer products, wholesale and medical devices. To establish a position in the wholesale distribution of OTC drugs, the Company spun off its wholesale operations to form Kobashou Co., Ltd. in 2001. In April 2006, we made Sowa Co., Ltd. (currently KS Tohoku Co., Ltd.), into a subsidiary and expanded our wholesaling network nationwide, with the exception of the Kyushu region. Currently, we command the number one position in the wholesale distribution of OTC drugs, and we can accommodate the increasingly wide areas served by drug stores, our principal clients.

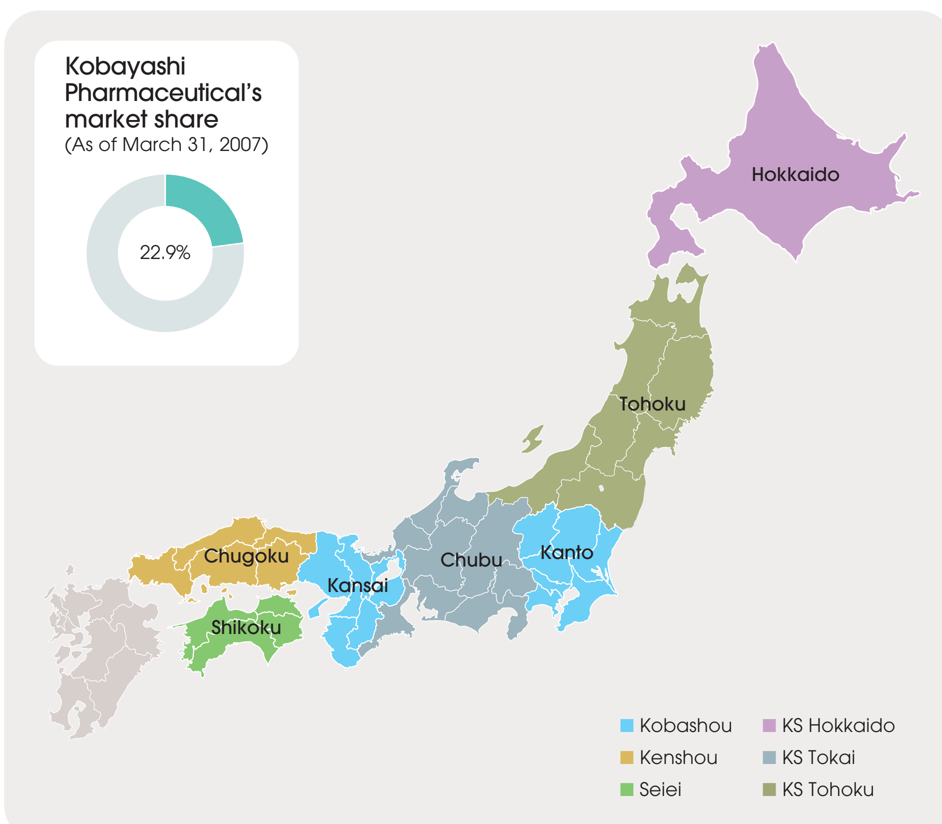
Reorganization of wholesale operations

Against this backdrop, in December 2006 we began discussions regarding a management integration between Kobashou and Paltac Corporation, aiming to achieve our goals of nationwide coverage and annual sales of ¥300.0 billion. The latter company is a consolidated subsidiary of Mediceo Paltac Holdings Co., Ltd.

Kobashou, which is a highly specialized wholesaler with strengths suited to the current age of self-medication, principally handles OTC drugs, health foods, and sundries. Paltac is a full-line wholesale distributor of products closely linked to consumer lifestyles—such as cosmetics, sundries, and OTC drugs—with a focus on customer satisfaction and solution-based proposals. In response to deregulation and other changes in the operating environment, Paltac aims to contribute to health and beauty, earning the trust of customers as it works to be a new, next-generation wholesaler with leading-edge capabilities. Although both companies have achieved operational growth in their own specialized fields, in the future there will be a need in the marketplace for a wholesaler that can transcend those boundaries.

Kobashou and Paltac are both leaders in their fields, and based on a relationship of mutual trust, collaboration, and cooperation, we will work to reinforce wholesale operations with a customer orientation.

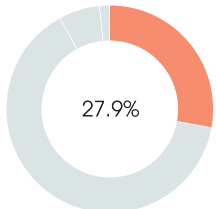
Kobashou Group Service Area and Market Share

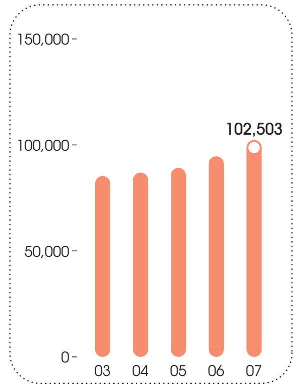


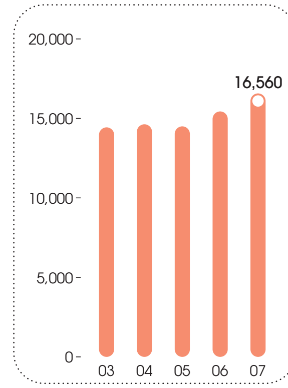
Business Segments at a Glance

Share of Sales (%) | Sales (¥ million) | Operating Income (¥ million)

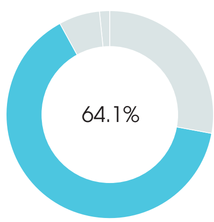
Consumer Products Operation

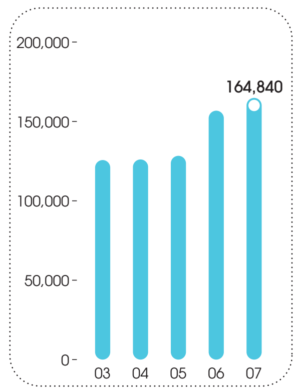


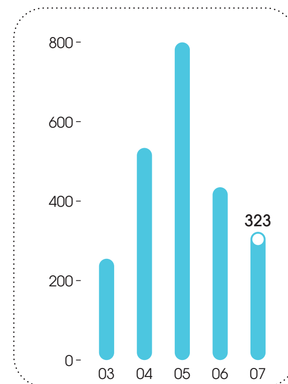




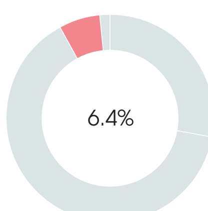
Wholesale Operation

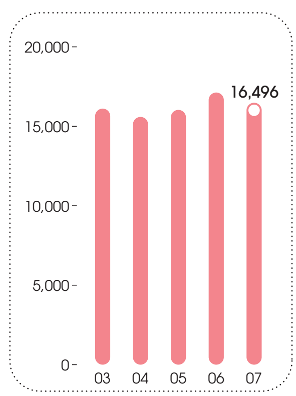


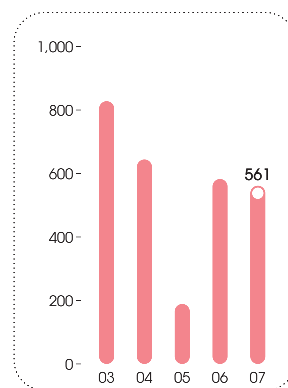




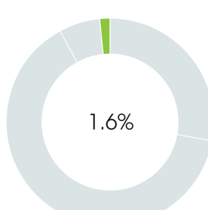
Medical Devices Operation

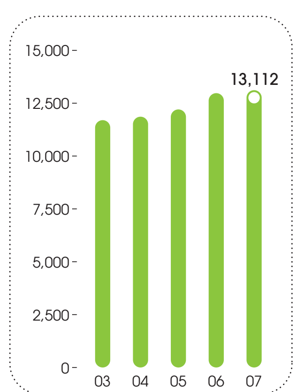


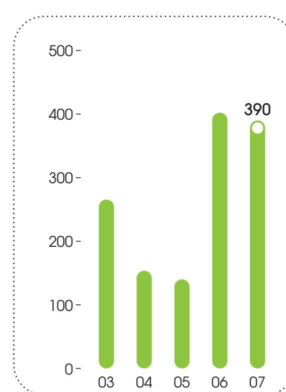




Other Operations







Note: The share of sales for each segment is calculated based on sales to external customers.

Main Group Companies

- Kobayashi Pharmaceutical Co., Ltd.
- Sendai Kobayashi Pharmaceutical Co., Ltd.
- Toyama Kobayashi Pharmaceutical Co., Ltd.
- Ehime Kobayashi Pharmaceutical Co., Ltd.
- Kiribai Chemical Co., Ltd.
- Kobayashi Healthcare, LLC.
- Kobayashi Healthcare Europe, Ltd.
- Kobayashi Healthcare Germany GmbH
- Shanghai Kobayashi Daily Chemicals Co., Ltd.
- Kobayashi Pharmaceutical (Hong Kong) Co., Ltd.
- HeatMax, Inc.
- Mediheat, Inc.
- Thermomax, Inc.
- Kobayashi Healthcare of America, Inc.
- Itoh Kanpo Pharmaceutical Co., Ltd.

Kobayashi Pharmaceutical is working to speed up product development in its mainstay Consumer Products Operation. To this end, an integrated product development and incubation system called the Category System was launched in April 2005. In parallel, top management is now involved in Idea Meetings from the earliest stages of product development. By launching around 30 new items every year, we aim to continually unveil innovative products that have a strong impact on consumer markets, as we strive to raise the contribution of new products to sales. We are currently putting emphasis on the healthcare categories of pharmaceuticals, oral hygiene products, and foods in particular. Efforts are also focused on M&As, including acquisitions of brands and companies. Overseas, we will strive to strengthen sales centered on body warmers in China, our top priority market.

- Kobashou Co., Ltd.
- Kenshou Co., Ltd.
- Seiei Co., Ltd.
- KS Hokkaido Co., Ltd.
- KS Tokai Co., Ltd.
- KS Tohoku Co., Ltd.

In 2001, Kobayashi Pharmaceutical spun off its wholesale operation to form Kobashou Co., Ltd. In 2006, Kobashou made Sowa Co., Ltd. a consolidated subsidiary, extending its area of operations to cover the whole of Japan excluding Kyushu. Going forward, Kobayashi Pharmaceutical will continue to pursue integration and greater efficiency in systems and logistics with the overriding goal of increasing annual sales from the Wholesale Operation to ¥300 billion. In this regard, the Company has commenced discussions regarding a management integration between Kobashou and Mediceo Paltac Holdings Co., Ltd.

- Kobayashi Pharmaceutical Co., Ltd.
- Kobayashi Pharmaceuticals of America, Inc.
- Kobayashi Medical America, LLC
- eVent Medical Inc.
- eVent Medical Ltd.
- eMed Ltd.
- Medicon, Inc.

The Kobayashi Medical Division imports and markets medical devices from manufacturers in Europe and the U.S. in Japan and also manufactures and sells proprietary medical devices developed in-house. In April 2004, the division formed an organization for the development of proprietary products, and since then has been manufacturing and selling products under the *Kobamed* brand. In November 2006, the division made eVent Medical Ltd. a subsidiary. By enhancing manufacturing functions alongside traditional trading functions, we aim to increase sales of proprietary brand products to 25% of total sales of this division. Going forward, we will concentrate particularly on the orthopedics and surgery room fields, which still have much more growth potential.

- Aoitori Distribution Co., Ltd.
- Kobayashi Pharmaceutical Distribution Co., Ltd.
- Kobayashi Seiyaku Plax Co., Ltd.
- Suehiro Sangyo Co., Ltd.
- Archer Corporation
- SP-Planning, Inc.
- Kobayashi Pharmaceutical Life Service Co., Ltd.
- Kobayashi Pharmaceutical Sales Promotion, Ltd.

Other Operations are conducted in support of the Company's three core businesses, namely the Consumer Products Operation, the Wholesale Operation, and the Medical Devices Operation. Support services include transportation, sales promotion, and market research. Each company in this segment manages its operations to achieve profitability on a standalone basis, while constantly reviewing the prices of materials and services to contribute to the three core businesses.

Kobayashi Pharmaceutical's Approach to CSR

Every company must fulfill its role as a member of society. That role includes providing safe, reassuring products and services and developing the human resources needed to do so. In addition, companies are able to contribute to local communities and to the solution of social problems in a way that individuals and other organizations cannot. The Kobayashi Pharmaceutical Group is committed to fulfilling those roles as a responsible member of society.

Promoting Corporate Brand Management

Kobayashi Pharmaceutical implements corporate brand management to enhance corporate value under the slogan, "You make a wish and we make it real." In this process, the Group recognizes that one of its most important management tasks is to not only provide products and services that meet customers' expectations, but also to earn the respect of society by fulfilling its social responsibilities. These responsibilities include creating a compliance system that encompasses corporate ethics, taking initiatives to protect the environment, and ensuring product quality and safety.

To ensure a proactive approach to driving forward corporate brand-related measures, every year since 2003 each Group department has had its own action plan aimed at enhancing the corporate brand. These action plans form the basis for departments' activities during the year; each department deliberates on what it is that stakeholders want, and uses the answers to identify areas to be included in its action plan.

In order to reinforce our commitment to corporate social responsibility and its related activities, we established the Corporate Brand Office in April 2006. Through these and other initiatives, we strive to raise our corporate value.

Kick Off poster

Product Quality and Safety

Product quality and safety are key points of focus for product manufacturers. To ensure high levels of quality and safety, the Kobayashi Pharmaceutical Group has established stringent standards for multifaceted review and evaluation at every stage, starting with the initial stage of product development.

In its pharmaceutical product operations, the Quality Assurance Department, which reports directly to the president, establishes quality assurance frameworks and conducts inspections. The department monitors the entire process from the product development and planning stages through to raw materials and equipment used in the manufacturing plant. In addition, it uses feedback obtained through the Customer Consulting Office to strive to improve product quality.

In medical devices operations, the Quality Assurance Division is in charge of overall quality and safety. The division supervises the process from manufacturing to shipment in accordance with the requirements of ISO 13485, the international standard for quality management systems pertaining to medical devices. In addition, the division cooperates with sales divisions to obtain information on how products perform during actual treatment of patients.

•Evaluating efficacy and safety for humans

In order to provide products for which quality can be guaranteed, the Kobayashi Pharmaceutical Group has established three specialized committees based on development stages. In this way, we are working to ensure efficacy and safety for humans.

The Safety Testing and Analysis Committee determines items to be evaluated for safety and evaluation methods needed for each product. The Animal Testing Committee considers ethical issues and scientific justification in regard to the necessity and appropriateness of animal testing. In accordance with the Declaration of Helsinki*, the Internal Clinical Testing Committee examines clinical testing plans from both ethical and scientific viewpoints.

* Ethical rules for medical research involving humans

Human Resources Development

Human resources development is an important priority for implementing "Creativity and Innovation," the key point of our management philosophy, and our slogan, "You make a wish and we make it real."

In 2005, we revamped our employee training programs. To rapidly cultivate candidates for management positions and realize strong frontline operations, we are working to reinforce managerial abilities and to enhance the capabilities of all employees.

Moreover, with a clear image of the attributes that we are looking for in our employees and a commitment to job security whether the Company is performing well or not, we are working to sustain and continually improve the capabilities of our human resources. Furthermore, by aggressively recruiting mid-career employees, we ensure that our employees have diverse attributes and introduce new expertise. In these ways, we endeavor to establish a corporate culture that continually fosters "Creativity and Innovation."

10 Attributes We Look for in Employees

1. Likes new things
2. Hates to lose
3. Asserts him/herself clearly
4. Communicates frankly
5. Perseveres
6. Energetic
7. Devoted to work
8. Not afraid of challenges or failure
9. Offers something unusual
10. Pleasant and likeable

Environmental Initiatives

The Kobayashi Pharmaceutical Group is aware of the impact its products have on the environment at every stage of the product life cycle from development and design through manufacture, sales and eventual disposal. As such, it is engaged in efforts to protect the environment, such as making the most effective use of resources and preventing global warming.

In the fiscal year ended March 2007, we ramped up our capacity for drug production under contract, and as a result of the repeated test runs and other additional activities required, our CO_2 emissions increased. On the other hand, we achieved an 8.7% reduction in waste overall and pursued measures to ensure an environmentally friendly approach with regard to product containers and wrappings, among other issues. However, there were some areas where we did not meet our goals, such as improving recycling rates and promoting green procurement. We will position these goals as future challenges and continue taking steps to achieve them.

Looking ahead, Kobayashi Pharmaceutical will continue to consider environmental protection activities one of its most essential management tasks and step up its measures at every stage from development and design to manufacture, distribution, use and disposal.

Social Contribution Activities

In November 1993, the Group established the Kobayashi Pharmaceutical UNICEF Fund, whereby it collects donations to support the underprivileged worldwide. The Company is also actively participating in such activities as the breast cancer Pink Ribbon Campaign, disaster relief activities, and local clean-up and tree-planting initiatives.

•Contributions through markets for secondhand goods

Led by employees of the head office departments, unused goods, such as clothing, handbags, and neckties, are collected from the homes of directors and employees and taken to a secondhand goods market in July and October. The money obtained from the sale of these items is donated to the Osaka Prefecture Greenery Fund. Items that are not sold are donated to the Loving Hands Charity Auction*.

* Loving Hands Charity Auction
This is a charitable event sponsored by the Mainichi Newspaper. Goods contributed by individuals and companies are auctioned off and the proceeds are donated to a family assistance society that searches for foster parents for children without families.

A secondhand goods market

•Support for the Japanese Society of Eucommia

The Japanese Society of Eucommia is a research society that is dedicated to collecting research about the eucommia tree—the bark of which is used as an ingredient in traditional Chinese medicine—and widely disseminating the results. At the same time, the society fosters new development of the eucommia tree's potential and promotes related research and activities. Eucommia research is being actively implemented in a wide range of fields, such as pharmaceuticals, health foods, and industrial raw materials. Kobayashi Pharmaceutical is proud to participate in the Japanese Society of Eucommia.

The Japanese Society of Eucommia

Corporate Governance

Kobayashi Pharmaceutical recognizes raising shareholder value as a key priority for achieving its fundamental management policy of maximizing corporate value. For this reason, we have implemented various measures to enhance corporate governance, including providing timely and accurate disclosure and improving management transparency.

Following approval by the general shareholders' meeting in June 2000, several measures were implemented to reshape the management structure so as to promote the separation of management and business execution functions. These included the adoption of an executive officer system and an in-house company system. Furthermore, in April 2004, the Kobayashi Pharmaceutical Group was reorganized into four business headquarters: the Product Business Headquarters, Wholesale Business Headquarters, Medical Device Business Headquarters and Group Corporate Business Headquarters. Executive officers execute business operations under the president and general managers of operating divisions. The Board of Directors, headed by the chairman, oversees these activities. In addition, the number of directors has been reduced to an optimal level to revitalize the Board of Directors.

The Board of Directors holds regular monthly meetings and special meetings as necessary. The Board decides on important matters relating to management and other issues required by law and regulations, and regularly monitors the execution of operations.

The Company has not appointed outside directors, but is confident that management decisions are being made promptly and appropriately by people who understand and can faithfully implement its management philosophy. However, reinforcing the Company's governance structure based on corporate auditors remains a key priority. The Board of Corporate Auditors consists of four corporate auditors, two of whom are outside corporate auditors. There are no equity relationships or business ties between the Company and its outside auditors. In addition, the number of internal auditing staff has been increased as part of efforts to reinforce audit functions.

The Company exchanges views on improving its operations with its independent auditor, Ernst & Young ShinNihon, through regular monthly meetings and other means. As part of the decision-making process, management also refers to advice from legal counsel and other experts on issues related to company management and day-to-day business affairs, as necessary.

In April 2003, the Company established a Compliance Committee (renamed the Internal Control Committee in May 2007) to foster a strong spirit of compliance with laws and regulations in all corporate activities. In September 2003, the Compliance Committee formulated Basic Policies on Corporate Behavior and Standards of Conduct for Directors and Employees. We are taking measures to apply these standards throughout the organization, as part of efforts to enhance awareness of compliance. In January 2003, Employee Consulting Centers were established both inside and outside the Company to facilitate internal reporting and ensure that the Company promptly gathers and responds to the latest information.

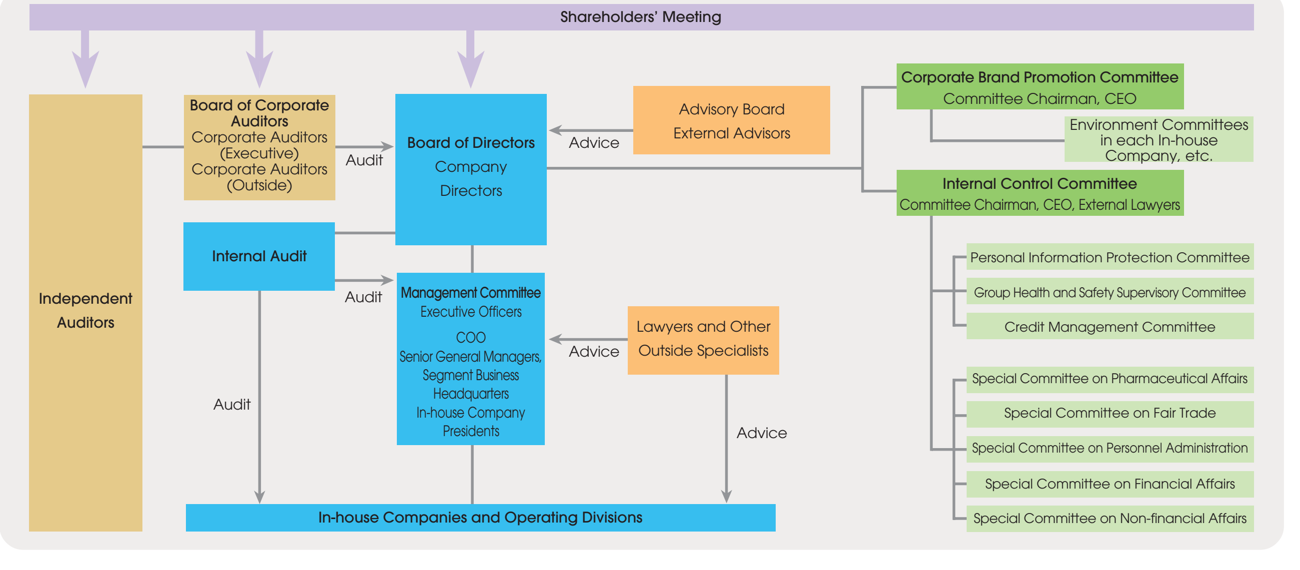
In addition, the Kobayashi Pharmaceutical Group is actively promoting opportunities for the views of on-site employees to be heard by top management, in order to create a favorable corporate climate where opinions can be freely exchanged. The Company believes that maintaining and developing this corporate climate is an effective means of ensuring strong corporate governance.

Introduction of Anti-takeover Measures

At the general shareholders' meeting held on June 28, 2007, the introduction of countermeasures to large-scale stock acquisitions (anti-takeover measures) was approved. The objectives of these measures are to secure and further enhance corporate value and profits and to prevent inappropriate takeovers.

In the event of large-scale stock acquisitions, these measures will ensure adequate information and time for shareholders to evaluate the appropriateness of the acquisitions and for the board of directors to formulate a counter plan. Moreover, with sufficient information, shareholders will be able to determine if a response to the large-scale stock acquisition is necessary, which will contribute to ensuring, and further raising, profits for all shareholders.

Corporate Governance Organization



Directors, Corporate Auditors and Officers (As of June 29, 2007)

Directors

Chairman and Chief Executive Officer
Kazumasa Kobayashi

President and Chief Operating Officer
Yutaka Kobayashi

Senior Executive Director
Akira Horiguchi
Senior General Manager, Medical Device Business Headquarters

Senior Executive Director
Jyoji Miki
President, Product Sales Company

Executive Director
Masaaki Tanaka
President, Manufacturing Company

Executive Director
Takashi Tsujino
President, Research and Development Company

Executive Director
Akihiro Kobayashi
President, International Sales Company and Manager, Marketing Office

Director
Satoshi Yamane
Senior General Manager, Group Corporate Business Headquarters

Corporate Auditors

Statutory Auditor
Toshiyuki Morii

Statutory Auditor
Masahiro Hiraoka

Auditor
Hiroshi Hayashi

Auditor
Ryuji Sakai

Executive Officers

Hiroshi Nomoto
President, Kiribai Chemical Co., Ltd.

Takafumi Sakaguchi
President, Kobayashi Medical Division

Hidetsugu Yamamoto
President, Business System Company

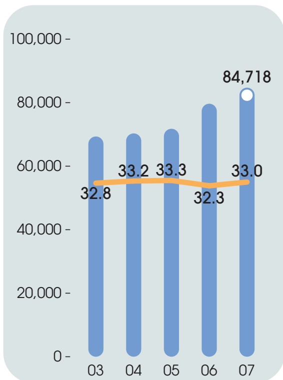
Haruyoshi Kosaka
Officer-in-charge, Wholesale Business Headquarters and President, Kobashou Co., Ltd.

Kunio Moriya
Manager, Wide Area Chain Store, Product Sales Company

Susumu Horiuchi
Manager, Product Sales Company

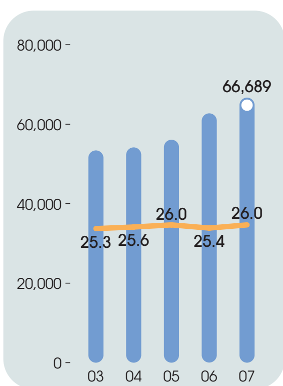
* Yutaka Kobayashi, Akira Horiguchi, Jyoji Miki, Masaaki Tanaka, Takashi Tsujino, Akihiro Kobayashi and Satoshi Yamane concurrently serve as executive officers.

Gross Profit and
Gross Profit to Net Sales
(¥ million/%)



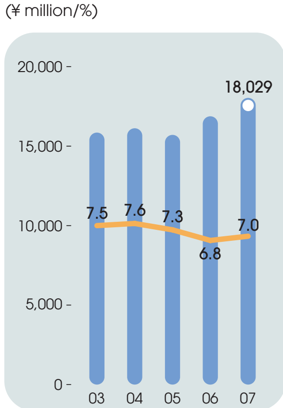
Gross Profit
Gross Profit to Net Sales

SG&A Expenses and
SG&A Expenses to Net Sales
(¥ million/%)



SG&A Expenses
SG&A Expenses to Net Sales

Operating Income and
Operating Income to Net Sales
(¥ million/%)



Operating Income
Operating Income to Net Sales

"You make a wish and we make it real"

The Kobayashi Pharmaceutical Group follows a management policy that defines the Company's mission as providing people and society with comfort through continuous "Creativity and Innovation." We will continue to work toward realizing the concept of our brand slogan—"You make a wish and we make it real"—by providing products and services for the health, comfort and happiness of all stakeholders.

Kobayashi Pharmaceutical is committed to the ongoing pursuit of "Something New, Something Different" through the development of products and services that meet consumer needs in the current age of rapid change and intensifying competition. We believe that this process is the driving force behind growth, and through this pursuit, we will work to raise stakeholder satisfaction by increasing the Group's corporate value.

Scope of Consolidation and Application of the Equity Method

Kobayashi Pharmaceutical has 32 consolidated subsidiaries, 18 in Japan and 14 overseas, and two affiliates in Japan accounted for by the equity method. The Company classifies its business activities into four segments: Consumer Products Operation (13 consolidated subsidiaries and 1 equity-method affiliate); Wholesale Operation (6 consolidated subsidiaries); Medical Devices Operation (5 consolidated subsidiaries and 1 equity-method affiliate); and Other Operations (8 consolidated subsidiaries).

Overview

In the fiscal year under review, crude oil prices were unstable, but there were signs of improvement in corporate profits and in the labor market. The Japanese economy benefited from a steady recovery in business conditions. On the other hand, despite a moderate recovery trend in consumer spending, the future course of business conditions remained uncertain.

In this environment, the Kobayashi Pharmaceutical Group took steps to fully express the spirit of its management philosophy of "Creativity and Innovation." The Group cultivated latent customer needs by introducing new products and services to seed new markets while activating existing markets by offering products and services with new added value. At the same time, Kobayashi Pharmaceutical also made aggressive efforts to form business partnerships, acquire companies, and pursue overseas business expansion.

Although we invested heavily in advertising to develop our brands, we also recorded increased sales in categories with high profit margins. In addition, we reduced costs with thorough manufacturing cost reduction measures, and we reviewed sales promotion expenses. As a result, we generated increased operating income.

Net Sales

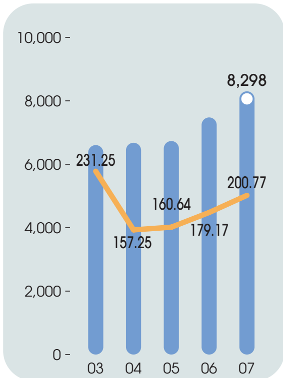
The Consumer Products Operation recorded an increase in sales due to the contribution of new products and to stronger overseas sales of body warmers. In the Wholesale Operation, the business environment was challenging, as unseasonable weather led to sluggish sales of seasonal products to drugstores, our principal customers. Nevertheless, we acquired all outstanding shares in KS Tohoku (formerly Sowa Co., Ltd.), and the Wholesale Operation recorded higher sales. In the Medical Devices Operation, we faced a difficult environment in Japan due to reductions in official drug prices. In this setting, the division concentrated its sales efforts in the orthopedic surgery field, where demand is expected to increase resulting in strong sales of proprietary brand products. However, because we did not anticipate synergies with our existing operations, during the year we sold all of our shares in the three Shield Healthcare Centers in the U.S., which were subsidiaries. As a result, the Medical Devices Operation registered a decline in sales. As a result, consolidated net sales for the year under review were up 4.1% from the previous fiscal year, to ¥257,022 million.

Gross Profit and Operating Income

After provisions for returned products, the cost of sales increased 3.0%, or ¥5,065 million, from the previous fiscal year, and gross profit rose 6.4% to ¥84,718 million. The Company continued to invest heavily in advertising to develop its brands, and selling, general and administrative (SG&A) expenses increased 6.3%, or ¥3,955 million. As a net result of the foregoing, operating income rose 6.8%, to ¥18,029 million.

The ratio of gross profit to net sales rose from 32.3% in the previous fiscal year to 33.0% in the year under review, and the ratio of operating income to net sales increased from 6.8% to 7.0%. These gains were primarily attributable to the substantial growth in sales recorded by the Consumer Products Operation, which has high profit margins.

Net Income and Net Income per Share
(¥ million/yen)



Net Income
Net Income per Share

Note: Kobayashi Pharmaceutical conducted a 1.5-for-1 stock split on November 20, 2003.

Income Before Income Taxes and Net Income

Income before income taxes and minority interests increased 14.5%, to ¥16,038 million, and net income rose 11.0% to ¥8,298 million.

Net income per share increased 12.0%, to ¥200.77, compared to ¥179.17 in the previous fiscal year.

Segment Information

The Kobayashi Pharmaceutical Group's business is classified into four segments: Consumer Products Operation, Wholesale Operation, Medical Devices Operation, and Other Operations.

Inter-group sales and transfers, which are included in segment sales, amounted to ¥34,962 million in the previous year and ¥39,930 million in the year under review.

Net Sales and Operating Income by Segment

Net Sales

(¥ million)

Consumer Products Operation	2003	2004	2005	2006	2007
Sales to third parties	66,027	66,523	67,525	68,869	71,717
Inter-group sales and transfers	19,532	20,532	21,749	25,908	30,786
	85,559	87,055	89,274	94,777	102,503
Wholesale Operation					
Sales to third parties	125,858	126,080	128,356	156,933	164,839
Inter-group sales and transfers	0	–	–	0	1
	125,858	126,080	128,356	156,934	164,840
Medical Devices Operation					
Sales to third parties	16,113	15,609	16,056	17,127	16,496
Other Operations					
Sales to third parties	2,923	3,458	3,771	3,923	3,970
Inter-group sales and transfers	8,783	8,401	8,434	9,053	9,143
	11,706	11,859	12,205	12,976	13,113

Operating Income

(¥ million)

	2003	2004	2005	2006	2007
Consumer Products Operation	14,438	14,631	14,493	15,447	16,560
Wholesale Operation	255	535	799	436	324
Medical Devices Operation	829	645	190	583	561
Other Operations	265	153	140	402	390

■Consumer Products Operation

We launched 35 new consumer products, not including nutritional supplements available only through direct sales, as part of efforts to create new markets and expand existing markets. Of these products, especially strong contributions to our improved performance were made by *Nicitol 85*, a diet pill for reducing abdominal fat; *Cleair*, an air freshener that eliminates unpleasant household odors by releasing ions; and *Araitate Shoshu Shabon*, a deodorizing air freshener that gives rooms a refreshing clean scent. Domestic sales of body warmers were sluggish in the year under review due to the record-setting warm winter. Nonetheless, the body warmer business is gaining ground overseas, and we took steps to increase sales of thermal socks. As a result, sales increased.

Net Sales and Operating Income

In the year under review, sales in the Consumer Products Operation increased 8.2% from the previous fiscal year, to ¥102,503 million. The segment's contribution to consolidated net sales was 27.9%.

By product category, sales of pharmaceuticals rose by a large margin, up 20.5%; sales of deodorizing air fresheners were up 6.1%; and sales of body warmers rose 12.8%. Sales of oral hygiene products and sanitary products were up 10.0% and 4.1%, respectively. However, sales of food products fell 2.1% from the previous year, and sales of household sundries declined 0.4%.

Operating income rose 7.2% from the previous year, to ¥16,560 million. This gain was attributable to growth in sales of products with high profit margins and to thorough efforts to cut manufacturing costs.

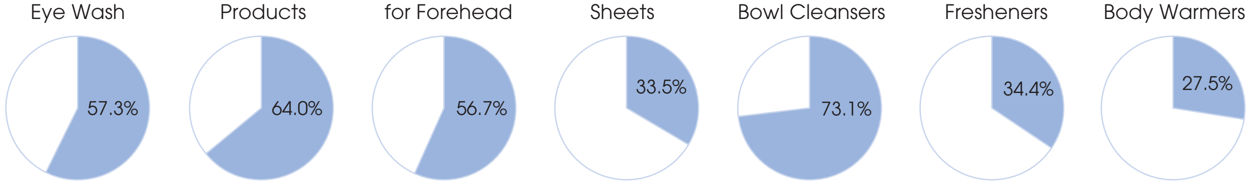
Sales by Category

(¥ million)

	2006		2007		Changes	
	Sales	% of Total Sales	Sales	% of Total Sales	Amount	Change (%)
Pharmaceuticals	16,434	17.3	19,799	19.3	3,365	20.5
Oral hygiene products	10,741	11.3	11,811	11.5	1,070	10.0
Sanitary products	13,256	14.0	13,796	13.5	540	4.1
Deodorizing air fresheners	28,307	29.9	30,020	29.3	1,713	6.1
Household sundries	4,517	4.8	4,501	4.4	(16)	(0.4)
Food products	11,421	12.0	11,186	10.9	(235)	(2.1)
Body warmers	10,099	10.7	11,388	11.1	1,289	12.8
Total	94,776	100.0	102,503	100.0	7,727	8.2

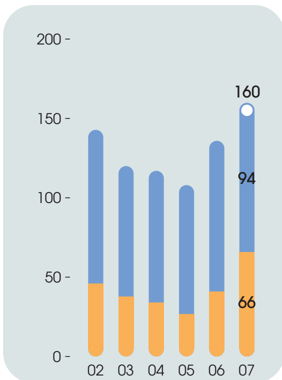
Market Share of Principal Brands (Pie Chart)

Eye Wash | Oral Hygiene Products | Cooling Gel Sheets for Forehead | Sanitary Sheets | Deodorizing Toilet Bowl Cleansers | Deodorizing Air Fresheners | Body Warmers

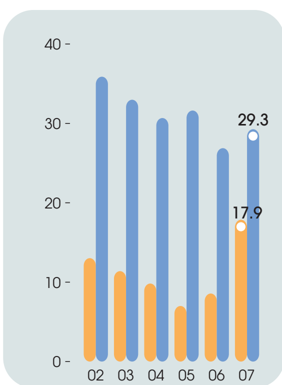


Eyebon | *Breath Care* | *Netsusama Sheet* | *Sarasarty* | *Bluelet* | *Sawaday, Shoshugen, etc.* | *Kiribai Haru*

Number of Profitable and Unprofitable Brands



New Products as a Percentage of Sales
(%)



Number of Profitable and Unprofitable Brands

	2002	2003	2004	2005	2006	2007
Profitable brands	97	82	83	81	95	94
Unprofitable brands	46	38	34	27	41	66

* The number of unprofitable brands includes certain new products.

New Products as a Percentage of Sales

(%)

	2002	2003	2004	2005	2006	2007
First year	13.0	11.4	9.8	7.0	8.6	17.9
First four years	35.9	33.0	30.7	31.6	26.9	29.3

Issues to be Addressed in the Fiscal Year Ending March 31, 2008

In an environment where product prices have generally stabilized, we worked to further increase sales with the launch in spring 2007 of 15 new products targeting emerging customer needs. These products included *Tamsil*, an athlete's foot medication that includes a fungicide ingredient and an anti-pruritic ingredient; *Tochu Gencha*, a 100% eucommia leaf tea that is a designated health food suitable for people with high blood pressure; and *Keshimin Pen*, a medicinal product that controls melanin formation while concealing worrisome black spots. For existing brands, the Company will aggressively promote sales in line with the marketing plans that are formulated for each brand. In overseas operations, we are working to create new markets, centered on body warmers.

As a result of these measures, we expect segment sales to increase 8.3% to ¥111,000 million.

We will continue working to reduce costs and investing aggressively in advertising to develop our brands. We are forecasting a year-on-year gain of 8.7% in operating income, to ¥18,000 million, as HeatMax, Inc. of the United States, which was acquired in November 2006, will make a full year's contribution to consolidated results from the fiscal year ending March 2008.

■Wholesale Operation

Due to unseasonable weather, the Wholesale Operation recorded flat sales of seasonal products to drugstores, our principal customers, and the market for health foods was sluggish. Moreover, industry realignment accelerated further as companies competed for survival.

Net Sales and Operating Income

On April 1, 2006, the Company acquired all of the outstanding shares of KS Tohoku Co., Ltd. (formerly Sowa Co., Ltd.). This acquisition contributed to a 5.0% increase in sales in the Wholesale Operation, to ¥164,840 million. Consequently, the segment's contribution to consolidated net sales increased from 63.6% in the previous fiscal year to 64.1%.

By product category, in drugs, sales of products increased 32.9% and sales of merchandise rose 11.8%. In sundries and food, sales of products declined 6.1%, and sales of merchandise were down 4.8%.

With regard to profits, the expanded operational reach enabled the Company to take advantage of economies of scale by purchasing products in bulk from manufacturers, which had a positive effect on the profit margin. Nonetheless, the profit margin did not improve as rapidly as we had expected due to the stock acquisition. As a result, operating income declined by 25.8% from the previous fiscal year, to ¥324 million.

Note: "Products" refers to goods procured from Kobayashi Pharmaceutical Co., Ltd., while "merchandise" refers to goods procured from other companies.

Sales by Category

(¥ million)

		2006		2007		Changes	
		Sales	% of Total Sales	Sales	% of Total Sales	Amount	Change (%)
Drugs	Products	10,459	6.7	13,901	8.4	3,442	32.9
	Merchandise	56,210	35.8	62,851	38.1	6,641	11.8
Sundries and food	Products	19,493	12.4	20,680	12.6	1,187	6.1
	Merchandise	70,772	45.1	67,406	40.9	(3,366)	(4.8)
Total		156,934	100.0	164,840	100.0	7,906	5.0

Issues to be Addressed in the Fiscal Year Ending March 31, 2008

We are working to expand our operations to new regions in response to the increasingly wide areas served by drug stores, our principal clients. We will work to further leverage the benefits of the stock acquisitions that we have implemented for that purpose. At the same time, we will invest aggressively in new categories, such as doctor-recommended skin care products. As a result, we are forecasting a 4.3% year-on-year increase in segment sales, to ¥172,000 million, and an 85.8% gain in operating income, to ¥600 million.

■Medical Devices Operation

The Kobayashi Medical Division, which leads the Medical Devices Operation, faced a difficult environment in the fiscal year ended March 2007 due to reductions in official prices. However, the division focused its sales efforts on surgical products, such as electric scalpels, and in the orthopedic surgery field, where demand is expected to increase. Proprietary brand products, which we are actively promoting, recorded strong sales.

The three Shield Healthcare Centers in the United States succeeded in raising profit margins by taking steps to reduce back-office costs, such as introducing new customer management systems. However, we do not anticipate synergies with existing businesses, so in November 2006, we transferred all of our shareholdings in these three companies to Dharma Ventures Group, Inc., which was established by the local Shield management team.

Net Sales and Operating Income

Sales of the Medical Devices Operation were down 3.7%, to ¥16,496 million. As a result, the segment's contribution to consolidated net sales declined to 6.4%, from 6.9% in the previous fiscal year.

By product category, the Kobayashi Medical Division, which has special strengths in products for orthopedic surgery, operating rooms, neurosurgery, and otorhinolaryngology, recorded an increase of 7.0% in sales. On the other hand, due to the transfer of shares in the three Shield Healthcare Centers, only 10 months of sales were recorded in the year under review, and sales for the year declined 15.4%.

As a result, operating income was down 3.6%, to ¥561 million. Equity in earnings of Medicon, Inc., an equity-method affiliate, were ¥110 million.

Sales by Category

(¥ million)

	2006		2007		Changes	
	Sales	% of Total Sales	Sales	% of Total Sales	Amount	Change (%)
Kobayashi Medical Division	7,544	44.1	8,072	48.9	528	7.0
Shield Healthcare Centers (3 firms)	8,586	50.1	7,262	44.0	(1,324)	(15.4)
Others	996	5.8	1,161	7.1	165	16.6
Total	17,126	100.0	16,496	100.0	(630)	(3.7)

Issues to be Addressed in the Fiscal Year Ending March 31, 2008

The Kobayashi Medical Division will bolster its product lineups in existing fields, such as operating room and orthopedic surgery products. At the same time, the division will aggressively develop proprietary products. Also, eVent Medical Ltd., which was acquired in November 2006, is working in global sales of ventilators and in the development of new products.

Due to such factors as the transfer of all shares in the three Shield Healthcare Centers, we expect a year-on-year decline of 31.5% in segment sales, to ¥11,300 million. We are forecasting a decline of ¥961 million in operating results, for an operating loss of ¥400 million.

■Other Operations

Other Operations, which include such activities as transportation, sales promotion, and market research, are conducted on a financially independent basis. Their objective is to support the Company's three principal businesses and to contribute to the profits of those businesses. The Group reviewed the transfer values of the materials and services these companies provide.

As a result, sales of Other Operations rose 1.0%, to ¥13,113 million. Operating income declined 3.0%, to ¥391 million.

Analysis of Financial Position

Assets

Total assets were ¥164,556 million as of March 31, 2007, an increase of 8.3% from the end of the previous fiscal year. This rise was primarily attributable to increases in goodwill due to M&As.

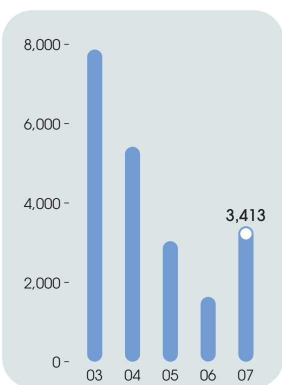
Current assets rose 3.2%, to ¥102,102 million. Due to aggressive M&A activities, the balance of cash and time deposits declined 26.0%, or ¥6,346 million. However, as a result of the new consolidation of subsidiaries, trade notes and accounts receivable rose 7.6%, or ¥3,638 million, and inventories rose 13.3%, or ¥2,324 million.

Property, plant and equipment, net declined 2.2% to ¥22,279 million. This was mainly the result of depreciation and amortization of existing assets.

Intangible assets were up 124.0% from the previous fiscal year-end, to ¥14,603 million. The principal reasons for this rise were increases in goodwill.

Investments and other assets were up 7.8% from the end of the previous fiscal year, to ¥25,571 million. This rise was primarily attributable to an increase of 15.1%, or ¥2,365 million, in investments in securities that resulted from a gain on valuation of investment securities.

Interest-bearing Debt
(¥ million)



Liabilities

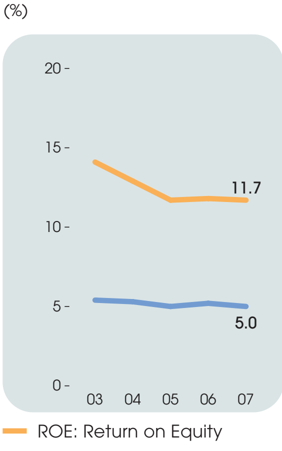
Total liabilities were ¥87,320 million at March 31, 2007, up 6.2% from the previous fiscal year-end. Current liabilities increased 6.9% to ¥77,028 million. This was mainly due to an increase of ¥2,138 million, or 4.3%, in trade notes and accounts payable resulting from the new consolidation of subsidiaries. Short-term loans payable increased 133.7%, to ¥3,206 million. Consequently, the current ratio declined 4.7 percentage points from a year earlier, to 132.6%.

Long-term liabilities were up 1.1%, to ¥10,292 million. This rise was principally due to an increase of ¥495 million, or 7.0%, in accrued retirement benefits for employees. Long-term debt at the end of the fiscal year under review was ¥208 million, down 20.6% from a year earlier.

Net Assets

Net assets, the total of shareholders' equity and minority interests at fiscal year-end, were up 10.8%, to ¥77,236 million. The principal factor was an increase in retained earnings of ¥6,688 million. Treasury stock, at cost, declined ¥169 million, to ¥3,311 million, due principally to the exercise of stock options. As a result, the equity ratio increased 1.2 percentage points, from 44.0% a year earlier to 45.2% at the end of the fiscal year under review. The return on equity (ROE) decreased 0.1 percentage point, from 11.8% to 11.7%. The ratio of net income to total assets (ROA) decreased 0.2 percentage points, from 5.2% to 5.0%.

ROE and ROA
(%)



KOBAYASHI PHARMACEUTICAL CO., LTD.
Annual Report 2007

Cash Flow Analysis

Cash Flows From Operating Activities

In the fiscal year ended March 2007, net cash provided by operating activities was ¥8,834 million. In comparison with the previous fiscal year, this was a decline of ¥4,325 million. Income before income taxes and minority interests increased by ¥2,028 million, but trade notes and accounts payable decreased by ¥4,997 million and income taxes paid increased ¥1,376 million.

Cash Flows From Investing Activities

Net cash used in investing activities was ¥11,803 million. This was an increase of ¥5,388 million from the previous fiscal year. This increase was primarily due to ¥9,063 million in payments for acquisition of shares in an overseas subsidiary.

As a result, free cash flow declined by ¥9,713 million, to –¥2,969 million.

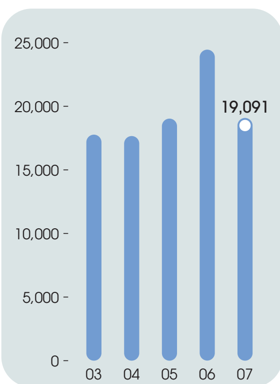
Cash Flows From Financing Activities

Net cash used in financing activities was ¥2,433 million, an increase in cash used of ¥1,013 million compared with the previous fiscal year. A principal factor was an increase in dividends paid in this fiscal period, although payments for purchase of treasury stock declined.

As a result, the balance of cash and cash equivalents at the fiscal year-end was ¥19,091 million, a decline of ¥5,346 million from a year earlier.

* The following formula was used to calculate free cash flow:
Free cash flow = Cash flow from operating activities + cash flow from investing activities

Cash and Cash Equivalents at End of Year
(¥ million)



Cash Flows

(¥ million)

	2006	2007	Change	
	Amount	Amount	Amount	Change (%)
Cash flows from operating activities	13,159	8,834	(4,325)	(32.9)
Cash flows from investing activities	(6,415)	(11,803)	(5,388)	84.0
Free cash flows	6,744	(2,969)	(9,713)	(144.0)
Cash flows from financing activities	(1,420)	(2,433)	(1,013)	71.5
Cash and cash equivalents at end of year	24,437	19,091	(5,346)	(21.9)

R&D Expenses

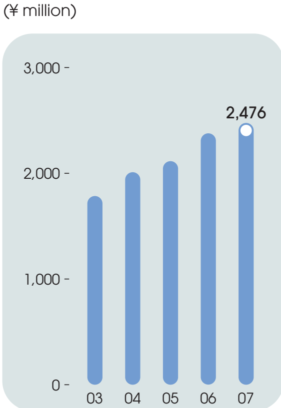
We believe that R&D underpins new product development, which is one of our core strengths.

In the fiscal year ended March 31, 2007, the Consumer Products Operation developed 35 products, not including nutritional supplements that are available only through direct sales. These products, which will help consumers to lead healthy and comfortable lives, were developed in six categories—pharmaceuticals, oral hygiene, sanitary products, deodorizing air fresheners, household sundries and food products.

In addition, the Medical Devices Operation worked aggressively to develop proprietary products.

Consequently, R&D expenses, which are included in selling, general and administrative expenses, increased ¥99 million from the previous year, to ¥2,476 million.

R&D Expenses
(¥ million)



Risk Factors

(1) Highly Competitive Business Environment

The Kobayashi Pharmaceutical Group aims to differentiate itself from rival companies by developing new products and services that satisfy customer needs. This is crucial as the Group's main products target retail consumers. However, we are susceptible to intensifying price-based competition triggered by the launch of competing products by rivals. In response, we may have to increase development costs for new products, or advertising and sales promotion expenses to stimulate demand. These and other factors could affect the Group's operating results and financial position.

(2) Highly Susceptible to Sales of New Products

The Group pursues aggressive product development activities as part of its strategy for spurring growth, launching new products every year in the spring and fall. However, delays in developing or bringing new products to market, sales of competing products, and other factors may have an impact on sales of the Group's new products, which could in turn affect the Group's operating results and financial position.

(3) Risk Concerning Inability to Reap Anticipated Benefits of Mergers or Alliances

While enhancing product lineups through M&As and business alliances, the Group is striving to expand sales regions in pursuit of a broader range of new markets both in Japan and overseas. However, these M&As and alliances are subject to uncertainties. The Group may be unable to reap the anticipated benefits of M&As and alliances or may be forced to change its business strategies, due to unforeseen post-merger or alliance events. This could affect the Group's operating results and financial position.

(4) Legal Constraints

The Group's businesses are subject to the Pharmaceutical Affairs Law as well as other relevant laws and regulations. The Medical Devices Operation is particularly susceptible to reductions in NHI reimbursement prices. These and other factors could affect the Group's operating results and financial position.

(5) Product Liability Risk

The Group's products include pharmaceuticals, quasi-pharmaceuticals, cosmetics, medical equipment and foods. Any health problems caused to consumers or patients as a result of quality defects in these products may result in large damages to the Group. This could affect the Group's operating results and financial position.

(6) Changes in Raw Material Prices

The Group's Consumer Products Operation is exposed to the risk of changes in raw material prices. Despite ongoing cost reductions, the Group's operating results and financial condition may be affected by a sharp rise in raw material prices triggered by surging crude oil prices and other factors.

(7) Impact of Inclement Weather

Sales of some of the Group's products, such as body warmers, hay fever-related products, and cold remedies, are highly susceptible to seasonal factors, such as temperatures and airborne pollen counts, which could have a large impact on sales. Trends in sales of these products could therefore affect the Group's operating results and financial position.

(8) Overseas Business Risk

The Group's trading transactions, principally the import of medical devices, are subject to fluctuations in exchange rates. However, the Group reduces their impact on operating results mainly by hedging foreign currency risk through forward exchange transactions. The Group does not engage in derivative transactions for speculative purposes. Line items denominated in foreign currencies, including the sales, expenses, assets and liabilities, of overseas subsidiaries, are converted into yen for the purpose of preparing consolidated financial statements. In the event of a large change in the prevailing exchange rate on the conversion date, there will be a substantial corresponding change in the yen value of such line items. The Group is also exposed to the risk of changes in regulations by foreign governments, as well as economic conditions. These and other factors could affect the Group's operating results and financial position.

(9) Information Management and System Risk

The Group holds large volumes of information mainly as part of its mail-order shopping businesses, including personal information. For this reason, the Group has established an internal information management system in conjunction with enhancing in-house training programs and information management. However, the Group's operating results and financial position could be affected by a loss of public trust caused by a leak of information.

(10) Intellectual Property Risk

Third-party infringement of intellectual property rights, including the Group's brands and related trademarks, may result in large damages to the Group. Furthermore, the inadvertent infringement of the intellectual property rights of a third party by the Group may also have adverse consequences. These and other factors could impact the Group's operating results and financial position.

Consolidated Financial Statements

Consolidated Balance Sheets

Kobayashi Pharmaceutical Co., Ltd. and Consolidated Subsidiaries
March 31, 2007 and 2006

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2007	2006	2007
Assets			
Current assets:			
Cash and time deposits (Note 5)	¥ 18,091	¥ 24,437	$ 153,249
Trade notes and accounts receivable (Note 6)	51,340	47,702	434,900
Securities (Note 7)	3,795	1,502	32,147
Inventories (Note 8)	19,847	17,523	168,124
Deferred income taxes (Note 15)	2,954	2,820	25,023
Other current assets	6,262	5,492	53,046
Allowance for doubtful accounts	(187)	(570)	(1,584)
Total current assets	102,102	98,906	864,905
Property, plant and equipment:			
Land (Note 9)	8,667	8,487	73,418
Buildings and structures (Note 9)	22,799	23,213	193,130
Machinery and equipment (Note 16)	4,552	4,427	38,560
Construction in progress	91	217	771
Other	5,114	5,471	43,320
	41,223	41,815	349,199
Accumulated depreciation	(18,944)	(19,027)	(160,474)
Property, plant and equipment, net	22,279	22,788	188,725
Investments and other assets:			
Investments in securities (Notes 7 and 9):			
Unconsolidated subsidiaries and affiliates	8,461	7,870	71,673
Other	9,505	7,739	80,517
Allowance for loss on devaluation of securities	(244)	(252)	(2,067)
	17,722	15,357	150,123
Deferred income taxes (Note 15)	1,767	2,292	14,968
Goodwill	11,870	2,597	100,551
Software	1,179	1,162	9,987
Other intangible assets	1,554	2,760	13,164
Other assets	7,059	7,426	59,797
Allowance for doubtful accounts	(976)	(1,343)	(8,268)
Total investments and other assets	40,175	30,251	340,322
Total assets	¥164,556	¥151,945	$1,393,952

See accompanying notes to consolidated financial statements.

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2007	2006	2007
Liabilities and Net Assets			
Current liabilities:			
Short-term loans (Note 9)	¥ 3,206	¥ 1,372	$ 27,158
Trade notes and accounts payable (Note 6)	51,261	49,188	434,231
Accrued income taxes (Note 15)	4,506	4,578	38,170
Accrued expenses	16,109	14,984	136,459
Other current liabilities	1,946	1,918	16,485
Total current liabilities	77,028	72,040	652,503
Long-term liabilities:			
Long-term debt (Note 9)	208	261	1,762
Accrued retirement benefits for employees (Note 10)	7,560	7,065	64,041
Accrued retirement benefits for directors and corporate auditors	1,400	1,358	11,859
Other liabilities	1,124	1,491	9,521
Total long-term liabilities	10,292	10,175	87,183
Total liabilities	87,320	82,215	739,686
Net Assets			
Shareholders' equity (Note 13):			
Common stock:			
Authorized – 170,100,000 shares			
Issued – 42,525,000 shares in 2007 and 2006	3,450	3,450	29,225
Capital surplus	4,207	4,192	35,637
Retained earnings	66,775	60,087	565,650
Treasury stock, at cost	(3,311)	(3,480)	(28,047)
Total shareholders' equity	71,121	64,249	602,465
Valuation and translation adjustments:			
Unrealized holding gain on securities	2,815	2,857	23,846
Unrealized gain on deferred hedges	292	–	2,474
Translation adjustments	201	(294)	1,703
Total valuation and translation adjustments	3,308	2,563	28,023
Minority interests	2,807	2,918	23,778
Total net assets	77,236	69,730	654,266
Total liabilities and net assets	¥164,556	¥151,945	$1,393,952

See accompanying notes to consolidated financial statements.

Consolidated Statements of Income

Kobayashi Pharmaceutical Co., Ltd. and Consolidated Subsidiaries
Years ended March 31, 2007 and 2006

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2007	2006	2007
Net sales (Note 18)	¥257,022	¥246,853	$2,177,230
Cost of sales	172,304	167,239	1,459,585
Gross profit	84,718	79,614	717,645
Selling, general and administrative expenses (Note 14)	66,689	62,734	564,922
Operating income (Note 18)	18,029	16,880	152,723
Other income (expenses):			
Interest and dividend income	178	156	1,508
Equity in earnings of affiliates	187	459	1,584
Interest expense	(71)	(94)	(601)
Sales discounts	(1,260)	(1,117)	(10,673)
Exchange loss	(93)	(22)	(788)
Loss on disposal or write-offs of inventories	(3,603)	(2,759)	(30,521)
Gain on sales of property, plant and equipment	1,183	53	10,021
Royalty income	540	544	4,574
Loss on disposal of property, plant and equipment	(408)	(134)	(3,456)
Loss on impairment of fixed assets (Note 16)	(124)	(1,656)	(1,050)
Gain on sales of goodwill (Note 4)	1,128	1,065	9,555
Loss on devaluation of investments in subsidiaries and affiliated companies	(405)	–	(3,431)
Other, net	757	635	6,413
Income before income taxes and minority interests	16,038	14,010	135,858
Income taxes (Note 15):			
Current	7,452	7,241	63,126
Deferred	408	(960)	3,456
	7,860	6,281	66,582
Minority interests	120	(254)	1,016
Net income	¥ 8,298	¥ 7,475	$ 70,292

See accompanying notes to consolidated financial statements.

Consolidated Statements of Changes in Net Assets

Kobayashi Pharmaceutical Co., Ltd. and Consolidated Subsidiaries
Years ended March 31, 2007 and 2006

	Number of shares issued (Thousands)	Millions of yen								
		Common stock	Capital surplus	Retained earnings	Treasury stock, at cost	Unrealized holding gain on securities	Unrealized gain on deferred hedges	Translation adjustments	Minority interests	Total net assets
Balance at March 31, 2005	42,525	¥3,450	¥4,184	¥53,585	¥(2,332)	¥1,851	¥ –	¥(622)	¥ 546	¥60,116
Net income for the year	–	–	–	7,475	–	–	–	–	–	7,475
Effect of changes in ownership interest in consolidated subsidiaries	–	–	–	498	–	–	–	–	–	498
Decrease in retained earnings resulting from inclusion of consolidated subsidiaries	–	–	–	(53)	–	–	–	–	–	(53)
Cash dividends	–	–	–	(1,374)	–	–	–	–	–	(1,374)
Bonuses to directors and corporate auditors	–	–	–	(44)	–	–	–	–	–	(44)
Purchases of treasury stock	–	–	–	–	(1,148)	–	–	–	–	(1,148)
Disposition of treasury stock	–	–	8	–	–	–	–	–	–	8
Other changes	–	–	–	–	–	1,006	–	328	2,372	1,334
Balance at March 31, 2006	42,525	3,450	4,192	60,087	(3,480)	2,857	–	(294)	2,918	69,730
Net income for the year	–	–	–	8,298	–	–	–	–	–	8,298
Cash dividends	–	–	–	(1,569)	–	–	–	–	–	(1,569)
Bonuses to directors and corporate auditors	–	–	–	(41)	–	–	–	–	–	(41)
Purchases of treasury stock	–	–	–	–	(10)	–	–	–	–	(10)
Disposition of treasury stock	–	–	15	–	179	–	–	–	–	194
Other changes	–	–	–	–	–	(42)	292	495	(111)	634
Balance at March 31, 2007	42,525	¥3,450	¥4,207	¥66,775	¥(3,311)	¥2,815	¥292	¥ 201	¥2,807	¥77,236

	Thousands of U.S. dollars (Note 1)							
	Common stock	Capital surplus	Retained earnings	Treasury stock, at cost	Unrealized holding gain on securities	Unrealized gain on deferred hedges	Translation adjustments	Minority interests	Total net assets
Balance at March 31, 2006	$29,225	$35,510	$508,996	$(29,478)	$24,202	$ –	$(2,490)	$24,718	$590,683
Net income for the year	–	–	70,292	–	–	–	–	–	70,292
Cash dividends	–	–	(13,291)	–	–	–	–	–	(13,291)
Bonuses to directors and statutory auditors	–	–	(347)	–	–	–	–	–	(347)
Purchases of treasury stock	–	–	–	(85)	–	–	–	–	(85)
Disposition of treasury stock	–	127	–	1,516	–	–	–	–	1,643
Other changes	–	–	–	–	(356)	2,474	4,193	(940)	5,371
Balance at March 31, 2007	$29,225	$35,637	$565,650	$(28,047)	$23,846	$2,474	$ 1,703	$23,778	$654,266

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

Kobayashi Pharmaceutical Co., Ltd. and Consolidated Subsidiaries
Years ended March 31, 2007 and 2006

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2007	2006	2007
Cash flows from operating activities:			
Income before income taxes and minority interests	¥ 16,038	¥14,010	$135,858
Adjustments for:			
Depreciation and amortization	3,375	3,414	28,590
Loss on impairment of fixed assets	124	1,656	1,050
Decrease in allowance for doubtful accounts	(774)	(532)	(6,557)
Increase in accrued retirement benefits	495	591	4,193
Interest and dividend income	(178)	(156)	(1,508)
Interest expense	71	94	601
Equity in earnings of affiliates	(187)	(459)	(1,584)
Loss on disposal or write-offs of inventories	3,603	2,759	30,521
Gain on sales of goodwill	(1,128)	(1,065)	(9,555)
Loss on disposal of property, plant and equipment	408	134	3,456
Allowance for loss on devaluation of securities	37	64	313
Loss on devaluation of investments in subsidiaries and affiliated companies	405	–	3,431
Changes in operating assets and liabilities:			
Decrease (increase) in trade notes and accounts receivable	333	(1,191)	2,821
Increase in inventories	(4,763)	(4,417)	(40,347)
(Decrease) increase in trade notes and accounts payable	(1,054)	3,943	(8,928)
(Decrease) increase in consumption taxes payable	(34)	240	(288)
Other	(281)	399	(2,380)
Subtotal	16,490	19,484	139,687
Interest and dividends received	178	156	1,508
Interest paid	(70)	(93)	(593)
Income taxes paid	(7,764)	(6,388)	(65,769)
Net cash provided by operating activities	8,834	13,159	74,833
Cash flows from investing activities:			
Purchases of short-term securities	(4,093)	–	(34,671)
Proceeds from redemption of short-term securities	2,800	–	23,719
Payments for purchases of property, plant and equipment	(1,478)	(1,391)	(12,520)
Proceeds from sales of property, plant and equipment	1,491	300	12,630
Payments for purchases of intangible assets	(469)	(895)	(3,973)
Increase in investments in securities	(2,021)	(6,490)	(17,120)
Proceeds from redemption of investments in securities	–	1,005	–
Increase in other assets	(1,355)	(223)	(11,478)
Decrease in short-term loans receivable	1	140	8
Proceeds from sales of goodwill	1,128	1,065	9,555
Acquisition of subsidiaries resulting in inclusion in consolidation	(9,063)	–	(76,773)
Proceeds from sale of a subsidiary's stock resulting in change in scope of consolidation	933	–	7,903
Other	323	74	2,737
Net cash used in investing activities	(11,803)	(6,415)	(99,983)
Cash flows from financing activities:			
Decrease in short-term loans, net	(556)	(931)	(4,710)
Repayment of long-term debt	(494)	(630)	(4,185)
Dividends paid	(1,569)	(1,374)	(13,291)
Increase in treasury stock	(8)	(1,219)	(68)
Proceeds from issuance of common stock to minority interests	–	2,650	–
Other	194	84	1,644
Net cash used in financing activities	(2,433)	(1,420)	(20,610)
Effect of exchange rate changes on cash and cash equivalents	56	77	474
Net (decrease) increase in cash and cash equivalents	(5,346)	5,401	(45,286)
Cash and cash equivalents at beginning of year	24,437	19,036	207,006
Cash and cash equivalents at end of year (Note 5)	¥ 19,091	¥24,437	$161,720

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Kobayashi Pharmaceutical Co., Ltd. and Consolidated Subsidiaries
Years ended March 31, 2007 and 2006

1. Basis of Presentation of Consolidated Financial Statements

Kobayashi Pharmaceutical Co., Ltd. (the "Company") and its domestic subsidiaries maintain their accounts and records in accordance with the new Corporation Law of Japan and the Securities and Exchange Law of Japan and in conformity with accounting principles generally accepted in Japan, which are different in certain respects as to the application and disclosure requirements of International Financial Reporting Standards. The Company's overseas subsidiaries maintain their accounts and records in conformity with generally accepted accounting principles prevailing in their respective countries of domicile.

The accompanying consolidated financial statements have been prepared based on the consolidated financial statements of the Company and its subsidiaries (the "Group") as required by the Securities and Exchange Law.

Effective the year ended March 31, 2007, the Company has adopted a new accounting standard for the presentation of net assets in the balance sheet and the related implementation guidance. In addition, effective the year ended March 31, 2007, the Company is required to prepare consolidated statements of changes in net assets instead of consolidated statements of shareholders' equity. In this connection, the previously reported consolidated balance sheet as of March 31, 2006 and consolidated statement of shareholders' equity for the year then ended have been restated to conform to the presentation and disclosure of the consolidated financial statements for the year ended March 31, 2007.

In preparing the accompanying consolidated financial statements, certain reclassifications have been made to the consolidated financial statements issued domestically in order to present them in a format which is more familiar to readers outside Japan. In addition, certain notes included herein are not required under accounting principles generally accepted in Japan but are presented as additional information.

Certain reclassifications of previously reported amounts have been made to conform the consolidated financial statements for the year ended March 31, 2006 to the 2007 presentation. Such reclassifications had no effect on consolidated net income or net assets.

The U.S. dollar amounts included herein are presented solely for convenience and are translated, as a matter of arithmetic computation only, at ¥118.05 = U.S.$1.00, the approximate exchange rate in effect on March 31, 2007. This translation should not be construed as a representation that Japanese yen amounts have been, could have been, or could in the future be, converted into U.S. dollars at the above or any other rate.

2. Summary of Significant Accounting Policies

(a) Principles of consolidation

The accompanying consolidated financial statements include the accounts of the Company and its significant subsidiaries. All significant intercompany transactions and accounts have been eliminated in consolidation. Investments in affiliates (companies over which the Company has the ability to exercise significant influence) are, with certain minor exceptions, accounted for by the equity method.

The difference between the cost and the underlying net equity in investments in consolidated subsidiaries and affiliates accounted for on an equity basis is allocated to identifiable assets based on their fair value at their respective dates of acquisition. Unallocated costs are deferred and amortized principally by the straight-line method over a twenty-year period. Minor differences are charged or credited to income in the year of acquisition.

The balance sheet date of certain consolidated subsidiaries is December 31. Any significant differences in intercompany accounts and transactions arising from intervening intercompany transactions during the period from January 1 through March 31 have been adjusted, if necessary.

In addition, the balance sheet date of one domestic consolidated subsidiary is September 30. For consolidation purposes, the financial statements of the subsidiary were prepared as of and for the year ended March 31, 2007.

(b) Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses for the reporting period. The actual results could differ from these estimates.

(c) Cash and cash equivalents

Cash and cash equivalents include cash on hand, deposits with banks withdrawable on demand, and short-term investments which are readily convertible to cash subject to an insignificant risk of any change in their value and which were purchased with an original maturity of three months or less.

(d) Foreign currency translation

Income and expenses denominated in foreign currencies are translated into Japanese yen at the exchange rates prevailing at the respective transaction dates. All monetary assets and liabilities denominated in foreign currencies are translated into Japanese yen at the rates of exchange in effect at the balance sheet date except for those items covered by forward foreign exchange contracts and currency options.

The balance sheet accounts of the overseas subsidiaries are translated into Japanese yen at the rates of exchange in effect at the balance sheet date except that the components of net assets excluding minority interests are translated at their historical exchange rates. Income and expense accounts are translated at the average rates of exchange in effect during the year. Differences resulting from translating the financial statements of the overseas subsidiaries have not been included in the determination of net income, but are presented as "Translation adjustments" in the consolidated balance sheets.

(e) Investments in securities

Securities are classified into three categories: trading securities, held-to-maturity debt securities, or other securities. Trading securities, consisting of debt and marketable equity securities, are stated at fair value. Gain or loss, both realized and unrealized, is charged to income. Held-to-maturity debt securities are stated at amortized cost. Marketable securities classified as other securities are carried at fair value with any changes in unrealized holding gain or loss, net of the applicable income taxes, reported as a separate component of net assets. Non-marketable securities classified as other securities are carried at cost.

If the fair value of other securities has declined significantly and the impairment in value is not deemed temporary, these securities are written down to fair value and the resulting loss is charged to income as incurred.

(f) Inventories

Commodities and raw materials are stated principally at cost determined by the moving average method. Finished goods, work in process and supplies are principally stated at cost determined by the total average method.

(g) Property, plant and equipment

Property, plant and equipment are stated at cost. The Company and its domestic subsidiaries calculate depreciation by the declining-balance method except for buildings (other than structures attached to the buildings) acquired after March 31, 1998, to which the straight-line method is applied. The overseas subsidiaries calculate depreciation by the straight-line method.

(h) Allowance for doubtful accounts

The Company and its domestic subsidiaries provide for doubtful accounts principally at an amount based on their historical bad debt ratio. In addition, an additional allowance is provided at an estimate of uncollectible amounts from certain specific doubtful receivables.

(i) Reserve for sales returns

The Company and certain domestic subsidiaries provide a reserve for sales returns based on the historical sales return ratio. The reserve for sales returns is included in "Other current liabilities."

(j) Accrued retirement benefits

The Company and certain domestic consolidated subsidiaries has an unfunded defined retirement benefit plan and a non-contributory funded pension plan. All other domestic consolidated subsidiaries have unfunded defined retirement benefit plans for their employees. The unfunded defined retirement benefit plans provide for lump-sum payments to eligible employees who terminate their services which are determined by reference to their current rate of pay, length of service and the conditions under which termination occurs.

Accrued retirement benefits for employees of the Company and certain domestic consolidated subsidiaries represent the estimated present value of the projected benefit obligation in excess of the fair value of the pension plan assets.

All other domestic consolidated subsidiaries have adopted a simplified method of calculation. Under this simplified method, accrued retirement benefits for employees are stated at 100% of the amount which would be required to be paid if all eligible employees voluntarily retired at the balance sheet date.

Prior service cost is being amortized by the straight-line method over ten years which is a shorter period than the average remaining years of service of the participants.

Actuarial differences are amortized in the year following the year in which differences are recognized by the straight-line method over ten years which is a shorter period than the average remaining years of service of the participants.

Directors and corporate auditors ("officers") are customarily entitled, subject to shareholders' approval, to lump-sum payments under the unfunded retirement allowances plan. The provision for retirement allowances for these officers has been made at an estimated amount based on the Company's and consolidated subsidiaries' internal regulations.

(k) Allowance for loss on devaluation of securities

An allowance for loss on devaluation of securities is provided to cover possible future losses on investments in securities at a level determined by considering the financial position of the individual unconsolidated subsidiaries.

(l) Income taxes

Accrued income taxes are provided at the amount currently payable.

The Company and its consolidated subsidiaries have adopted interperiod income tax allocation by the asset and liability method. Deferred tax assets and liabilities are recognized for the expected tax consequences attributable to the temporary differences between the tax bases of the assets and liabilities and the amounts reported in the consolidated financial statements.

(m) Leases

The Company and its subsidiaries lease offices and other facilities. Finance leases, except for those which transfer the legal title of the underlying property from the lessor to the lessee at the end of the lease term, are accounted for as operating leases.

(n) Research and development costs and computer software

Research and development costs are charged to income when incurred.

Expenditures relating to computer software developed for internal use are charged to income when incurred, except if they contribute to the generation of income or to future cost savings. Such expenditures are capitalized as assets and are amortized over their estimated useful lives, customarily 5 years.

(o) Appropriation of retained earnings

Under the new Corporation Law of Japan, appropriations of retained earnings with respect to a given financial period can be made by resolution of the Board of Directors at a meeting held subsequent to the close of the financial period. The accounts for that period do not, therefore, reflect such appropriations (see Note 21).

(p) Derivatives and hedging activities

Derivative financial instruments, which include forward foreign exchange contracts and currency options, are used to offset the Group's risk of exposure to fluctuation in currency exchange rates.

Derivatives are carried at fair value with any changes in unrealized gain or loss credited or charged to income, except for those which meet the criteria for deferral hedge accounting under which unrealized gain or loss is deferred as net assets. When a forward foreign exchange contract meets certain criteria, receivables and payables covered by the contract are translated at the contracted rates.

The Company evaluates the effectiveness of its hedging activities by reference to the accumulated gain or loss on each hedging instrument and on the related underlying hedged item from the commencement of the hedge.

3. Changes in Accounting Policies

(a) Presentation of net assets in the balance sheet

Effective the year ended March 31, 2007, the Company has adopted "Accounting Standard for Presentation of Net Assets in the Balance Sheet" (Accounting Standards Board of Japan (ASBJ) Statement No. 5 issued on December 9, 2005) and "Guidance on Accounting Standard for Presentation of Net Assets in the Balance Sheet" (ASBJ Guidance No. 8 issued on December 9, 2005).

As a result of the adoption of this new accounting standard and the related guidance, there was no impact on the Company's operating results for the year ended March 31, 2007.

(b) Practical solution on unification of accounting policies applied to foreign subsidiaries for consolidated financial statements

Effective the year ended March 31, 2007, the Company has adopted "Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries for Consolidated Financial Statements" (ASBJ Practical Solution No. 18 issued on May 17, 2006). As a result of the adoption of this practical solution, operating income and income before income taxes and minority interests decreased by ¥31 million ($263 thousand) from the amounts which would have been recorded under the previous method.

(c) Accounting standards for business combinations

Effective the year ended March 31, 2007, the Company has adopted "Accounting Standard for Business Combinations," (issued on October 31, 2003 by the Business Accounting Council of Japan), and "Accounting Standard for Business Divestitures" and "Guidance on Accounting Standard for Business Combinations and Accounting Standard for Business Divestitures" (Accounting Standards Board of Japan (ASBJ) Statement No. 7 and ASBJ Guidance No. 10, respectively, both of which were issued on December 27, 2005).

(d) Impairment of fixed assets

Effective the year ended March 31, 2006, the Company and its domestic consolidated subsidiaries adopted an accounting standard for the impairment of fixed assets which requires that tangible and intangible fixed assets be carried at cost less depreciation, and be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Companies are required to recognize an impairment loss in their statement of income if certain indicators of asset impairment exist and if the book value of an asset exceeds the undiscounted sum of its future cash flows. The standard states that impairment losses are to be measured as the excess of the book value over the higher of (1) the fair market value of the asset, net of disposition costs, and (2) the present value of future cash flows arising from ongoing utilization of the asset and from its disposal after use. The standard covers land, factories, buildings, other forms of property, plant and equipment, and leased assets as well as intangible assets.

As a result of the adoption of this accounting standard, a loss on impairment of fixed assets including leased assets in the amount of ¥1,619 million was recognized and income before income taxes and minority interests decreased by the same amount for the year ended March 31, 2006 from the corresponding amount which would have been recorded under the previous method.

4. Termination of a Joint Business

Revenue from sale of distribution rights:

In March 2002, the Company and Medtronic Sofamor Danek Inc. terminated their joint business in Japan. As a consequence, the Company has received and will receive in installments the proceeds from the sale of distribution rights in Japan. This revenue has been and will be recorded in the Company's books of account on a cash basis as follows:

	Thousands of U.S. dollars
In April 2007	$11,000
In April 2008	11,000

5. Cash and Cash Equivalents

A reconciliation of cash and time deposits in the consolidated balance sheets to cash and cash equivalents in the consolidated statements of cash flows at March 31, 2007 and 2006 is summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Cash and time deposits	¥18,091	¥24,437	$153,249
Short-term investments whose redemption dates are within three months of the dates of acquisition, included in "Securities"	1,000	–	8,471
Cash and cash equivalents	¥19,091	¥24,437	$161,720

6. Notes Receivable and Notes Payable

Although the balance sheet date for the year ended March 31, 2007 fell on a bank holiday, notes receivable, trade of ¥1,229 million ($10,411 thousand) and notes payable, trade of ¥1,604 million ($13,587 thousand) with due dates of March 31, 2007 were excluded in the respective balances and were settled on the next business day.

7. Securities and Investments in Securities

Securities classified as "other securities" at March 31, 2007 and 2006 are summarized as follows:

(a) Securities whose carrying value exceeds their acquisition cost

	Millions of yen					
	2007			2006		
	Acquisition cost	Carrying value	Unrealized gain	Acquisition cost	Carrying value	Unrealized gain
Equities	¥ 734	¥5,470	¥4,736	¥ 788	¥5,460	¥4,672
Debt securities	599	599	0	501	501	0
	¥1,333	¥6,069	¥4,736	¥1,289	¥5,961	¥4,672

	Thousands of U.S. dollars		
	2007		
	Acquisition cost	Carrying value	Unrealized gain
Equities	$ 6,218	$46,336	$40,118
Debt securities	5,074	5,074	0
	$11,292	$51,410	$40,118

(b) Securities whose acquisition cost exceeds their carrying value

	Millions of yen					
	2007			2006		
	Acquisition cost	Carrying value	Unrealized loss	Acquisition cost	Carrying value	Unrealized loss
Equities	¥ 760	¥ 652	¥(108)	¥ 190	¥ 185	¥ (5)
Debt securities	5,197	5,189	(8)	2,505	2,493	(12)
	¥5,957	¥5,841	¥(116)	¥2,695	¥2,678	¥(17)

	Thousands of U.S. dollars		
	2007		
	Acquisition cost	Carrying value	Unrealized loss
Equities	$ 6,438	$ 5,523	$(915)
Debt securities	44,024	43,956	(68)
	$50,462	$49,479	$(983)

(c) Securities whose market value is not determinable

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Unlisted stock other than those traded on the over-the-counter market	¥1,390	¥316	$11,775
Investment trusts	–	286	–

(d) Redemption schedule for other securities with maturities

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Due within one year	¥3,795	¥1,502	$32,147
Due after one year but within five years	1,993	1,491	16,883
	¥5,788	¥2,993	$49,030

(e) Proceeds from sales of, and gross realized gain on, other securities

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Proceeds from sales	¥10	0	$85
Gross realized gain	2	0	17

8. Inventories

Inventories at March 31, 2007 and 2006 are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Commodities	¥ 9,828	¥ 9,607	$ 83,253
Finished goods	7,908	5,875	66,989
Raw materials, work in process and supplies	2,111	2,041	17,882
	¥19,847	¥17,523	$168,124

9. Short-Term Loans and Long-Term Debt

The average interest rates on short-term bank loans at March 31, 2007 and 2006 were 1.77% and 2.95%, respectively.

Long-term debt at March 31, 2007 and 2006 is summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Loans from banks with average interest rates of 1.04% for 2007 and 1.49% for 2006	¥ 309	¥342	$2,618
Less amounts due within one year	(101)	(81)	(856)
	¥ 208	¥261	$1,762

The aggregate annual maturities of long-term debt subsequent to March 31, 2007 are summarized as follows:

Year ending March 31,	Millions of yen	Thousands of U.S. dollars
2008	¥101	$ 856
2009	147	1,245
2010	50	424
2011	11	93
	¥309	$2,618

Assets pledged as collateral at March 31, 2007 are summarized as follows:

	Millions of yen	Thousands of U.S. dollars
Land	¥2,122	$17,975
Buildings and structures	989	8,378
Investments in securities	171	1,449
	¥3,282	$27,802

Secured liabilities at March 31, 2007 are summarized as follows:

	Millions of yen	Thousands of U.S. dollars
Trade notes and accounts payable	¥8,583	$72,707
Short-term loans	350	2,965
Long-term loans	18	152
	¥8,951	$75,824

In order to achieve more efficient and flexible financing, the Company and its consolidated subsidiaries have concluded line-of-credit agreements with certain financial institutions. The status of these at March 31, 2007 is summarized as follows:

	Millions of yen	Thousands of U.S. dollars
Lines of credit	¥19,752	$167,319
Credit used	720	6,099
Available credit	¥19,032	$161,220

10. Accrued Retirement Benefits for Employees

The following table sets forth the funded and accrued status of the plans, and the amounts recognized in the consolidated balance sheets at March 31, 2007 and 2006 for the Group's defined benefit plans:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Projected benefit obligation	¥(13,819)	¥(12,550)	$(117,060)
Fair value of pension plan assets	5,984	5,282	50,690
Unfunded retirement benefit obligation	(7,835)	(7,268)	(66,370)
Unrecognized prior service cost	620	726	5,252
Unrecognized actuarial differences	656	283	5,557
Net retirement benefit obligation	(6,559)	(6,259)	(55,561)
Prepaid pension cost	(1,001)	(806)	(8,480)
Accrued retirement benefits for employees	¥ (7,560)	¥ (7,065)	$ (64,041)

The components of net pension cost for the years ended March 31, 2007 and 2006 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Service cost	¥ 806	¥ 864	$6,828
Interest cost	236	224	1,999
Expected return on pension plan assets	(106)	(75)	(898)
Amortization:			
Prior service cost	103	103	872
Actuarial differences	76	438	644
Net pension cost	¥1,115	¥1,554	$9,445

The assumptions used in accounting for the above plans for the years ended March 31, 2007 and 2006 were as follows:

	2007	2006
Discount rate	2.0%	2.0%
Expected rate of return on plan assets	2.0%	2.0%

11. Leases

The following *pro forma* amounts represent the acquisition cost and the related accumulated depreciation of property and accumulated loss on impairment of property leased to the Group at March 31, 2007 and 2006, which would have been reflected in the consolidated balance sheets if finance leases other than those which transfer the ownership of the leased property (currently accounted for as operating leases) were capitalized:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Machinery and equipment:			
Acquisition cost	¥ 8,587	¥ 8,197	$ 72,740
Accumulated depreciation	(5,188)	(4,873)	(43,947)
Accumulated loss on impairment of leased property	(212)	(152)	(1,796)
	3,187	3,172	26,997
Furniture and fixtures:			
Acquisition cost	2,212	2,441	18,738
Accumulated depreciation	(1,297)	(1,412)	(10,987)
	915	1,029	7,751
Others:			
Acquisition cost	3,397	2,617	28,776
Accumulated depreciation	(2,646)	(2,122)	(22,414)
	751	495	6,362
Total	¥ 4,853	¥ 4,696	$ 41,110

Future minimum lease payments (including the interest portion thereon) subsequent to March 31, 2007 for finance leases other than those which transfer ownership of the leased property to the lessees are summarized as follows:

Year ending March 31,	Millions of yen	Thousands of U.S. dollars
2008	¥1,678	$14,214
2009 and thereafter	3,381	28,641
Total	¥5,059	$42,855

The amounts of allowance for loss on impairment of leased property at March 31, 2007 and 2006 were ¥131 million ($1,110 thousand) and ¥115 million, respectively.

Future minimum lease payments subsequent to March 31, 2007 for non-cancelable operating leases were as follows:

Year ending March 31,	Millions of yen	Thousands of U.S. dollars
2008	¥ 50	$ 424
2009 and thereafter	137	1,160
Total	¥187	$1,584

Lease payments related to finance leases accounted for as operating leases and depreciation and interest expense, which have not been reflected in the consolidated statements of income for the years ended March 31, 2007 and 2006, are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Lease expenses	¥2,281	¥2,311	$19,322
Reversal of allowance for loss on impairment of leased property	60	36	508
Estimated depreciation expense	2,111	2,104	17,882
Estimated interest expense	99	83	839
Loss on impairment of leased property	87	152	737

12. Derivatives and Hedging Activities

The Company utilizes forward foreign exchange contracts and currency options to reduce the risk of fluctuation in foreign exchange rates. The Company has established a control environment which includes policies and procedures for risk assessment and for the approval, reporting and monitoring of transactions involving derivatives. The Company does not hold or issue derivatives for speculative trading purposes.

The forward foreign exchange contracts outstanding as of March 31, 2007 are summarized as follows:

	Millions of yen			
	2007			
	Notional amount			
	Total	Amount maturing after more than one year	Fair value	Valuation gain
Buy Euro	¥60	–	¥65	¥5
	¥60	–	¥65	¥5

	Thousands of U.S. dollars			
	2007			
	Notional amount			
	Total	Amount maturing after more than one year	Fair value	Valuation gain
Buy Euro	$508	–	$551	$43
	$508	–	$551	$43

There were no open derivatives positions at March 31, 2006.

13. Shareholders' Equity

The new Corporation Law of Japan (the "Law"), which superseded most of the provisions of the Commercial Code of Japan (the "Code"), went into effect on May 1, 2006. The Law provides that an amount equal to 10% of the amount to be disbursed as distributions of capital surplus (other than the capital reserve) and retained earnings (other than the legal reserve) be transferred to the capital reserve and the legal reserve, respectively, until the sum of the capital reserve and the legal reserve equals 25% of the capital stock account. Such distributions can be made at any time by resolution of the shareholders, or by the Board of Directors if certain conditions are met.

Retained earnings include the legal reserve provided in accordance with the provisions of the Law. The legal reserve of the Company included in retained earnings amounted to ¥340 million ($2,880 thousand) at March 31, 2007 and 2006.

Stock-based compensation plan

In accordance with the Code, a stock option plan for directors and certain employees of the Company and one consolidated subsidiary and corporate auditors of the Company was approved at the annual general meeting of the shareholders held on June 27, 2003.

The stock option plan referred to above is summarized as follows:

		Yen	
Date of approval	Number of stock options outstanding at March 31, 2007	Exercise price at March 31, 2007	Exercisable period
June 27, 2003	178,200	3,051	From July 1, 2005 up to and including June 30, 2008

Treasury stock

Movements in treasury stock for the year ended March 31, 2007 are summarized as follows:

	Number of shares			
	2007			
	March 31, 2006	Increase	Decrease	March 31, 2007
Treasury stock	1,234,262	2,044	63,800	1,172,506

14. Selling, General and Administrative Expenses

The major components of selling, general and administrative expenses for the years ended March 31, 2007 and 2006 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Sales promotional activities	¥ 5,720	¥ 5,289	$ 48,454
Freight and storage	10,976	9,928	92,978
Advertising	13,129	12,371	111,216
Salaries and bonuses	13,115	12,887	111,097
Office rent and other rental charges	3,102	3,110	26,277
External services	4,612	4,012	39,068
Research and development costs	2,476	2,378	20,974

15. Income Taxes

The Company and its domestic subsidiaries are subject to several taxes based on income which, in the aggregate, resulted in a statutory tax rate of approximately 40.6% for the years ended March 31, 2007 and 2006. The overseas subsidiaries are subject to the income taxes of their respective countries of domicile.

A reconciliation of the differences between the statutory tax rate and the effective tax rates in the accompanying consolidated statements of income is as follows:

	2007	2006
Statutory tax rate	40.6%	40.6%
Tax loss carryforwards of consolidated subsidiaries	4.1	2.7
Valuation allowances	5.0	1.8
Utilization of tax loss carryforwards	(2.6)	(1.5)
Tax credits on research and development costs	(1.3)	(2.0)
Amortization of excess of cost over net assets acquired	2.0	1.7
Expenses not deductible for tax purposes	1.1	1.4
Equity in earnings of affiliates	(0.1)	(0.9)
Other	0.2	1.0
Effective tax rates	49.0%	44.8%

The tax effects of the temporary differences which gave rise to a significant portion of the deferred tax assets and liabilities at March 31, 2007 and 2006 are presented below:

	Millions of yen		Thousands of U.S. dollars
	2007	2006	2007
Deferred tax assets:			
Accrued retirement benefits for employees	¥ 2,608	¥ 2,451	$ 22,092
Net operating loss carryforwards	2,569	2,359	21,762
Reserve for employees' bonuses	799	816	6,768
Accrued retirement benefits for directors and statutory auditors	568	575	4,812
Allowance for doubtful accounts	74	201	627
Accrued expenses	737	736	6,243
Accrued enterprise tax	358	379	3,033
Unrealized intercompany profits	369	409	3,126
Loss on impairment of fixed assets	664	656	5,625
Loss on disposal or write-offs of inventories	436	–	3,693
Other	886	973	7,505
Gross deferred tax assets	10,068	9,555	85,286
Valuation allowance	(3,679)	(2,583)	(31,165)
Total deferred tax assets	6,389	6,972	54,121
Deferred tax liabilities:			
Unrealized holding gain on securities	(1,641)	(1,889)	(13,901)
Other	(77)	–	(652)
Total deferred tax liabilities	(1,718)	(1,889)	(14,553)
Net deferred tax assets	¥ 4,671	¥ 5,083	$ 39,568

16. Loss on Impairment of Fixed Assets

The Company and its domestic consolidated subsidiaries group their fixed assets for business use at each business segment unit and these are defined as the smallest identifiable group of assets generating cash inflows. The head office building, delivery centers and other are grouped as one common asset group.

For the year ended March 31, 2007, the carrying value of leased property and that of production facilities which are not anticipated to be utilized in the future, have been reduced to their respective recoverable amounts and a loss on impairment of fixed assets was recognized in the accompanying consolidated statement of income for the year then ended. The recoverable amounts of production facilities are measured based on value in use (the present value of future cash flows or their estimated selling price).

Loss on impairment of fixed assets for the years ended March 31, 2007 and 2006 are summarized as follows:

			Millions of yen	Thousands of U.S. dollars
Place	Description	Classification	2007	2007
Osaka and other	Production facilities	Machinery and equipment and other	¥ 37	$ 313
Osaka and other	Production facilities	Leased property (currently accounted for as operating leases)	87	737
			¥124	$1,050

Place	Description	Classification	Millions of yen 2006
Osaka and other	Production facilities	Machinery and equipment and other	¥ 67
Osaka and other	Production facilities	Leased property (currently accounted for as operating leases)	151
Osaka	Leasing	Land	1,076
Miyagi	Idle assets	Land	362
			¥1,656

17. Supplementary Cash Flow Information

In April 2006, the Company purchased shares of KS Touhoku Co., Ltd. and initially consolidated the accounts of KS Touhoku Co., Ltd. as of and for the year ended March 31, 2007. The assets and liabilities included in consolidation are summarized as follows:

	Millions of yen	Thousands of U.S. dollars
	2007	2007
Current assets	¥4,478	$37,933
Long-term assets	967	8,192
Total assets	¥5,445	$46,125
Current liabilities	¥5,222	$44,235
Long-term liabilities	418	3,541
Total liabilities	¥5,640	$47,776

In November 2006, the Company purchased shares of HEATMAX Inc. and initially consolidated the accounts of HEATMAX Inc. and its consolidated subsidiaries as of and for the year ended March 31, 2007. The assets and liabilities included in consolidation are summarized as follows:

	Millions of yen	Thousands of U.S. dollars
	2007	2007
Current assets	¥1,601	$13,562
Long-term assets	7,816	66,209
Total assets	¥9,417	$79,771
Current liabilities	¥ 495	$ 4,193
Long-term liabilities	10	85
Total liabilities	¥ 505	$ 4,278

In November 2006, the Company purchased shares of eVent Medical Ltd. and initially consolidated the accounts of eVent Medical Ltd. and its consolidated subsidiaries as of and for the year ended March 31, 2007. The assets and liabilities included in consolidation are summarized as follows:

	Millions of yen	Thousands of U.S. dollars
	2007	2007
Current assets	¥101	$ 856
Long-term assets	70	593
Total assets	¥171	$1,449
Current liabilities	¥791	$6,701
Long-term liabilities	–	–
Total liabilities	¥791	$6,701

In November 2006, the Company sold shares of Shield California Healthcare Centers Inc. and excluded the accounts of Shield California Healthcare Centers Inc. and its consolidated subsidiaries from consolidation as of and for the year ended March 31, 2007. The assets and liabilities excluded from consolidation are summarized as follows:

	Millions of yen	Thousands of U.S. dollars
	2007	2007
Current assets	¥2,795	$23,677
Long-term assets	909	7,700
Total assets	¥3,704	$31,377
Current liabilities	¥ 598	$ 5,066
Long-term liabilities	312	2,643
Total liabilities	¥ 910	$ 7,709

18. Segment Information

The Company and its consolidated subsidiaries are engaged primarily in the manufacture and sale of products and wholesale operations principally in Japan.

The business segment information of the Company and its consolidated subsidiaries for the years ended March 31, 2007 and 2006 is outlined as follows:

	Millions of yen						
	2007						
	Consumer Products Operation	Wholesale Operation	Medical Devices Operation	Other Operations	Total	Eliminations or unallocable accounts	Consolidated
I. Sales and operating income							
Sales to third parties	¥ 71,717	¥164,839	¥16,496	¥ 3,970	¥257,022	¥ –	¥257,022
Inter-group sales and transfers	30,786	1	–	9,143	39,930	(39,930)	–
Net sales	102,503	164,840	16,496	13,113	296,952	(39,930)	257,022
Operating expenses	85,943	164,516	15,935	12,722	279,116	(40,123)	238,993
Operating income	¥ 16,560	¥ 324	¥ 561	¥ 391	¥ 17,836	¥ 193	¥ 18,029
II. Total assets, depreciation, loss on impairment of fixed assets and capital expenditures							
Total assets	¥ 66,653	¥ 57,975	¥14,674	¥ 7,998	¥147,300	¥ 17,256	¥164,556
Depreciation	2,540	247	330	168	3,285	90	3,375
Loss on impairment of fixed assets	37	–	–	–	37	–	37
Capital expenditures	1,646	310	76	125	2,157	72	2,229

	Millions of yen						
	2006						
	Consumer Products Operation	Wholesale Operation	Medical Devices Operation	Other Operations	Total	Eliminations or unallocable accounts	Consolidated
I. Sales and operating income							
Sales to third parties	¥68,869	¥156,934	¥17,127	¥ 3,923	¥246,853	¥ –	¥246,853
Inter-group sales and transfers	25,908	1	–	9,053	34,962	(34,962)	–
Net sales	94,777	156,935	17,127	12,976	281,815	(34,962)	246,853
Operating expenses	79,330	156,499	16,544	12,574	264,947	(34,974)	229,973
Operating income	¥15,447	¥ 436	¥ 583	¥ 402	¥ 16,868	¥ 12	¥ 16,880
II. Total assets, depreciation, loss on impairment of fixed assets and capital expenditures							
Total assets	¥59,095	¥ 51,954	¥ 9,878	¥ 7,728	¥128,655	¥ 23,290	¥151,945
Depreciation	2,024	196	325	172	2,717	97	2,814
Loss on impairment of fixed assets	580	–	–	–	580	1,076	1,656
Capital expenditures	1,915	261	262	110	2,548	249	2,797

	Thousands of U.S. dollars						
	2007						
	Consumer Products Operation	Wholesale Operation	Medical Devices Operation	Other Operations	Total	Eliminations or unallocable accounts	Consolidated
I. Sales and operating income							
Sales to third parties	$607,514	$1,396,349	$139,737	$ 33,630	$2,177,230	$ –	$2,177,230
Inter-group sales and transfers	260,788	8	–	77,450	338,246	(338,246)	–
Net sales	868,302	1,396,357	139,737	111,080	2,515,476	(338,246)	2,177,230
Operating expenses	728,022	1,393,613	134,985	107,768	2,364,388	(339,881)	2,024,507
Operating income	$140,280	$ 2,744	$ 4,752	$ 3,312	$ 151,088	$ 1,635	$ 152,723
II. Total assets, depreciation, loss on impairment of fixed assets and capital expenditures							
Total assets	$564,617	$ 491,105	$124,303	$ 67,751	$1,247,776	$ 146,176	$1,393,952
Depreciation	21,516	2,092	2,795	1,425	27,828	762	28,590
Loss on impairment of fixed assets	313	–	–	–	313	–	313
Capital expenditures	13,943	2,626	644	1,059	18,272	610	18,882

Geographic Segment Information

The geographic segment information of the Company and its consolidated subsidiaries for the year ended March 31, 2007 is outlined as follows:

	Millions of yen						
	2007						
	Japan	North America	Europe	Asia	Total	Eliminations and unallocable accounts	Consolidated
I. Sales and operating income (loss)							
Sales to third parties	¥246,428	¥ 8,333	¥ 731	¥1,530	¥257,022	¥ –	¥257,022
Inter-group sales and transfers	376	42	0	738	1,156	(1,156)	–
Net sales	246,804	8,375	731	2,268	258,178	(1,156)	257,022
Operating expenses	228,009	8,434	1,138	2,599	240,180	(1,187)	238,993
Operating income (loss)	¥ 18,795	¥ (59)	¥ (407)	¥ (331)	¥ 17,998	¥ 31	¥ 18,029
II. Total assets							
Total assets	¥112,848	¥16,786	¥ 608	¥1,839	¥132,081	¥32,475	¥164,556

	Thousands of U.S. dollars						
	2007						
	Japan	North America	Europe	Asia	Total	Eliminations	Consolidated
I. Sales and operating income (loss)							
Sales to third parties	$2,087,488	$ 70,589	$ 6,192	$12,961	$2,177,230	$ –	$2,177,230
Inter-group sales and transfers	3,185	356	0	6,251	9,792	(9,792)	–
Total sales	2,090,673	70,945	6,192	19,212	2,187,022	(9,792)	2,177,230
Operating expenses	1,931,461	71,445	9,640	22,016	2,034,562	(10,055)	2,024,507
Operating income (loss)	$ 159,212	$ (500)	$(3,448)	$ (2,804)	$ 152,460	$ 263	$ 152,723
II. Total assets							
Total assets	$ 955,934	$142,194	$ 5,150	$15,578	$1,118,856	$275,096	$1,393,952

Geographic segment information for the year ended March 31, 2006 has been omitted because more than 90% of total consolidated sales were recorded in Japan and more than 90% of total assets were located in Japan.

Overseas Sales Information

Overseas sales information has been omitted because overseas sales, consisting of export sales of the Company and its domestic consolidated subsidiaries and sales (other than exports to Japan) of overseas consolidated subsidiaries constituted less than 10% of total consolidated sales.

19. Amounts per Share

	Yen		U.S. dollars
	2007	2006	2007
Net income:			
Basic	¥ 200.77	¥ 179.17	$ 1.70
Diluted	200.47	179.01	1.70
Cash dividends	50.00	38.00	0.42
Net assets	1,799.87	1,617.10	15.25

Basic net income per share has been computed based on the net income available for distribution to shareholders of common stock and the weighted-average number of shares of common stock outstanding during the year. Diluted net income per share has been computed based on the net income available for distribution to the shareholders of common stock and the weighted-average number of shares of common stock outstanding during the year after giving effect to the dilutive potential of the shares of common stock issuable upon the exercise of stock options issued by the Company. The amounts per share of net assets have been computed based on the net assets available for distribution to the shareholders of common stock and the number of shares of common stock outstanding at the year end.

Cash dividends per share represent the cash dividends proposed by the Board of Directors as applicable to the respective years together with the interim cash dividends paid.

20. Acquisitions

On November 3, 2006, the Company acquired all of the outstanding shares of common stock of eVent Medical Ltd. ("eVent"). The eVent Group consists of eVent, eMed Ltd., and eVent Medical Inc. eVent produces and provides medical equipment. The Company determined that the acquisition would provide it with production technology regarding medical equipment and enable it to maintain its global market share. The aggregate purchase price was ¥1,276 million ($10,809 thousand), which consisted of ¥1,167 million ($9,886 thousand) for purchases of shares of common stock and ¥109 million ($923 thousand) of transaction costs. The acquisition was accounted for using the purchase method of accounting. Goodwill arising from the acquisition is being amortized over seven to ten years using the straight-line method.

The accompanying consolidated statement of income for the year ended March 31, 2007 reflected the operating results of eVent for the period from November 4, 2006 to December 31, 2006. The amounts of assets acquired and liabilities assumed of eVent at the date of acquisition were as follows:

	Millions of yen	Thousands of U.S. dollars
Current assets	¥101	$ 856
Fixed assets	70	593
Current liabilities	791	6,701

The following unaudited pro forma information presents a summary of the results of operations of eVent as if the acquisition had occurred on January 1, 2006 and includes the related adjustment for the amortization of goodwill:

	Millions of yen	Thousands of U.S. dollars
Net sales	¥ 425	$ 3,600
Operating loss	(473)	(4,007)
Loss before income taxes and minority interests	(426)	(3,609)
Net loss	¥(426)	$(3,609)

On November 30, 2006, the Company acquired all of the outstanding shares of common stock of HEATMAX Inc. ("HEATMAX"). The HEATMAX Group consists of HEATMAX, MEDHEAT Inc., and THERMOMAX Inc. HEATMAX produces and provides body warmers, cura heat and other products. The Company determined that the acquisition would expand its market share in North America. The aggregate purchase price was ¥9,144 million ($77,458 thousand), which consisted of ¥9,020 million ($76,408 thousand) for purchases of shares of common stock and ¥124 million ($1,050 thousand) of transaction costs. The acquisition was accounted for using the purchase method of accounting. Goodwill arising from the acquisition is being amortized over four to twenty years using straight-line method.

The accompanying consolidated statement of income for the year ended March 31, 2007 reflected the operating results of HEATMAX for the period from December 1, 2006 to December 31, 2006. The amounts of the assets acquired and liabilities assumed of HEATMAX at the date of acquisition were as follows:

	Millions of yen	Thousands of U.S. dollars
Current assets	¥1,601	$13,562
Fixed assets	7,816	66,209
Current liabilities	495	4,193
Long-term liabilities	10	85

The following unaudited pro forma information presents a summary of the results of operations of HEATMAX as if the acquisition had occurred on January 1, 2006 and includes the related adjustment for the amortization of goodwill.

	Millions of yen	Thousands of U.S. dollars
Net sales	¥2,481	$21,017
Operating income	5	42
Loss before income taxes and minority interests	(14)	(119)
Net loss	¥ (8)	$ (68)

21. Subsequent Event

The following appropriation of retained earnings of the Company, which has not been reflected in the consolidated financial statements for the year ended March 31, 2007, was approved at a meeting of the Board of Directors held on May 28, 2007:

	Millions of yen	Thousands of U.S. dollars
Cash dividends (¥50.00 = $0.42 per share)	¥2,067	$17,510

Report of Independent Auditors

ERNST & YOUNG SHINNIHON

■ **Certified Public Accountants**
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The Board of Directors
Kobayashi Pharmaceutical Co., Ltd.

We have audited the accompanying consolidated balance sheets of Kobayashi Pharmaceutical Co., Ltd. and consolidated subsidiaries as of March 31, 2007 and 2006, and the related consolidated statements of income, changes in net assets, and cash flows for the years then ended, all expressed in Japanese 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.

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 Kobayashi Pharmaceutical Co., Ltd. and consolidated subsidiaries at March 31, 2007 and 2006, and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in Japan.

Supplemental Information

As described in Note 3 (d), effective April 1, 2005, the Company and its domestic consolidated subsidiaries adopted an accounting standard for the impairment of fixed assets.

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 1.

June 28, 2007

Ernst & Young ShinNihon

Six-year Consolidated Financial Summary

Kobayashi Pharmaceutical Co., Ltd. and Consolidated Subsidiaries
Years ended March 31

	Millions of yen					
	2007	2006	2005	2004	2003	2002
For the Year						
Net Sales	¥257,022	¥246,853	¥215,708	¥211,670	¥210,922	¥204,647
Cost of Sales (after provisions for returned products)	172,304	167,239	143,912	141,388	141,675	139,404
Gross Profit (after provisions for returned products)	84,718	79,614	71,796	70,282	69,247	65,243
Selling, General and Administrative Expenses	66,689	62,734	56,097	54,159	53,394	51,613
Operating Income	18,029	16,880	15,699	16,123	15,853	13,630
Income before Income Taxes and Minority Interests	16,038	14,010	12,770	11,825	12,840	10,924
Net Income	8,298	7,475	6,731	6,677	6,606	6,595
Per Share Data (Yen)						
Net Income	200.77	179.17	160.64	157.25	231.25	232.64
Cash Dividends	50	38	33	21	21	18.5
Cash Flows from Operating Activities	8,834	13,159	8,364	6,971	12,046	4,039
Free Cash Flows	(2,969)	6,744	4,428	4,613	11,770	(2,892)
Depreciation and Amortization Expenses	3,375	3,414	3,239	3,350	3,480	2,598
Capital Expenditures*1	2,229	2,797	5,021	2,441	2,631	4,329
R&D Expenses	2,476	2,378	2,115	2,010	1,785	1,778
At Year-end						
Current Assets	102,102	98,906	86,705	80,031	77,315	72,759
Property, Plant and Equipment, Net	22,279	22,788	25,003	24,567	27,758	28,301
Current Liabilities	77,028	72,040	65,007	64,298	65,926	62,645
Long-term Liabilities	10,292	10,175	8,960	9,094	99,367	13,218
Equity*2	74,429	66,812	60,116	54,454	49,267	44,428
Total Assets	164,556	151,945	134,629	128,326	125,680	120,855
Working Capital	25,074	26,866	21,698	15,733	11,389	10,114
Interest-bearing Debt	3,414	1,633	3,034	5,417	7,859	9,196
Financial Ratios (%)						
As a percent of net sales:						
Gross Profit	33.0%	32.3%	33.3%	33.2%	32.8%	31.9%
Operating Income	7.0	6.8	7.3	7.6	7.5	6.7
Net Income	3.2	3.0	3.1	3.2	3.1	3.2
Current Ratio	132.6	137.3	133.4	124.5	117.3	116.1
ROE	11.7	11.8	11.7	12.9	14.1	15.9
ROA	5.0	5.2	5.0	5.3	5.4	5.8
Equity Ratio	45.2	44.0	44.7	42.4	39.2	36.8
Debt-equity Ratio (times)*3	0.05	0.02	0.05	0.10	0.16	0.21

*1 Capital expenditures as shown in Segment Information in the Notes to Consolidated Financial Statements.
*2 Presented as Shareholders' Equity until fiscal 2006. Presented as Equity from fiscal 2007 due to a change in accounting standards.
*3 Debt-equity ratio: Interest-bearing debt at the fiscal year-end divided by Shareholders' equity.

History

1886	Founder Chubei Kobayashi established Kobayashi Seidaido, Ltd., an unlimited general partnership in the Monzen-cho district of Naka-ku, Nagoya. The company sold general merchandise, cosmetics, and Western liquor.
1919	Established Kobayashi Daiyakubo, Ltd. in Nishi-ku, Osaka.
1940	Spun off the manufacturing unit of Kobayashi Daiyakubo, Ltd. to establish Kobayashi Pharmaceutical Co., Ltd.
1956	Kobayashi Daiyakubo Co., Ltd. and Kobayashi Pharmaceutical Co., Ltd. were merged and renamed Kobayashi Pharmaceutical Co., Ltd.
	Relocated the Head Office to Chuo-ku, Osaka.
1967	Launched *Anmerts*, a treatment for sore shoulders.
1969	Launched *Bluelet*, a deodorizing toilet bowl cleanser that became the Company's first toiletries product.
1972	Formed partnership with C.R. Bard Inc. of the U.S. to establish Medicon, Inc.
1975	Launched *Sawaday*, a deodorizing air freshener for toilets.
1982	Established Toyama Kobayashi Pharmaceutical Co., Ltd.
1990	Acquired Shield Healthcare Centers to enter the field of home nursing care services.
1993	Established Sendai Kobayashi Pharmaceutical Co., Ltd.
1998	Established Shanghai Kobayashi Friendship Daily Chemicals Co., Ltd. in China.
	Established Kobayashi Healthcare, Inc. in the U.S.
1999	Listed on the Second Section of the Osaka Securities Exchange.
2000	Introduced the in-house company and executive officer systems.
	Listed on the first sections of the Tokyo Stock Exchange and Osaka Securities Exchange.
	Spun-off the Trade Company to form Kobashou Co., Ltd.
2001	Established Kobayashi Healthcare Europe, Ltd. in UK
	Acquired Kiribai Chemical Co., Ltd.
2002	Sold all shares of Kobayashi Sofamor Danek K.K., following the dissolution of a joint venture agreement.
	Established Kobayashi Pharmaceutical (Hong Kong) Co., Ltd. in Hong Kong.
	Took over the *Tochucha* health food business of Hitachi Zosen Bio Corporation.
2003	Established Seiei Co., Ltd., an OTC pharmaceutical wholesaler with operations covering the entire Shikoku region, through a joint investment by four wholesalers, namely subsidiary Kobashou Co., Ltd., ASTIS Co., Ltd., Kowa Pharmaceutical Wholesalers Co., Ltd., and DAIWA Pharmaceutical Wholesalers Co., Ltd.
2004	Kobashou Co., Ltd. concluded business alliance agreements with Mitsubishi Corporation and Ryoshoku Ltd.
	Reorganized the Kobayashi Pharmaceutical Group into four business headquarters.
2005	Acquired the OTC pharmaceutical business of Suzuken Co., Ltd.
	Formed an equity-based alliance with Itoh Kanpo Pharmaceutical Co., Ltd.
2006	Made Sowa Co., Ltd. (currently KS Tohoku Co., Ltd.) a subsidiary
	Made eVent Medical Limited a subsidiary
	Made Heatmax, Inc. a consolidated subsidiary

Group Companies (As of March 31, 2007)

Company	Location	Capital	Main Business
Domestic consolidated subsidiaries			
■ Sendai Kobayashi Pharmaceutical Co., Ltd.	Yamato-cho, Kurokawa-gun, Miyagi, Japan	¥200 million	Manufacturing of pharmaceuticals and other products
■ Toyama Kobayashi Pharmaceutical Co., Ltd.	Toyama, Japan	¥100 million	Manufacturing of pharmaceuticals and other products
■ Ehime Kobayashi Pharmaceutical Co., Ltd.	Niihama, Ehime, Japan	¥77 million	Hygienic and paper goods manufacturing
■ Kiribai Chemical Co., Ltd.	Yodogawa-ku, Osaka, Japan	¥49 million	Disposable body warmer manufacturing and sales
■ Kobashou Co., Ltd.	Chuo-ku, Tokyo, Japan	¥4,297 million	Pharmaceutical products wholesaling
■ Kenshou Co., Ltd.	Hatsukaichi, Hiroshima, Japan	¥465 million	Pharmaceutical products wholesaling
■ Seiei Co., Ltd.	Takamatsu, Kagawa, Japan	¥300 million	Pharmaceutical products wholesaling
■ KS Hokkaido Co., Ltd	Higashi-ku, Sapporo, Hokkaido, Japan	¥10 million	Pharmaceutical products wholesaling
■ KS Tokai Co., Ltd	Chidane-ku, Nagoya, Aichi, Japan	¥10 million	Pharmaceutical products wholesaling
■ KS Tohoku Co., Ltd.	Miyagi, Sendai, Japan	¥10 million	Pharmaceutical products wholesaling
■ Aoitori Distribution Co., Ltd.	Chuo-ku, Osaka, Japan	¥99 million	Transportation services
■ Kobayashi Seiyaku Plax Co., Ltd.	Toyama, Japan	¥95 million	Synthetic resin products manufacturing
■ Suehiro Sangyo Co., Ltd.	Chuo-ku, Osaka, Japan	¥15 million	Daily goods sales
■ Archer Corporation	Chuo-ku, Tokyo	¥10 million	Advertising, planning and creation
■ SP-Planning, Inc.	Chuo-ku, Osaka, Japan	¥10 million	Displays and model production
■ Kobayashi Pharmaceutical Life Service Co., Ltd.	Chuo-ku, Osaka, Japan	¥10 million	Insurance agency and real estate management
■ Kobayashi Pharmaceutical Sales Promotion, Ltd.	Chuo-ku, Osaka, Japan	¥100 million	Marketing and sales promotional activities of pharmaceuticals and daily goods
■ Kobayashi Pharmaceutical Distribution Co., Ltd.	Chuo-ku, Osaka, Japan	¥10 million	Transportation Services
Overseas consolidated companies			
■ Kobayashi Healthcare, LLC	Pennsylvania, U.S.A.	US$5,110,000	Daily goods sales
■ Kobayashi Healthcare Europe, Ltd.	London, U.K.	UK£14,081	Daily goods sales
■ Kobayashi Healthcare Germany GmbH	Düsseldorf, Germany	974,000 Euro	Daily goods sales
■ Shanghai Kobayashi Daily Chemicals Co., Ltd.	Shanghai, China	141,428,621 RMB	Daily goods manufacturing and sales
■ Kobayashi Pharmaceutical (Hong Kong) Co., Ltd.	Hong Kong, China	HK$1,570,000	Daily goods sales
■ HeatMax, Inc.	Georgia, U.S.A.	US$1,230,000	Disposable body warmer manufacturing and sales
■ Mediheat, Inc.	Georgia, U.S.A.	US$10	Disposable body warmer manufacturing and sales
■ Thermomax, Inc.	Georgia, U.S.A.	US$0	Disposable body warmer manufacturing and sales
■ Kobayashi Healthcare of America, Inc.	Georgia, U.S.A.	US$6,100	Holding company
■ Kobayashi Pharmaceuticals of America, Inc.	California, U.S.A.	US$1	Management of U.S. operations
■ Kobayashi Medical America, LLC	California, U.S.A.	US$23,000,000	Research into imported products
■ eVent Medical Inc.	California, U.S.A.	US$100	Respirator sales
■ eVent Medical Ltd.	Galway, Ireland	UK£2,660	Respirator manufacturing and sales
■ eMed Ltd.	Galway, Ireland	UK£127	Respirator sales
Equity-method affiliates			
■ Medicon, Inc.	Chuo-ku, Osaka	¥160 million	Medical equipment and device import and sales
■ Itoh Kanpo Pharmaceutical Co., Ltd.	Higashi Osaka, Osaka	¥2,085 million	Daily goods manufacturing and sales

Notes: 1. The following companies are Specified Subsidiaries as defined by Japanese law: Kobashou Co., Ltd.; Toyama Kobayashi Pharmaceutical Co., Ltd.; Kenshou Co., Ltd.; Shanghai Kobayashi Daily Chemicals Co., Ltd.; Kobayashi Healthcare, LLC; and Kobayashi Medical America, LLC.

2. During the year ended March 31, 2007, the following companies became affiliated companies: KS Tohoku Co., Ltd.; Kobayashi Medical America, LLC; Kobayashi Pharmaceutical Sales Promotion, Ltd.; Kobayashi Healthcare of America, Inc.; eVent Medical Inc.; eVent Medical Ltd.; eMED Ltd.; HeatMax, Inc.; Mediheat, Inc.; Thermomax, Inc.; and Kobayashi Pharmaceutical Distribution Co., Ltd.

3. The following companies were excluded from the scope of affiliated companies due to the transfer of share ownership: Shield California Healthcare Centers, Inc.; Shield Denver Healthcare Centers, Inc.; and Shield Distribution, Inc.
The following companies were excluded from the scope of affiliated companies due to liquidation: Bluebird Development LLC and Kobayashi Healthcare, Inc.
Aoitori Distribution Co., Ltd. was split into two companies in January 2007—Aoitori Distribution Co., Ltd. and Kobayashi Pharmaceutical Distribution Co., Ltd. Aoitori Distribution Co., Ltd. subsequently merged with Kobashou Co., Ltd. in April 2007.

4. The net sales of Kobashou Co., Ltd. (excluding inter-group sales and transfers) comprise more than 10% of total consolidated net sales.

■ Consumer Products Operation ■ Wholesale Operation ■ Medical Devices Operation ■ Other Operations

Corporate Data / Investor Information (As of March 31, 2007)

Corporate Data

- Corporate Name: KOBAYASHI PHARMACEUTICAL CO., LTD.
- Foundation: August 22, 1919
- Head Office: 3-6, Doshomachi 4-chome, Chuo-ku, Osaka 541-0045, Japan
- Representative Director: Yutaka Kobayashi, President (Appointed president on June 29, 2004)
- Number of Employees: 2,173 (Consolidated)
- Consolidated Subsidiaries: 32
- Non-consolidated Subsidiaries: 6
- Affiliates Accounted for by the Equity Method: 2

Investor Information

- Common Stock: ¥3,450 million
- Number of Shares Authorized: 170,100,000
- Number of Shares Issued: 42,525,000
- Number of Shareholders: 8,295
- Stock Exchange Listing: Tokyo Stock Exchange 1st Section,
  Osaka Securities Exchange 1st Section
- Transfer Agent: Mitsubishi UFJ Trust and Banking Corporation
- Annual Shareholders' Meeting: June
- Investor Relations: KOBAYASHI PHARMACEUTICAL CO., LTD.
  Corporate Communication Department
  Tel. 81-6-6222-0142
  Fax. 81-6-6222-4261
  E-mail: info@kobayashi.co.jp
  URL: http://www.kobayashi.co.jp/

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