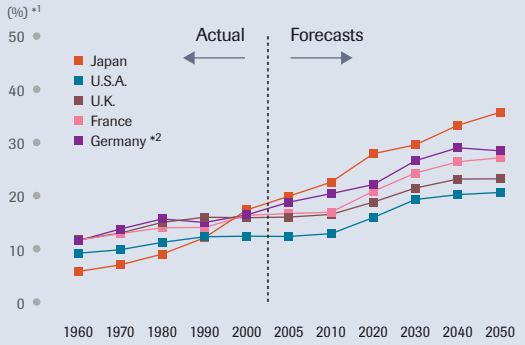
TAISHO PHARMACEUTICAL CO., LTD.

ANNUAL REPORT 2006

Balanced for Flight

MARKET ENVIRONMENT DATA

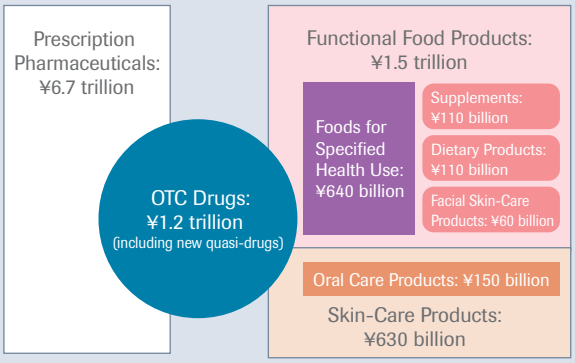
PERCENT OF POPULATION AGED 65 AND OVER



*1 Percentages are based upon estimated populations (medium projections) for each year in "World Population Prospects: The 2004 Revision" by the United Nations. Percentages for Japan, however, are based upon "Population Census Report" by the Statistics Bureau, Ministry of Internal Affairs and Communications, and "Population Projections for Japan: 2001 – 2050" (medium projections) published in January 2002 by the National Institute of Population and Social Security Research.
*2 Figures for all of Germany

Source: National Institute of Population and Social Security Research

SIZE OF THE HEALTH-RELATED PRODUCTS MARKET



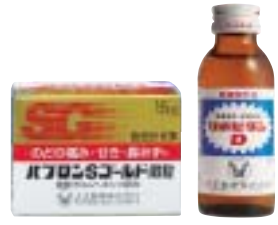
Source:
Prescription Pharmaceuticals:
Shipments according to the Statistical Survey on Trends in Pharmaceutical Production by the Ministry of Health, Labour and Welfare
OTC: SDI+SRI
Supplements/Dietary Products/Facial Skin-Care Products: FUJI KEIZAI CO., LTD.
Foods for Specified Health Use: Japan Health Food & Nutrition Food Association
Functional Food Products/Skin-Care products/Oral Care Products: Sogo Kikaku Center Osaka Co., Ltd.

Prompted by an aging population and a growing awareness among consumers regarding personal health, Japan's pharmaceutical market is experiencing a fundamental shift, as it strives to address evolving consumer needs, from treatment to prevention and anti-aging.

STRENGTHS OF TAISHO PHARMACEUTICAL

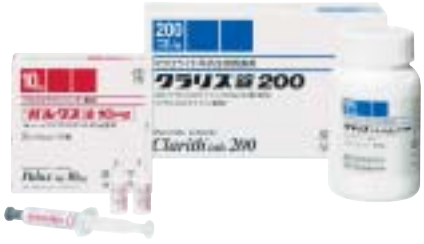
SELF-MEDICATION

- Japan's leading OTC drug company
- The top ranking in a number of market categories
- Growing presence in the functional foods and skin-care markets underpinned by its excellent reputation as a pharmaceuticals provider



PRESCRIPTION PHARMACEUTICAL

- From a sales and marketing perspective, Taisho Pharmaceutical will continue to focus on its fields of particular strength
- A broad product lineup and top-class share in the infectious diseases field
- Concentrated allocation of resources in specified domains including central nervous system (CNS), diabetes and infectious diseases research and development



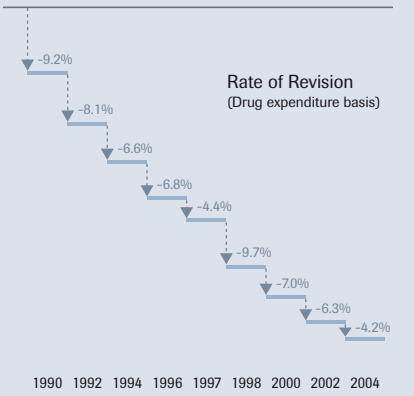
CONTENTS

CALCULATION OF DRUG PRICES IN EACH COUNTRY AND CONNECTION TO SETTING OF DRUG PRICES BY PHARMACEUTICAL COMPANIES

Country	Health insurance framework	Drug price calculations	Connection to pharmaceutical companies
Japan	• National health insurance (Social insurance system)	Official pricing	Submit application forms, present opinion regarding scheme for calculating drug price and file appeals
U.S.A.	• Private health insurance • Public health insurance (Medicare, Medicaid)	Free pricing	Prices set by pharmaceutical companies
U.K.	• National health insurance service (tax-basis)	Free pricing (Profit margins regulated)	Prices set by pharmaceutical companies

Source: Documents from the Office of Pharmaceutical Industry Research, Japan Pharmaceutical Manufacturers Association

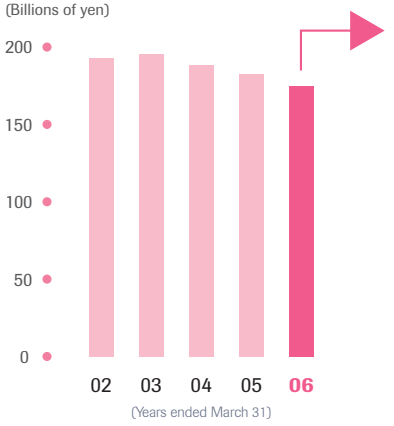
REVISIONS IN DRUG PRICES SINCE 1990



Source: Ministry of Health, Labour and Welfare presentation documents

Just as the lowering of drug prices is critical to healthcare expense reduction, the development and release of new drugs is essential to pharmaceutical company growth.

NET SALES



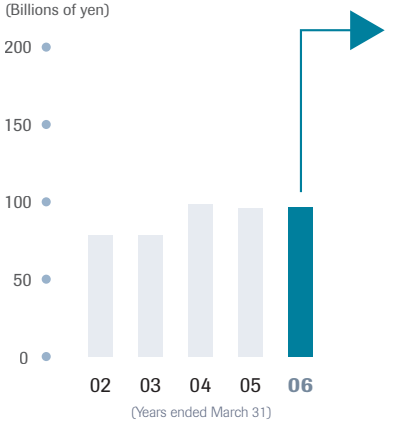
ACTIVITIES IN FISCAL 2005

Established a platform for growth in new business domains

- Commenced activities in the health and beauty business
- Commenced mail-order and direct sales

Proactively pursued business alliance

- Taisho Pharmaceutical strives to leverage external know-how through collaborative arrangements with a variety of companies in growth fields, including functional food and skin-care products.



Adopted a selection and focus approach toward sales and marketing as a means to promote sales growth

- Prioritized products in four categories including *Clarith*

Achieved further progress in new drug pipeline

- Within its new drug pipeline, two proprietary drugs entered Phase 2

Fellow Stakeholders

LEFT: Shoji Uehara, Chairman of the Board
RIGHT: Akira Uehara, President

Taisho Pharmaceutical's mission is to contribute to society by creating and offering superior pharmaceuticals and health-related products, as well as healthcare-related information and services in socially responsible ways that enrich people's lives by improving health and beauty. Guided by this fundamental philosophy, we strive to become a pharmaceutical manufacturer capable of covering a variety of needs from enhancing health and preventive measures to treatment. To accomplish this, we are forging ahead with our self-medication business, which is centered on OTC drugs, and our prescription pharmaceutical business, which handles ethical drugs. Through these endeavors, Taisho Pharmaceutical works tirelessly to maximize corporate value.

Taisho Pharmaceutical's Efforts in Response to Health-Related Industry Trends

The pharmaceuticals industry is currently confronting a critical turning point in its ongoing development. From a health-related perspective, the industry is experiencing a fundamental shift and expansion from the prescription pharmaceutical (¥6.7 trillion) and OTC drug (¥1.2 trillion) markets to the functional food products (¥1.5 trillion) and skin-care (¥630 billion) markets. (Figures in parentheses represent market scale as of fiscal 2004—Company estimate.) Along with the conventional need for drugs to treat diseases and disorders, we are witnessing an upsurge in demand for health foods and other products that can prevent lifestyle-related ailments and aging. Under these circumstances, the industry is evolving across traditional boundaries and expanding toward growth markets, including functional food products and skin care.

Amid this changing environment, Taisho Pharmaceutical will work to further strengthen its position in its mainstay pharmaceuticals business by placing particular emphasis on the discovery and development of innovative new ethical drugs in addition to sales growth in the OTC drug market. Furthermore, we endeavor to expand business in high-growth health-related fields such as beauty and food products by leveraging consumer confidence and trust as a pharmaceutical company, as well as our brand power and marketing expertise.

Outlook for the Self-Medication Business

Many of the OTC drugs marketed by Taisho Pharmaceutical hold a leading position in their respective market categories. With a continued decline in retail prices and market contraction, however, boosting the development of existing applications alone is unlikely to result in market and sales growth.

Against this backdrop, the Japanese Diet passed an amendment to the Pharmaceutical Affairs Law concerning the sale of OTC drugs in June 2006. With high expectations for market expansion, particularly for switch-OTC drugs (products that incorporate the active ingredients of prescription drugs), Taisho Pharmaceutical will continue to pursue opportunities in new business fields and develop products that accurately address consumer needs, facilitate the prevention and treatment of lifestyle-related disease and serve to enhance quality of life. Furthermore, with ongoing progress in the screening of switch-OTC drugs, signs are emerging of significant activity within the market. Extending beyond existing boundaries, new applications

are contributing to OTC drug market expansion. Looking ahead, we expect OTC drugs to play a prominent role in curtailing medical expenses and realizing increased efficiency in medical systems. Recognizing the positive impact of new ingredients and applications on market growth in Europe and the United States, we expect the domestic market to follow suit with new developments in switch-OTC drugs, creating fresh opportunities for growth.

Outlook for the Prescription Pharmaceutical Business

The most important feature of our prescription pharmaceutical business is the ability to continuously deliver new products. Our research activities therefore focus on highly original research themes, incorporating the latest advanced technologies and leveraging the Company's deep-rooted capacity to conceive original compounds.

Since realigning our R&D organization in 1995, we have submitted a succession of original compounds for clinical testing. As the Company approaches its centenary celebrations, Taisho Pharmaceutical plans to launch one or two new drugs each year covering select strategic domains such as diabetes and CNS. In the interim period, we intend to bring new products to market developed by Toyama Chemical Co., Ltd. and through joint development with Nissan Chemical Industries, Ltd. Taisho Pharmaceutical products are sold in Japan through Taisho Toyama Pharmaceutical Co., Ltd., a joint-venture company established with Toyama Chemical. As the Company moves steadily toward its proprietary new drug pipeline, Taisho Pharmaceutical will continue to leverage sales rights of other companies' products and engage in product sales under collaborative agreements. Focusing on strategic fields, including infectious, inflammatory and immunologic diseases, we will redouble our efforts to secure revenue and earnings growth.

In Partnership with Other Companies

Looking ahead, the health and beauty markets offer enormous potential for growth. To fully grasp the opportunities at hand, we recognize the need to implement measures that break through existing convention. To this end, Taisho Pharmaceutical is committed to accelerating the development of new products that address the diverse needs of consumers and to cultivate new markets. Going forward, we will therefore consider business alliances and partnerships, leveraging the wealth of ideas and know-how that currently lie outside our scope and capabilities. This philosophy was the driving force behind the Company's business and equity tie-up with Yomeishu Seizo Co., Ltd. in 2005. Respecting the corporate culture and tradition of each company, we will consider additional partnerships in an effort to expand business further.

Overview of Fiscal 2005 Results

Fiscal 2005, ended March 31, 2006, was a year of intense pressure as the Company strove to keep pace with changing market conditions and needs. For the second year in succession, we experienced a decline in both revenues and earnings. Buffeted by a contraction in the nutrient drink and OTC drug markets, Taisho Pharmaceutical recorded stagnant sales in its mainstay products, including Lipovitan D, Pabron and RiUP. On a positive note, efforts to focus on strategic products in prescription pharmaceuticals proved accurate, with results in this category essentially in line with initial forecasts.

As Japan confronts a major overhaul of its legal system, OTC drugs are expected to gain significant prominence within the boundaries of a newly defined market. Over the next two to three years, switch-OTC drugs, in particular, are expected to realize substantial market potential. Ahead of the changes in the OTC drug industry, Taisho Pharmaceutical has continued to develop products that reflect and address changing conditions and needs. Recognizing the growing importance of peripheral fields, we are also pursuing businesses related to health and beauty in an effort to further strengthen our activities.

Taisho Pharmaceutical is distinguished by its efforts to promote growth across both the OTC drug and prescription pharmaceutical fields. The Company's business approach is to maintain optimal balance between each field, generate maximum synergy benefits and accelerate growth through proactive collaboration with other companies in Japan and overseas. In addition to business tie-ups, we allocate cash flows to the development of new drugs and the introduction of new products in growth fields with the aims of promoting long-term growth and enhancing corporate value.

Taking into consideration the long-term funds required to address and create the needs of a new era, Taisho Pharmaceutical also targets a dividend payout ratio of 30% and the appropriate return of profits to shareholders. Committed to fulfilling our mission of raising value and contributing to society as a whole, we kindly request the continued support and understanding of all stakeholders.

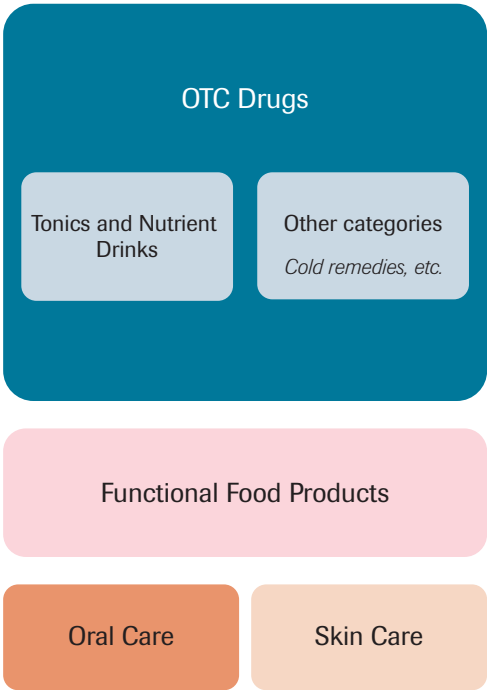
Shoji Uehara, Chairman of the Board

Akira Uehara, President

Japan's OTC drug market has suffered negative growth over the past several years. Efforts by the government and private sector to promote self-medication are cited as one method to alleviate pressure on financing for public medical insurance. These efforts have not yet gained sufficient acceptance and recognition, however, and have not, thus far, led to the expansion of the OTC drug market. In contrast, consumer awareness of health is rising, leading to heightened enthusiasm surrounding functional foods such as Foods for Specified Health Use (FOSHU) and supplements, as well as other health-related products. The functional food product market, in particular, is forecast to outpace the growth of the OTC drug market. Taisho Pharmaceutical is implementing a variety of measures in the health-related market, encompassing cure, prevention and beauty. As a leading company in OTC drugs, Taisho Pharmaceutical will grasp opportunities for growth in switch-OTC drugs. At the same time, the Company will cultivate new domains in health-related products. In its drive to expand, Taisho Pharmaceutical will leverage the brand strength of its market-leading products such as *Lipovitan D* nutrient drink, *Pabron* cold remedy and *RiUP* hair regrowth treatment. We believe it is also important to utilize the trust we have earned as a pharmaceutical manufacturer.

Spreading Our Wings across New Domains

THE SELF-MEDICATION OPERATION GROUP'S BUSINESS DOMAIN



The nutrient drink business, which is the nucleus of the self-medication business, continues to contract. In addition to falling retail prices, other factors include slow sales growth at food retailers such as convenience stores and supermarkets, and more intense competition with functional beverages and similar products. Aiming to reinvigorate its nutrient drink business, Taisho Pharmaceutical has set clear targets to drive expansion of product sales. We have also delivered samples of the drink at our events called "*Lipovitan D Jack*," promoting *Lipovitan D* in major cities throughout Japan, and are making efforts to broaden the user base. While continuing to enhance our product lineup, we will endeavor to strengthen sales of individual bottles at stores and reform our sales organization, assigning sales representatives to chain stores to be responsible for either nutrient drinks or for other OTC drugs. Leveraging the brand power of our well-known *Lipovitan D* product, we will strive to expand sales of the overall *Lipovitan* series.

Taisho Pharmaceutical's *Pabron* brand cold remedy also enjoys a solid footing in the market in spite of variations

in the incidence of colds and hay fever. We will continue to bolster the *Pabron* lineup through relentless initiatives to develop and market new products, and thereby increase market share. Regarding *RiUP* hair regrowth treatment, Taisho Pharmaceutical will promote further entrenchment of the brand among male users, and focus on expanding market recognition of *RiUP Lady* for women.

Trends in switch-OTC drugs hold the key to the future of the OTC drug market. Partial revisions of the Pharmaceutical Affairs Law in April 2007 will usher in changes in the methods of selling OTC drugs. It is also expected these changes will help to underpin the expansion of the switch-OTC market. Though the number of switch-OTC active ingredients that have been approved in Japan currently lags behind numbers in Europe and the U.S., a growing number of people expect approval of such ingredients to increase from this time forward. Should products be introduced in the areas of preventing lifestyle-related diseases and enhancing quality of life, such developments would undoubtedly serve to invigorate the OTC drug market. In order to get a head start on such changes, Taisho Pharmaceutical has numerous candidate ingredients and is pushing vigorously ahead with development of switch-OTC drugs.

In notably growing market domains, Taisho Pharmaceutical has made the health and beauty business, which handles FOSHU and skin-care products, into an independent division. At the same time, Taisho Pharmaceutical launched *Nourish*, a new series of supplements and skin-care products. In this context, Taisho Pharmaceutical began selling supplements and skin-care products through a joint venture agreement with Toyo Shinyaku Co., Ltd., and plans to expand the number of items in the product lineup. In FOSHU, the *Livita* brand product line continues to gain recognition among consumers. We will introduce a stream of new products in high-demand areas such as metabolic syndrome and anti-aging in a push to rapidly attain ¥5 billion in *Livita* brand sales.

Nourish brand products will be sold exclusively through mail order, representing a groundbreaking endeavor in Taisho Pharmaceutical's marketing strategy. Making full use of our expertise as a pharmaceutical manufacturer, Taisho Pharmaceutical will tap new customer segments by meeting the needs of consumers, and strive to attain steady growth.

Taisho Pharmaceutical will maintain a careful watch on legislation regarding pharmaceuticals and market trends. We will leverage the brand strength, marketing power and the development capabilities we have accumulated through our previous endeavors, and make focused investment of management resources in growth fields.

Taisho Pharmaceutical is striving to address a number of core issues in the prescription pharmaceutical business. First, the Company is working to further enhance the synergistic effects of business integration, following the establishment of Taisho Toyama Pharmaceutical, a joint venture established with Toyama Chemical. Another primary focus is to create highly original new drugs for the global market. In pursuit of integration effects, we have been working to focus and consolidate our sales organization and to standardize our personnel evaluation system as rapidly as possible. In addition, we have almost completed construction of a structural framework that will empower us to concentrate on expanding performance.

Taisho Toyama Pharmaceutical currently boasts a force of about 1,000 medical representatives (MRs), reflecting vigorous efforts to bolster the sales organization since full-fledged operations got underway in April 2003.

The first initiative undertaken was to clarify focus areas. Taisho Toyama Pharmaceutical has continued to prioritize and focus on infectious diseases, as well as inflammatory and immunologic diseases, and calls on its conventionally strong client bases in orthopedics and respiratory tract medicine. Rather than developing sales in all directions, we are aiming to establish a sales organization capable of outdoing global mega-pharmaceutical companies in selected areas.

Taking Flight across Focused Domains

NEW DRUG PIPELINE (As of August 31, 2006)

Stage	Name	Formulation	Indication	In Development with	Originator	Remarks
Field	T-3811	Oral	New-type quinolone antibacterial agent	Toyama Chemical	Toyama Chemical	
	Clarith	Oral	H. pylori eradication in combination with rabeprazole and amoxycillin	Eisai, Abbott Japan, etc.	Taisho Pharmaceutical	Change of dosage and administration
Phase 2	NT-702	Oral	Intermittent claudication caused by ASO*, SCS*	Nissan Chemical	Nissan Chemical	
	(NM-702)	(Oral)	(Intermittent claudication caused by ASO*)	(Nissan Chemical)	(Nissan Chemical)	(Overseas)
	NT-702	Oral	Asthma	Nissan Chemical	Nissan Chemical	
	TS-033	Oral	Type 1 and 2 diabetes	In-house	Taisho Pharmaceutical	In Japan and overseas
	TS-022	Topical	Atopic dermatitis	In-house	Taisho Pharmaceutical	
	Palux	Injection	Intermittent claudication caused by SCS*	In-house	Taisho Pharmaceutical / Mitsubishi Pharma	Additional indication
Phase 1	TS-021	Oral	Type 2 diabetes	In-house	Taisho Pharmaceutical	In Japan and overseas
	TS-041	Oral	Depression and anxiety	Janssen Pharmaceutica N.V.	Taisho Pharmaceutical	Overseas
	TS-011	Injection	Cerebral infarction (acute)	In-house	Taisho Pharmaceutical	Overseas

* ASO: Arteriosclerosis obliterans * SCS: Spinal canal stenosis

Integrating sales methods is also an important step on the way to focus and consolidation. We have worked to unify thinking in relation to principal physicians, an area in which Taisho Pharmaceutical and Toyama Chemical previously have not moved in step. MRs at Taisho Toyama Pharmaceutical have created lists of approximately 100 principal physicians each, drawn up indices for the number of visitations, and implemented other initiatives, to consolidate activities. Currently, Taisho Toyama Pharmaceutical's physician coverage ratio is 100% at major hospitals. As for physicians in general practice, Taisho Toyama Pharmaceutical intends to make focused visits to physicians in the fields of orthopedics, as well as infectious diseases such as respiratory tract medicine and otorhinolaryngology (ENT), with the aim of raising its coverage ratio in these areas.

Taisho Toyama Pharmaceutical has also selected four core products on which to focus, namely macrolide antibiotic agent *Clarith*, new quinolone antibacterial agent *OZEX*, antibacterial agent *PENTCILLIN* for injections, and the peripheral vasodilator *Palux*. As a result of these initiatives, all four of these products have accomplished, under tough and challenging market circumstances, sales growth compared to the previous fiscal year.

In addition, a standardized personnel evaluation system, which was introduced in April 2005, is making the shift from an abilities-based system to a performance-based system. Evaluation periods have been shortened from one year to a half-year in order to accelerate the turnover of all work processes, including smooth and rapid sales expansion of new products. An issue for the future is that most of the main products are sold through co-marketing with other firms. In the event that new products are to be brought to the market and sold solely by Taisho Toyama Pharmaceutical, Taisho Toyama Pharmaceutical will examine the options of increasing the number of MRs and physician coverage.

Enhancing the skills and quality of MRs is indispensable to further strengthening the sales organization. Taisho Toyama Pharmaceutical has established an in-house "Super MR" certification system in an initiative to educate MRs to enhance their knowledge in specific fields. The first fruit of this endeavor was the certification of 70 "Super MRs" in the area of infectious diseases following two years of training. The short-term goal is to increase the number of "Super MRs" to 100 in the area, with the field of inflammatory and immunologic diseases being considered as the next area for other "Super MRs" training.

The prescription pharmaceutical business continues to face tough and challenging market conditions, including the launch of a lot of generic versions of macrolide antibiotic agent *Clarith* in Japan in July 2006. To minimize the impact of such generic products, Taisho Pharmaceutical introduced improved-formula *Clarith dry syrup* for children in June 2006, following introduction of smaller tablets for adults. In parallel with proceeding efficiently toward the creation and development of new drugs, which are expected to be launched after 2010, the Prescription Pharmaceutical Operation Group will strive to expand its business by focusing on priority areas such as infectious diseases, and by consolidating marketing strengths.

Research and Development

Augmenting Our Research Base and Development Infrastructure

Conditions surrounding Japan's pharmaceutical industry are experiencing significant upheaval. Most notably, organizations such as the International Conference on Harmonization of Technical Requirements for Registration of Pharmaceuticals for Human Use (ICH) are accelerating market internationalization, while reforms to medical care delivery systems including efforts to contain pharmaceutical costs are gaining in prominence. As the era of government protection draws to a close, pharmaceutical companies in Japan are confronted by full-fledged global competition and a battle for their very survival. Under these circumstances, each company has endeavored to reestablish its research and development strategy and has shifted toward a unique R&D organizational structure. Through these means, each company is working to secure a viable position in the 21st century and to ensure continuous operations as a going concern.

Taisho Pharmaceutical has continued to pursue pharmaceutical research and development since 1995 guided by its basic philosophy "to develop drugs imbued with creativity and rooted in science and ethics, aiming to contribute to the health of the public." In the Prescription Pharmaceutical Operation Group, we are focusing R&D efforts on the strategic fields of CNS, diabetes, allergies and infectious diseases. Concentrating on these areas, we are working to consistently create new drugs that are viable in the international market, as well as to improve our international development infrastructure and to bolster our marketing platform in Japan. In addition, we are further developing our information-gathering network from research institutes in Japan, the U.S. and Europe in efforts to stay abreast of cutting-edge information. Through the introduction of new computer-based technologies in the areas of genome analysis and sequence prediction, as well as High-Throughput Screening, Combinatorial Chemistry and other technologies, we are making significant improvements to our new drug development system in terms of both quality and speed. Through such endeavors, we have transformed our system to one that is able to produce a consistent stream of clinical candidate compounds.

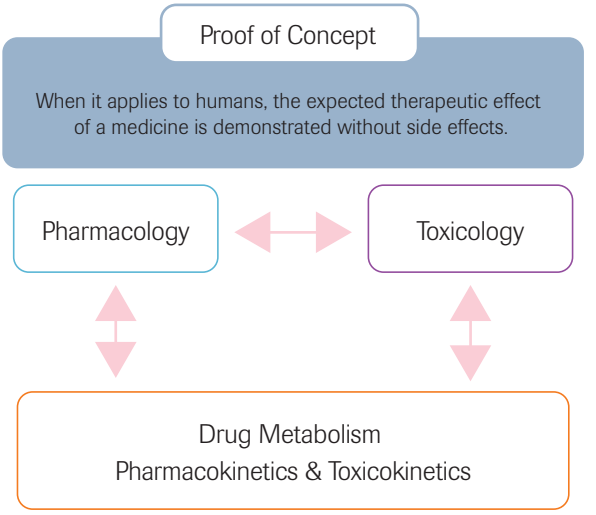
Mission of the Medicinal Development Research Laboratories

Taisho Pharmaceutical completed the development of its sophisticated drug discovery infrastructure by approximately 2002. With our original compounds having advanced to the development stage, we established the Medicinal Development Research Laboratories in April 2004. The new facility aims to strengthen our safety evaluation for candidate compounds at the preclinical stage and pharmacokinetic studies. The facility was also established for the purpose of developing and fully operating evaluation systems related to the safety, pharmacokinetics and physicochemical properties of compounds at the discovery stage, in order to produce high-quality clinical candidate compounds.

Strengthening Preclinical Evaluation

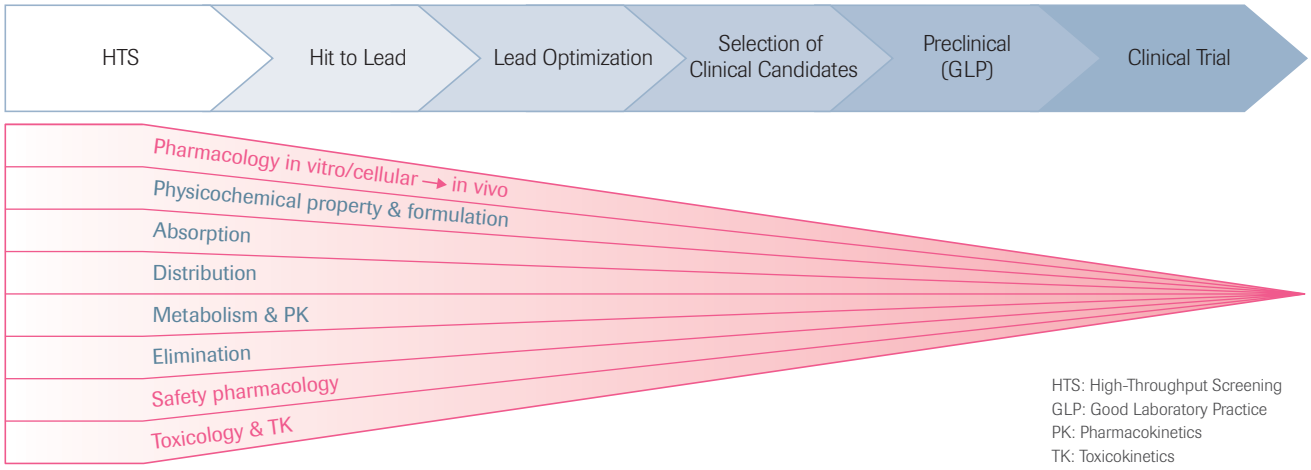
Through the planning and implementation of studies to grasp the innate toxicity and pharmacokinetics of candidate compounds, we are bolstering our safety and pharmacokinetic studies at the preclinical stage. The ultimate

STRENGTHENING OF A PRECLINICAL STUDY



DRUG DISCOVERY PARADIGM

High-quality clinical candidate compounds are found, since physicochemical property/formulation, absorption, distribution, metabolism/pharmacokinetics, elimination, safety pharmacology and toxicology/toxicokinetics are carried out in the early stage of drug discovery, and the compounds are narrowed down to the most sophisticated ones.

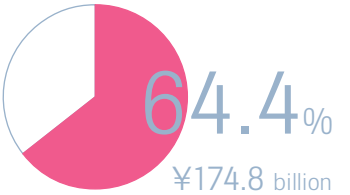


purpose of such infrastructure development is "to ensure the safety of products when used in humans," and "to predict problems and prepare appropriate countermeasures." Toward those ends, in addition to general toxicity, Taisho Pharmaceutical is considering the characteristics of targeted disorders and the action mechanisms of clinical candidate compounds, as well as the dosage and administration applied in clinical practice. We are also focused on substantiating that candidate compounds have no suspected side effects. (Fig. 1)

Developing and Fully Operating Evaluation Systems Related to the Safety, Pharmacokinetics and the Physicochemical Properties of Compounds at the Discovery Stage

There are many cases where, after the pharmacological effects of compounds have been assessed at the discovery stage (optimization of lead structures and selection of clinical candidate compounds), development is discontinued at the clinical trial phase due to problems with the safety (side-effects), pharmacokinetics or the physicochemical properties of compounds. This fact highlights the need for evaluation systems related to safety, pharmacokinetics, and the physicochemical properties of compounds at the discovery stage. Many causes of suspension of new drug development are related to a poor selection of candidates because compounds are chosen in spite of insufficient investigation at the time of discovery. To enhance the selection of clinical candidate compounds, Taisho Pharmaceutical is constructing a comprehensive evaluation system that assesses such compounds from a diverse range of scientific fields such as pharmacology/biochemistry/physiology, toxicology/pathology, pharmacokinetics and pharmaceutics. (Fig. 2). Conducting comprehensive assessment from a diverse range of scientific disciplines offers the following advantages. First, it evaluates effects and safety while striking a balance between pharmacological effects and toxicological effects (side effects), including assessment of pharmacokinetics. Second, it provides an evaluation of a compound's suitability for development based upon an assessment of its physicochemical properties, or in other words, an evaluation of a compound's preparation adjustability in clinical trials. Third, it gives an evaluation of the structure activity/toxicity relationship (based on data related to pharmacology, toxicity and pharmacokinetics). And fourth, it enables clarification of latent risks within compounds and formulation of countermeasures.

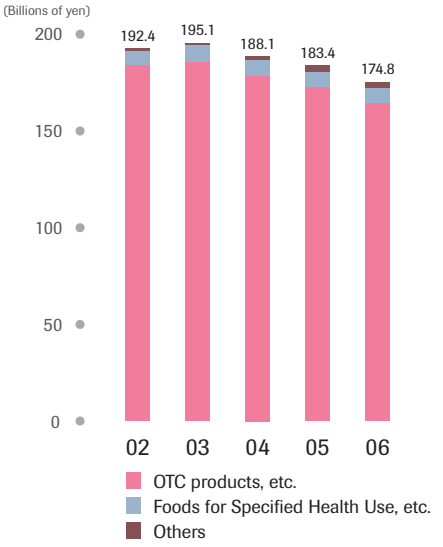
Self-Medication Operation Group



The Self-Medication Operation Group is comprised of OTC drugs, Foods for Specified Health Use and other businesses. In this segment, Taisho Pharmaceutical boasts a number of brands that rank first in their respective market categories. In the midst of a severe market environment, the Company shall endeavor to lead the market as the top manufacturer of OTC drugs, striving to expand sales areas, introduce new products and bolster its marketing organization.

NET SALES

(Years ended March 31)



NET SALES OF MAIN PRODUCTS

(Years ended March 31)

(Billions of yen)

	2006	2005	2004
OTC products, etc.	163.9	172.4	178.2
Lipovitan series	91.4	95.1	96.9
Lipovitan D	68.2	70.8	72.9
Others	23.2	24.3	24.0
ZENA series	4.9	5.0	4.6
Pabron series	26.1	27.3	28.1
RiUP series	12.0	13.5	15.3
Gastrointestinal treatments	4.9	4.9	5.4
Foods for Specified Health Use, etc.	8.1	7.8	7.9
Livita series	2.4	2.1	1.1
Overseas drinks	4.3	4.3	4.2

Lipovitan series and *Pabron* series

Livita series

1. Performance in Fiscal 2005

OTC Products, etc.

Sales of *Lipovitan* (nutrient drink) products dipped 3.9% to ¥91.4 billion. In the *Lipovitan* series, *Lipovitan D Super*, which was newly classified as a quasi-drug, leading to expanded sales channels, and new *Lipovitan Wins A* (Ace), which is primarily for sale in convenience stores, contributed to sales results. However, these results could not help cover the shortfall of the flagship product, *Lipovitan D*, which occurred in the first half of the fiscal year.

Tight raw material supply conditions in the first half of the year led to delays in production of the *Pabron* cold remedy series. Despite recovering from these delays, sales of *Pabron* products declined 4.4% to ¥26.1 billion, mainly owing to slumping sales of sinus medicine as a result of the low incidence of hay fever in the second half of the fiscal year.

In the *RiUP* series of hair regrowth treatments for androgenic alopecia, market penetration of the new *RiUP Lady*, released in March 2005 as Japan's first hair regrowth treatment for women, was slower than expected. This and other factors caused sales to decrease by 10.9% to ¥12.0 billion. In another OTC drug series, athlete's foot treatment *Dermarin* made a strong showing, posting a sales increase of 9.8% to ¥2.6 billion.

Foods for Specified Health Use, etc.

Sales of *Livita* brand products increased 16.9% year on year to ¥2.4 billion, spurred by strong sales of *Glucocare*, and new products *Canton Beauty* and *Livita Q10 Green Tea*. In addition, overseas sales of nutrient drinks increased 0.9% to ¥4.3 billion.

Other Business

Sales for this business segment include ¥1.2 billion in sales at subsidiaries involved in the hotel business and others.

2. Initiatives in Fiscal 2005

Establishment of the Health and Beauty Business

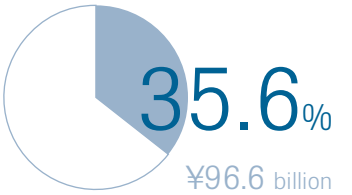
In light of its expansion in the health-related market, Taisho Pharmaceutical established a health and beauty business in order to grasp new business opportunities in this field. Leveraging the expertise accumulated through the development of pharmaceuticals, we launched mail order and direct sales of the new *Nourish* brand of supplements and skin care products in March 2006. In addition, Taisho Pharmaceutical took decisive action in forming alliances, entering a capital and operational partnership with Yomeishu Seizo Co., Ltd., as well as establishing a joint venture with Toyo Shinyaku Co., Ltd.

Launch of New Products

Aiming to strengthen its core nutrient drink lineup, Taisho Pharmaceutical began selling a number of products with clearly segmented targets, including *Lipovitan Wins A* (Ace), the highest-priced product among the *Lipovitan* series at convenience stores. The Company also introduced innovative new switch-OTC drugs. Among these was *Pabron Nasal Spray Z*, the world's first nasal spray to incorporate the antiallergenic agent ketotifen fumarate. Also introduced was *Dermarin Ace Liquid*, an athlete's foot treatment that leverages Taisho Pharmaceutical's unique drug delivery technologies to include amorolfine hydrochloride, an antifungal agent with exceptional penetration ability, that was thought to be difficult to make into a liquid formulation.

In response to heightening public awareness of "metabolic syndrome," in the Food for Specified Health Use series, Taisho Pharmaceutical launched *Naturalcare Tablet*, which mildly reduces blood pressure, under the *Livita* health support brand. This rounds out our lineup of products to combat the three risk factors contributing to hardening of the arteries, namely, high cholesterol, high blood sugar and high blood pressure.

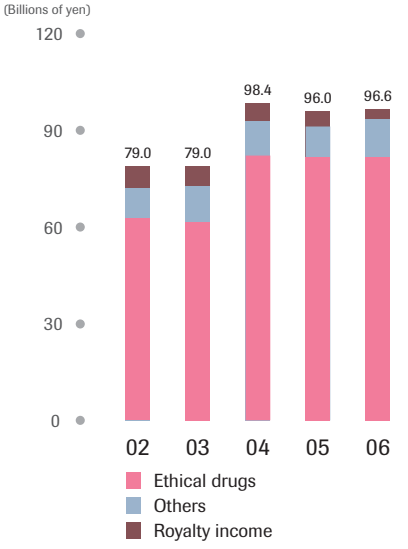
Prescription Pharmaceutical Operation Group



In the Prescription Pharmaceutical Operation Group, by concentrating resources in its strong areas, such as medications for the treatment of infectious diseases, Taisho Pharmaceutical is working to strengthen its sales organization and to focus on creating highly original new drugs for the global market. In efforts to ensure profitability until original new drugs go to market, Taisho Pharmaceutical is aggressively pursuing partnerships and alliances with Japanese and foreign companies.

NET SALES

(Years ended March 31)



NET SALES OF MAIN PRODUCTS

(Years ended March 31)

(Billions of yen)

Ethical drugs	2006	2005	2004	Application
Clarith	27.5	27.4	27.6	Macrolide antibiotic
Palux	12.0	12.0	13.2	Prostaglandin E1 preparation
PENTCILLIN	6.6	6.5	6.4	Synthetic penicillin product
Lorcam	4.5	4.5	4.5	Nonsteroidal anti-inflammatory/analgesic drug
TOMIRON	4.2	4.8	4.9	Cephem antibiotic product for oral use
OZEX	3.3	3.3	2.9	Broad spectrum antibacterial product for oral use
Metligine	2.1	2.2	2.2	Therapeutic agent for hypotension
LIMAS	2.4	2.3	2.3	Therapeutic agent for mania, manic states
SOLON	2.0	2.1	2.3	Mucosal protective and tissue healing agent for gastritis and gastric ulcer
LUPRAC	1.9	1.8	1.6	Loop diuretic
PASIL	1.2	1.2	0.9	New quinolone antibacterial product for injections

Mainstay products and products launched in fiscal 2005.

1. Performance in Fiscal 2005

Ethical Drugs

Efforts to boost the efficiency of sales activities at Taisho Toyama Pharmaceutical have been successful. Sales results of core products were slightly higher, with sales of macrolide antibiotic agent *Clarith* totaling ¥27.5 billion (up 0.1%) and peripheral vasodilator *Palux* totaling ¥12.0 billion (up 0.1%). Demand also grew steadily for new quinolone antibacterial agent *OZEX*, as well as for antibacterial injection agents *PENTCILLIN* and *PASIL*. Launched in 2005, the topical anti-inflammatory analgesic drug *Sumilu* also contributed to sales growth. As a result of these factors, sales at Taisho Toyama Pharmaceutical totaled ¥82.7 billion, up 0.5% from the previous fiscal year.

Others

Sales increased steadily, with sales of intermediates to Abbott Japan Co., Ltd. reaching ¥10.3 billion (up 23.7%), and sales of bone filling material *BIOPEX* totaling ¥0.8 billion (up 66.9%).

Royalty Income

Royalty income declined to ¥3.1 billion (down 37.0%) owing to the expiration of the U.S. patent for *Clarithromycin* and other factors.

New Drug Pipeline

Following the new-type quinolone antibacterial agent T-3811 (filed) that was jointly developed with Toyama Chemical, new drugs in the pipeline include NT-702, a treatment for arteriosclerosis obliterans that is currently in Phase 2 clinical study in Japan. NT-702 is being jointly developed with Nissan Chemical Industries, Ltd. Known by the development code NM-702 outside Japan, its positive results from Phase 2b clinical study were announced in March 2006. In addition, our original compounds TS-033, a treatment for diabetes featuring a new mechanism, and TS-022, a treatment for atopic dermatitis that meets needs that conventional drugs cannot, both entered Phase 2 clinical trials at the end of fiscal 2005 in Japan.

2. Initiatives in Fiscal 2005

Taisho Toyama Pharmaceutical also continued to develop the sales and marketing activities it began in the latter half of the previous fiscal year, focusing on four priority products.

Aiming to bolster our lineup of existing products, we launched sales of *Palux injection Dispo 10μg*, an injection kit for our peripheral vasodilator *Palux*. Moreover, we entered an agreement with Mikasa Seiyaku Co., Ltd. to undertake collaborative marketing of the topical anti-inflammatory analgesics *Sumilu Stick and Sumilu Tape*. Such new product launches in strategic fields contributed to increased sales.

ORIGINAL NEW DRUGS ENTERING CLINICAL TRIAL STAGE (As of August 31, 2006)

Therapeutic Area	Name	Application	Mechanism	Stage	Area Developed	Partner
Diabetes	TS-033	Type 1 and 2 diabetes	SGLT inhibitor	Phase 2	Japan Overseas	
	TS-021	Type 2 diabetes	DPP-IV inhibitor	Phase 1	Japan Overseas	
CNS	TS-041	Depression and anxiety	CRF1 receptor antagonist	Phase 1	Overseas	Janssen Pharmaceutica N.V.*
	TS-011	Acute stage of cerebral infarction	20-HETE synthesizing enzyme inhibitor	Phase 1	Overseas	
Allergies	TS-022	Atopic dermatitis	Prostaglandin derivative	Phase 2	Japan	

SGLT: Sodium dependent glucose cotransporter
CRF1: Corticotropin-releasing factor 1
DPP: Dipeptidyl peptidase
20-HETE: 20-hydroxyeicosatetraenoic acid
*Co-development for overseas

Corporate Governance and Corporate Social Responsibility

Corporate Governance

1. Fundamental Policy

In an effort to ensure appropriate action and response to changes in its business environment, Taisho Pharmaceutical has positioned corporate governance as one of its highest management priorities. In this context, the Company adopted an executive officer system and reduced the size of its Board of Directors with the aims of enhancing supervisory functions and facilitating more accurate and speedy decision-making.

2. Management Structure

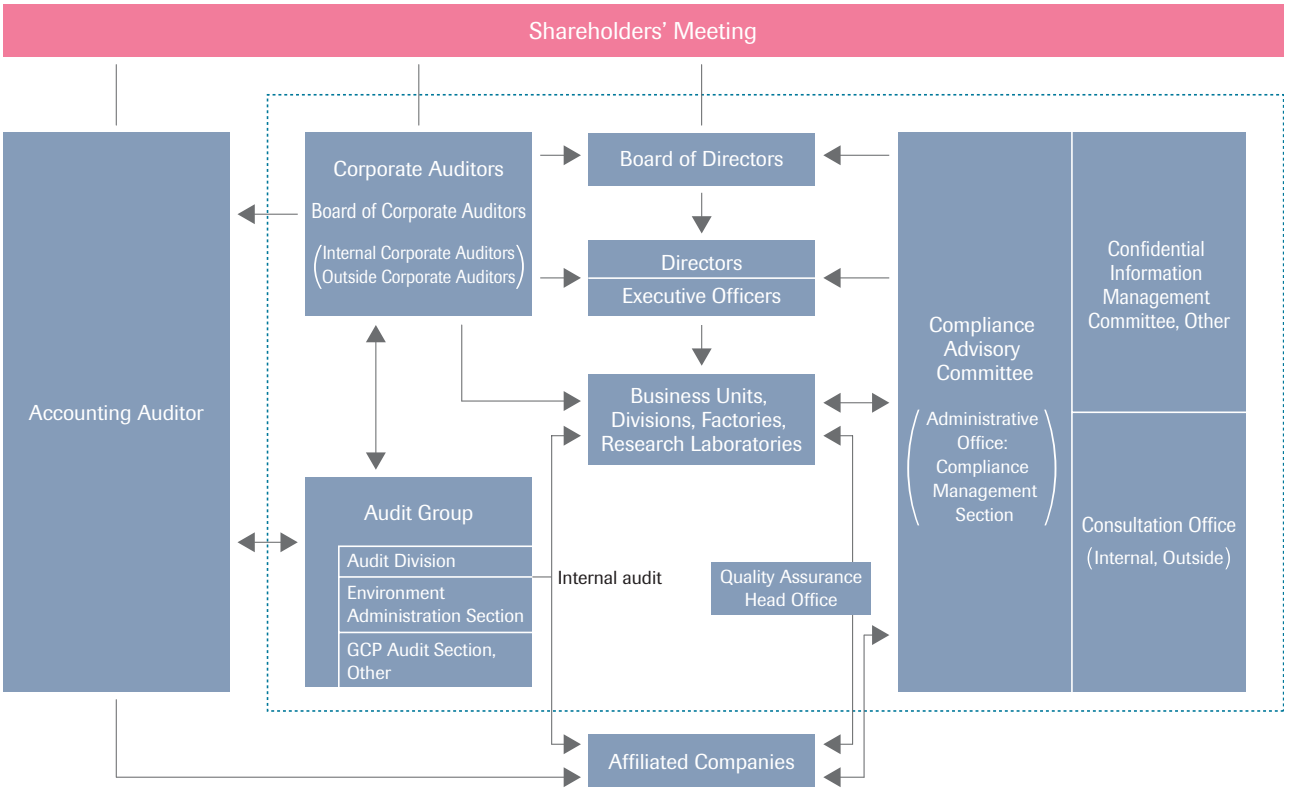
Directors, Board of Directors and Executive Officers

Taisho Pharmaceutical's current management structure is comprised of seven directors and eight executive officers. In principle, the Board of Directors meets once a month with extraordinary sessions convened on a needs basis. In addition to meetings of the Board of Directors, other meetings of directors and corporate auditors are regularly held to receive reports from executive officers, business unit managers and other managers relating to business operations, issues and other matters concerning business groups, administrative divisions and other units.

Corporate Auditors

Taisho Pharmaceutical has adopted the corporate auditor system to ensure the transparency of its management. There are currently four corporate auditors, two of whom are from outside the Company. Corporate auditors collectively supervise the management of the Taisho Pharmaceutical Group. When performing their duties, corporate auditors collaborate with administrative units such as the Audit Division, Accounting Division, Legal Division and Compliance Management Section. In addition, corporate auditors attend meetings of the Board of Directors and other important meetings. Corporate auditors also review important documents, receive reports on the

CORPORATE GOVERNANCE STRUCTURE



activities of major business units, accompany the financial auditor on visits to factories, branches and subsidiaries, regularly receive reports from the Audit Department, and confirm that compliance programs, risks management systems and internal rules are functioning properly.

3. Risk Management System

Risk management committees are established within each business unit to manage respective risks associated with overall business activities. From a strategic perspective, risk policy, preventive measures and management are discussed and determined at the representative director level.

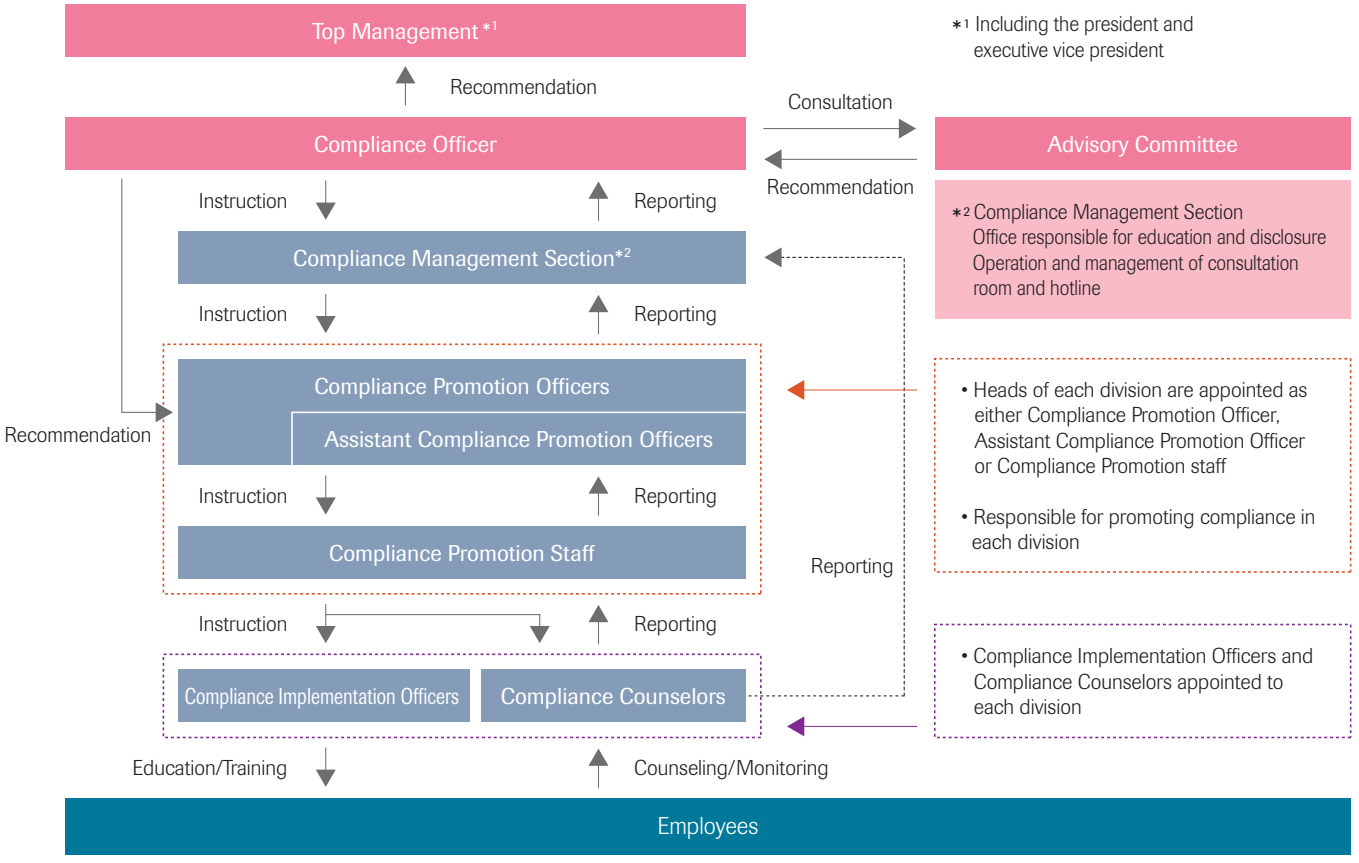
Corporate Social Responsibility

1. Compliance

As a company active in the life science field, Taisho Pharmaceutical has positioned compliance activities as a core platform of its management philosophy. With the aims of ensuring strict adherence to statutory requirements and promoting greater understanding of corporate ethics throughout the Group, Taisho Pharmaceutical formulated its Corporate Code of Conduct in 2001. At the same time, the Company appointed a director as Compliance Officer, responsible for the implementation and operations of the Group's compliance systems, and established the Compliance Management Section. Through these and other means, Taisho Pharmaceutical has worked diligently to inform and educate employees in the critical aspects of compliance.

In addition, all general managers were appointed as compliance promotion officers in an effort to reinforce the Company's monitoring systems and to facilitate the prompt recognition of issues and problems. Taisho Pharmaceutical has endeavored to implement all necessary reforms to ensure a detailed and forward-looking compliance structure focusing on the frontline.

COMPLIANCE FRAMEWORK



2. Quality Assurance

Taisho Pharmaceutical has established the Quality Assurance Head Office in an effort to further promote quality assurance at each stage of its business activities from research and development through manufacture, sales and after-sales service. Among its key roles, the Quality Assurance Head Office is responsible for evaluating the Group's products in terms of their compliance with laws and regulations, determining from a scientific perspective, the level of customer safety assurance to be achieved and maintaining quality assurance and safety management at the post-marketing stage. In addition to the audit of clinical trials and the monitoring of quality assurance at research facilities, the Quality Assurance Head Office also formulates the Group's fundamental quality assurance philosophy and policies and implements plans designed to strengthen Group-wide systems and structures.

3. Social and Environmental Activities

Taisho Pharmaceutical established the Uehara Memorial Foundation in 1985. The Foundation has worked actively to promote advances and to support individuals engaged in research in a variety of fields related to life sciences by hosting international symposiums and providing incentive awards for significant research achievements.

The promotion of self-medication is gaining full-fledged recognition and is increasingly identified as a key health policy issue throughout the world. In Japan, for example, the Self-Medication Advocacy Council (SMAC, a Non-Profit Organization) was founded in May 2002. In basic agreement with its principles and goals, Taisho Pharmaceutical collaborates with SMAC activities.

Recognizing the environment as a key consideration within the Company's activities, Taisho Pharmaceutical formulated its basic environmental policies and action guidelines in fiscal 2001. Based upon these, we have made extensive efforts to conserve resources, reduce CO_2 emissions and cut down on industrial waste.

In fiscal 2002 Taisho Pharmaceutical instituted environmental audits conducted by headquarter organizations. In addition to efforts to reduce environmental risk, we also publish the Environmental and Social Report each year as part of our information disclosure activities. Among the Company's other initiatives, we reduced the weight of 100 mL bottles for our tonics and nutrient drinks by 9% in fiscal 2003, and achieved zero emissions standards at our Omiya, Hanyu and Okayama factories in fiscal 2005.

QUALITY ASSURANCE HEAD OFFICE

- PRODUCT QUALITY ASSURANCE DIVISION
  Quality assurance for pharmaceuticals, quasi-drugs and cosmetics
- PRESCRIPTION DRUG PHARMACOVIGILANCE DIVISION
  Safety of ethical drugs; collection of information on and the evaluation and reporting of the safety of investigational drugs
- SELF MEDICATION PHARMACOVIGILANCE DIVISION
  Safety of over-the-counter drugs, quasi-drugs and cosmetics
- GCP AUDIT SECTION
  Audits to verify GCP conformity of clinical tests in Japan; verification of reliability and suitability of clinical tests outside Japan
- NON-CLINICAL QUALITY ASSURANCE DIVISION
  Reliability of non-clinical tests; reliability of investigational drugs
- QA MANAGEMENT SECTION
  Management of approaches to manufacturing and sales; assurance of reliability from R&D stage through commercialization; administration and management of the Quality Assurance Head Office

Financial Section

Financial Summary

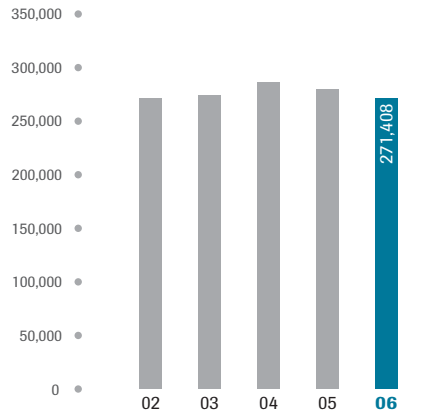
Taisho Pharmaceutical Co., Ltd. and its Consolidated Subsidiaries For the years ended March 31, 2006, 2005, 2004, 2003 and 2002

	Millions of yen				
	2006	2005	2004	2003	2002
For the year:					
Net sales	**¥ 271,408**	¥ 279,437	¥ 286,434	¥ 274,077	¥ 271,397
Cost of sales	**86,687**	84,855	85,006	73,346	70,826
Gross profit	**184,721**	194,582	201,428	200,731	200,571
Selling, general and administrative expenses	**138,325**	139,884	143,728	146,337	139,870
Operating income	**46,396**	54,698	57,700	54,394	60,701
Net income	**35,884**	35,489	40,910	35,392	37,361
At year-end:					
Total assets	**¥ 664,431**	¥ 613,803	¥ 601,956	¥ 577,707	¥ 590,036
Current assets	**271,157**	273,144	254,715	247,589	251,793
Current liabilities	**57,725**	56,345	62,019	46,347	60,156
Working capital	**213,432**	216,800	192,696	201,242	191,637
Shareholders' equity	**567,364**	517,634	500,761	485,717	486,883
R&D expenses	**23,072**	23,221	24,171	29,526	32,212
R&D expenses as a percentage of net sales (%)	**8.5**	8.3	8.4	10.8	11.9
Capital expenditure	**13,397**	7,074	8,829	8,957	24,996
Free cash flows	**21,123**	(9,320)	84,783	63,839	14,199
Per share data:					
Shareholders' equity (yen)	**¥1,840.63**	¥1,678.78	¥1,597.78	¥1,474.65	¥1,434.51
Net income—basic (yen)	**116.18**	114.15	127.87	105.81	109.66
Ratio data:					
Asset turnover (times)	**0.4**	0.5	0.5	0.5	0.5
Tangible fixed assets turnover (times)	**2.8**	2.8	2.8	2.6	2.7
Return on equity—ROE (%)	**6.6**	7.0	8.3	7.3	7.8
Return on assets—ROA (%)	**5.6**	5.8	6.9	6.1	6.4

Graphs of Selected Financial Highlights

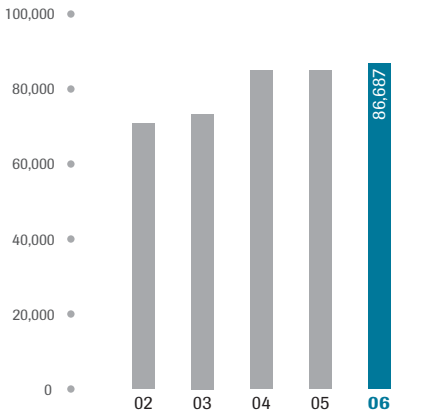
NET SALES

(Millions of Yen)



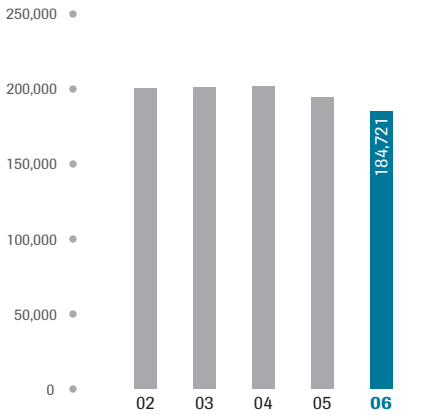
COST OF SALES

(Millions of Yen)



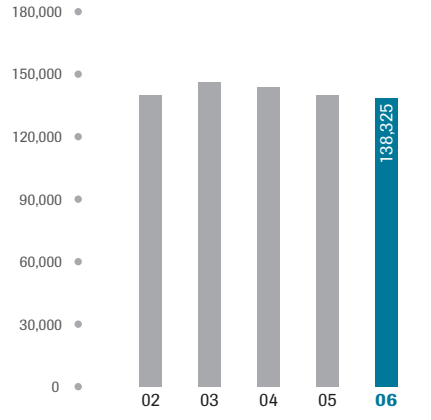
GROSS PROFIT

(Millions of Yen)



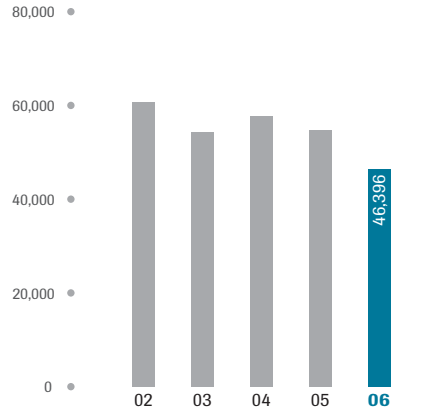
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

(Millions of Yen)



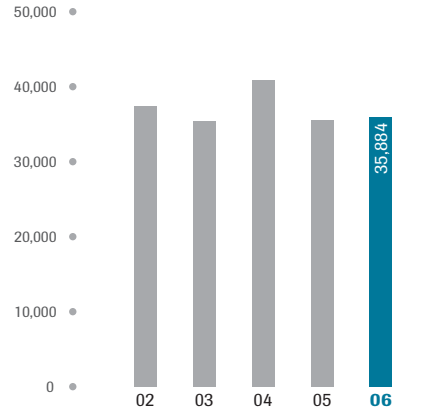
OPERATING INCOME

(Millions of Yen)



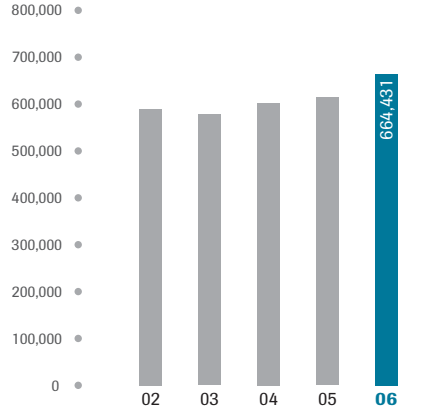
NET INCOME

(Millions of Yen)



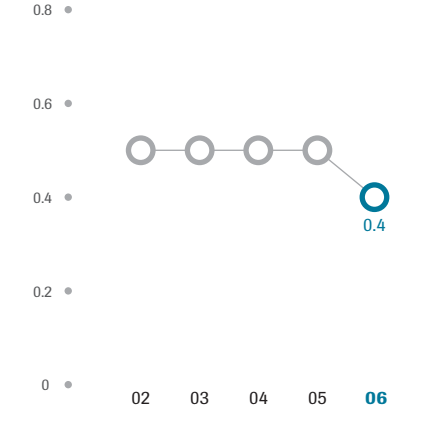
TOTAL ASSETS

(Millions of Yen)



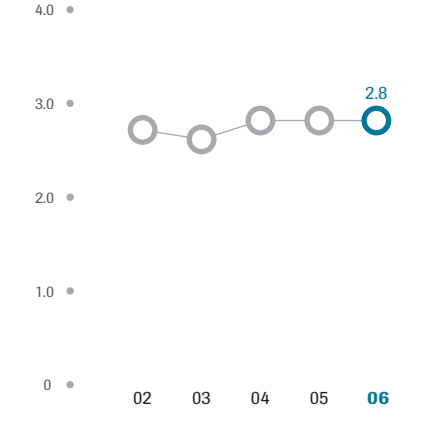
ASSET TURNOVER

(Times)



TANGIBLE FIXED ASSETS TURNOVER

(Times)



Management's Discussion and Analysis

GROUP OVERVIEW

The Taisho Pharmaceutical Group is made up of Taisho Pharmaceutical Co., Ltd. and its 24 subsidiaries and three affiliated companies. Taisho Pharmaceutical is engaged in activities across two broad operating activities, the Self-Medication Operation Group, which entails the manufacture and sale of OTC drugs, food products and miscellaneous goods, and the Prescription Pharmaceutical Operation Group, which encompasses the manufacture and sale of prescription pharmaceuticals.

NET SALES

During fiscal 2005, ended March 31, 2006, consolidated net sales amounted to ¥271.4 billion, a decline of ¥8.0 billion, or 2.9%, compared with the previous fiscal year. The cost of sales margin was 31.8% as increase of 1.5 percentage points year on year. This was attributed to changes in the composition of net sales.

GROSS PROFIT

Gross profit fell ¥9,861 million, or 5.1%, compared with the previous fiscal year to ¥184,721 million.

OPERATING INCOME

Buoyed by efforts to curtail overhead expenses, particularly in the areas of advertising and promotion and personnel expenditure, selling, general and administrative expenses decreased ¥1,559 million, or 1.1%, year on year to ¥138,325 million. As a result, operating income for the period was ¥46,396 million, a drop of ¥8,302 million, or 15.2%, compared with the previous fiscal year. Accounting for these factors, the operating income margin declined 2.5 percentage points to 17.1%.

NET INCOME

Other income rose ¥8,944 million to ¥14,527 million. Major components were interest and dividends, which increased ¥535 million to ¥4,382 million and a gain on sales of investment securities to affiliated company totaling ¥8,496 million absent in the previous fiscal year. In the fiscal year under review, other expenses climbed ¥671 million to ¥2,611 million. As a result, income before income taxes and minority interests amounted to ¥58,312 million, a slight year-on-year decrease of 0.1%. After accounting for current and deferred income taxes and minority interests in loss of consolidated subsidiaries, net income edged up ¥395 million, or 1.1%, year on year to ¥35,884 million. Based on these figures, net income per share was ¥116.18, an increase of ¥2.03, and return on equity was 6.6%, down 0.4 of a percentage point compared with the previous fiscal year.

SEGMENT INFORMATION

Please refer to pages 10 through 13 for details.

LIQUIDITY AND FUNDS PROCUREMENT

FINANCIAL POSITION

Taisho Pharmaceutical's finance policy is based on efforts to ensure an appropriate and prudent level of liquidity and working

Taisho Pharmaceutical Co., Ltd. and its Consolidated Subsidiaries For the years ended March 31

	Millions of yen				
	2006	2005	2004	2003	2002
Net sales	**¥271,408**	¥ 279,437	¥ 286,434	¥ 274,077	¥ 271,397
Cost of sales	**86,687**	84,855	85,006	73,346	70,826
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Selling, general and administrative expenses	**138,325**	139,884	143,728	146,337	139,870
Operating income	**46,396**	54,698	57,700	54,394	60,701
Income before income taxes and minority interests	**58,312**	58,341	69,910	60,269	66,446
Net income	**35,884**	35,489	40,910	35,392	37,361

capital as well as a sound balance sheet. As of March 31, 2006, total assets stood at ¥664,431 million, an increase of ¥50,628 million, or 8.2%, compared with the previous fiscal year-end. Total assets comprised current assets, which edged down ¥1,987 million, or 0.7%, to ¥271,157 million and fixed assets totaling ¥393,274 million, an increase of ¥52,615 million, or 15.4%, year on year. Within current assets, marketable securities declined ¥7,774 million compared with the previous fiscal year-end reflecting the redemption of bonds. Property, plant and equipment, net, climbed ¥2,771 million, or 2.9%, to ¥99,042 million, due to the increase in construction in progress and other factors. This contributed to fixed asset growth. Intangible assets fell ¥2,485 million, or 18.8%, to ¥10,759 million. This was mainly attributed to the amortization of trademark rights. Investment and other assets surged ¥52,329 million, or 22.6%, owing to the acquisition of shares and bonds and an increase in unrealized gains. Total liabilities as of March 31, 2006 totaled ¥94,891 million, a slight increase compared with the end of the previous fiscal year. Current liabilities rose ¥1,380 million, or 2.4%, to ¥57,725 million, while total long-term liabilities declined ¥1,378 million, or 3.6%, to ¥37,166 million. Major component within current liabilities was notes and accounts payable, trade, which climbed ¥1,427 million, or 7.0%. Accrued retirement benefits dropped ¥15,742 million, or 45.6%, impacting total long-term liabilities. As of March 31, 2006, shareholders' equity stood at ¥567,364 million, an increase of ¥49,730 million, or 9.6%. Major components were net unrealized gains on securities, which jumped ¥20,114 million, or 144.2%, and treasury stock, which declined ¥19,695 million.

As a result, the shareholders' equity ratio rose 1.1 percentage points to 85.4%. Shareholders' equity per common share was ¥1,840.63, up ¥161.85.

CASH FLOWS

As of the end of the fiscal year under review, cash and cash equivalents amounted to ¥92,196 million, up ¥14,639 million from the previous fiscal year-end.

Cash flows from operating activities

Net cash provided by operating activities was ¥38,487 million, down ¥4,692 million compared with fiscal 2004. This was mainly attributed to the decrease in reserves for retirement benefits of ¥15,745 million in line with contributions following a change in retirement benefit systems, a turnaround of ¥16,508 million. For the period under review, income taxes paid were ¥20,877 million, down ¥6,608 million compared with the pervious fiscal year. Other major components included depreciation and amortization, which totaled ¥12,809 million, and impairment loss on fixed assets totaling ¥208 million.

Cash flows from investing activities

Net cash used in investing activities amounted to ¥17,364 million, a drop of ¥35,135 million. Major cash outflows comprised payments for purchases of investment securities of ¥61,698 million and payments for purchases of property, plant and equipment of ¥12,122 million. Principal cash inflows were proceeds from sales of investment securities and marketable securities of ¥38,010 million and ¥12,545 million, respectively.

Cash flows from financing activities

In the fiscal year under review, net cash used in financing activities was ¥6,888 million, a decrease of ¥12,494 million compared with fiscal 2004. The major components were payments for purchases of treasury stock of ¥200 million, a significant drop of ¥10,457 million year on year, and payments for cash dividends totaling ¥7,688 million.

BUSINESS AND OTHER RISKS

Of the potential risks encountered by Taisho Pharmaceutical during the course of developing its business activities, those deemed to have the greatest likelihood of occurring are highlighted as follows. Forward-looking statements mentioned in this discussion of risks reflect management's beliefs and judgment as of March 31, 2006.

1. Legal risks and risks related to healthcare policy

Taisho Pharmaceutical's operations are subject to laws and regulations governing pharmaceutical affairs. A number of different approval and permission systems exist at each stage of pharmaceutical operations, including development, manufacturing, import and distribution. Consequently, there is a risk that Taisho Pharmaceutical's products could fail to conform to regulations at one of these stages, or that a previously granted approval could be revoked. Depending on trends in healthcare policy, health insurance systems and other changes, Taisho Pharmaceutical may also face the risk of a decline in pharmaceutical prices, among other risks.

2. Risks involving pharmaceutical quality, side effects and other issues

Taisho Pharmaceutical does its utmost to guarantee the reliability and quality of its products. Nevertheless, unanticipated side effects, accidents and other factors could force Taisho Pharmaceutical to recall or halt the sales of the products affected or incur claims for damages.

3. Risks involving pharmaceutical development and commercialization

The development of pharmaceuticals is a lengthy process and requires a substantial amount of capital investment. There is uncertainty concerning the possibility of successfully launching products and businesses.

4. Risks involving the proper protection of intellectual property rights

If Taisho Pharmaceutical cannot properly protect its intellectual property rights, there is the risk that a third party might use Taisho Pharmaceutical's technology and other intellectual property and undermine the Company's competitiveness in the market. Similarly, there is also the risk that Taisho Pharmaceutical might encroach on the intellectual property rights of third parties.

5. Risks related to expiration of patents

Although Taisho Pharmaceutical strives to extend product life cycles, sales could be negatively impacted, for example, by the emergence of generic drugs or the switch to over-the-counter drugs produced following the expiration of patents.

Taisho Pharmaceutical Co., Ltd. and its Consolidated Subsidiaries For the years ended March 31

	Millions of yen				
	2006	2005	2004	2003	2002
Sales:					
Self-Medication Operation Group:	**¥174,832**	¥ 183,417	¥ 188,063	¥ 195,125	¥ 192,428
OTC products, etc.	**163,866**	172,404	178,233	185,233	183,492
Foods for Specified Health Use etc.	**8,140**	7,840	7,876	8,535	7,389
Others	**2,825**	3,172	1,953	1,357	1,547
Prescription Pharmaceutical Operation Group:	**96,576**	96,020	98,371	78,952	78,969
Ethical drugs	**81,779**	81,688	82,129	61,637	62,547
Others	**11,686**	9,391	10,631	10,994	9,647
Royalty income	**3,111**	4,941	5,611	6,321	6,775
Operating income:					
Self-Medication Operation Group	**¥ 33,603**	¥ 39,015	¥ 43,392	¥ 50,412	¥ 53,216
Prescription Pharmaceutical Operation Group	**12,793**	15,683	14,308	3,982	7,485
Identifiable assets:					
Self-Medication Operation Group	**¥232,502**	¥ 225,638	¥ 257,285	¥ 267,434	¥ 262,978
Prescription Pharmaceutical Operation Group	**115,499**	119,140	119,801	117,176	102,082
Depreciation:					
Self-Medication Operation Group	**¥ 9,336**	¥ 10,104	¥ 11,133	¥ 12,455	¥ 9,573
Prescription Pharmaceutical Operation Group	**3,473**	3,398	4,210	4,377	4,616
Capital expenditure:					
Self-Medication Operation Group	**¥ 9,291**	¥ 6,178	¥ 7,050	¥ 13,463	¥ 18,811
Prescription Pharmaceutical Operation Group	**4,461**	1,414	2,107	3,436	6,823

6. Risks from lawsuits

Taisho Pharmaceutical faces the possibility of lawsuits during the course of its business activities related to product liability, environmental issues and other matters.

7. Risks from fluctuations in foreign exchange rates

Fluctuations in foreign currency exchange rates could affect royalties denominated in foreign currencies received from outside Japan, commercial transactions and other factors, thus impacting Taisho Pharmaceutical's operating results.

8. Other risks

Any deterioration in sociopolitical stability overseas could cause Taisho Pharmaceutical suffer damage, such as the destruction of overseas business sites, or downsizing or withdrawal from its businesses. In addition, there are various other risks, including the risk of dependency on the license of products developed by other companies. Please note, therefore, that the aforementioned risks do not cover all of the potential risks encountered by Taisho Pharmaceutical.

BASIC EARNINGS DISTRIBUTION POLICY

Taisho Pharmaceutical has continued to adopt the policy of consistently delivering a high level of dividends over the long term. At the same time, the Company strives to secure retained earnings growth in an effort to fortify its corporate structure. These retained earnings are appropriated for investment that will

Taisho Pharmaceutical Co., Ltd. and its Consolidated Subsidiaries For the years ended March 31

	Millions of yen				
	2006	2005	2004	2003	2002
Net cash provided by operating activities	**¥ 38,487**	¥ 43,179	¥ 57,529	¥ 53,420	¥ 44,654
Net cash provided by (used in) investing activities	**(17,364)**	(52,499)	27,254	10,419	(30,455)
Net cash used in financing activities	**(6,888)**	(19,382)	(39,651)	(27,613)	(11,480)
Cash and cash equivalents at the beginning of the year	**77,557**	106,802	62,126	26,064	22,864
Cash and cash equivalents at the end of the year	**92,196**	77,557	106,802	62,126	26,064

Taisho Pharmaceutical Co., Ltd. and its Consolidated Subsidiaries As of March 31

	Millions of yen				
	2006	2005	2004	2003	2002
Cash and cash equivalents	**¥ 92,196**	¥ 77,557	¥ 106,802	¥ 62,126	¥ 26,064
Time deposits	**63,170**	69,748	31,570	54,142	89,926
Inventories	**23,613**	22,905	21,709	18,580	19,296
Total current assets	**271,157**	273,144	254,715	247,589	251,793
Investment securities	**276,614**	215,786	214,058	179,102	197,304
Property, plant and equipment, net	**99,042**	96,271	100,710	102,720	107,775
Intangible assets	**10,759**	13,244	15,707	17,839	14,308
Total intangible assets and other assets	**17,618**	28,602	32,473	48,296	33,164
Total assets	**¥ 664,431**	¥ 613,803	¥ 601,956	¥ 577,707	¥ 590,036
Common stock	**¥ 29,804**	¥ 29,804	¥ 29,804	¥ 29,804	¥ 29,804
Additional paid-in capital	**14,935**	14,935	14,935	14,935	14,935
Treasury stock	**(23,253)**	(42,948)	(51,234)	(22,756)	(3,447)
Total shareholders' equity	**567,364**	517,634	500,761	485,717	486,883
Total liabilities and shareholders' equity	**¥ 664,431**	¥ 613,803	¥ 601,956	¥ 577,707	¥ 590,036

strengthen the Company's foundations, including R&D, capital investment, and new business development. This fundamental policy regarding retained earnings has not changed. From the fiscal year ended March 31, 2006, however, Taisho Pharmaceutical has decided to pursue a dividend policy pegged to non-consolidated operating results for each business term. The goal is to achieve a dividend payout ratio of 30% of net income, excluding extraordinary gains. As a result, the Company paid a full-year dividend of ¥30 per share, an increase of ¥5 year on year, for fiscal 2005.

Furthermore, as a part of Taisho Pharmaceutical's strategy to return profits to shareholders, the Company also cancelled 10.5 million shares of treasury stock.

CAPITAL EXPENDITURE

In its ongoing efforts to expand business operations, the Group undertook capital expenditure totaling ¥13,397 million. The principal components were ¥4,617 million to fund the construction of a liquid formulation pharmaceutical facility at the Company's Omiya Factory, ¥2,086 million for improvements to the Okayama Factory and ¥1,338 million for the construction of a business office in Yokohama. In the fiscal year under review, there was no material impact to the Company's production capacity following sales or disposal of property, plant and equipment.

MAJOR EVENTS, STRATEGIES AND OUTLOOK

KEY ISSUES CONFRONTED IN FISCAL 2005 AND FUTURE MANAGEMENT POLICY

Looking ahead, increasingly harsh operating conditions are forecast for Taisho Pharmaceutical's business environment. Against this backdrop, the Company is adopting strategic and proactive measures to expand in the self-medication business, including OTC drugs and health-related products, and reinforce activities in its prescription pharmaceutical and related businesses. In the self-medication field, Taisho Pharmaceutical is focusing on providing a comprehensive range of products that best fit consumer needs, including health management, illness prevention, early detection, prompt treatment, and the treatment of minor and other ailments. Leveraging the fruits of its extensive research and expertise accumulated over a lengthy period in the prescription pharmaceuticals field, the Company is also endeavoring to develop new products that boast a high degree of safety and efficacy. In an effort to revitalize a contracting OTC drugs market, industry players are working diligently to review existing systems and approval procedures. At the same time, Taisho Pharmaceutical is concentrating on the development and release of new products in accord with system revisions and switch-OTC drugs. In addition, the Company is launching new FOSHU and other products in markets that are showing initial signs of expansion. To complement the release of new products, the Company is also developing new sales channels, and fostering and strengthening product brands. Collectively these efforts are aimed at securing a position as the preferred choice of consumers through an appealing package of products and sales. Guided by these policies and in an effort to maximize synergies among research and development, marketing and sales organizations, Taisho Pharmaceutical is pursuing strategic capital and business tie-ups with select third parties. In this context, the Company executed a capital and business collaboration agreement with Yomeishu Seizo Co., Ltd. in July 2005. Under this agreement, the Company acquired a 20% equity holding in Yomeishu Seizo Co., Ltd. through successive purchases up to April 18, 2006. In addition, Taisho Pharmaceutical established a joint-venture company with Toyo Shinyaku Co., Ltd. to engage in the research and development of FOSHU and other products in September 2005. Furthermore, the Company commenced steps for a mail order and direct sales health and beauty business in March 2006.

In the prescription pharmaceutical business fields, Taisho Pharmaceutical is focusing on enhancing efficiencies in business development. To this end, the Company is bolstering research and development efforts in innovative new drugs capable of competing on the world stage and the selection of strategic partners to ensure a leading position in the global market. In an effort to increase sales efficacy, Taisho Pharmaceutical is upgrading its marketing organization and boosting business alliances. As a part of these efforts, the Company established Taisho Toyama Pharmaceutical Co., Ltd. (equity ownership 55%) in the prescription pharmaceutical business together with Toyama Chemical Co., Ltd. Operating as a sales company in Japan, Taisho Toyama Pharmaceutical was first comprised of Medical Representatives and staff appointed from both Taisho Pharmaceutical and Toyama Chemical. In April 2005, workers on assignment were asked to join the new company on a permanent basis to ensure a uniform compensation and appraisal system. Working under this structure, Taisho Pharmaceutical will work to further enhance sales efficacy in the prescription pharmaceutical business.

Overseas, the Company is focusing on its nutrient drink business as the means to establish a leading position in global markets. To this end, Taisho Pharmaceutical is striving to reinforce its business platform in Asia and to cultivate business in Europe and the United States.

FISCAL 2006 OUTLOOK

Self-Medication Operation Group

In the fiscal year ending March 31, 2007, sales in the Self-Medication Operation Group are forecast to decline slightly to ¥173,400 million, a nominal decrease of 0.8% year on year. Despite continued contraction in the OTC drugs market and an expected impact on sales, Taisho Pharmaceutical will work diligently to secure a positive turnaround through the cultivation of new products and efforts to strengthen sale and marketing systems and structures. Full-year sales in this category are estimated to reach ¥161,400 million. In nutrient drinks, sales of the *Lipovitan* series are forecast to decline to ¥88,300 million. Sales of the *Pabron* series are expected to reach ¥26,300 million, while sales of the *RiUP* series will fall to ¥11,700 million. Expectations in the FOSHU category are high, with sales estimated to climb to ¥9,100 million. This is mainly attributed to anticipated contributions from increased sales of products with efficacy for people with metabolic syndrome, including products in the mainstay *Livita* series, as well as multiple categories of new products. Overseas, sales of nutrient drinks, particularly in Asia are expected to remain high.

Prescription Pharmaceutical Operation Group

Sales estimates in the Prescription Pharmaceutical Operation Group indicate a year-on-year drop of 3.2% to ¥79,200 million. While sales of ethical drugs will be impacted by the decline in pharmaceutical prices (an average decline of 6.5% for Taisho Toyama products), and the release of generic *Clarith* products, difficult conditions will be offset by sales of an improved *Clarith Dry Syrup for Pediatric* use and marketing efforts that will include measures to ensure increased acceptance of *Sumilu*, launched in 2005. For the fiscal year ending March 31, 2007, Taisho Pharmaceutical is planning full-year sales of *Clarith* and *Palux injection* of ¥27,300 million and ¥11,200 million, respectively. In addition, sales of Toyama Chemical's *PENTCILLIN* and *OZEX* are budgeted to decline. Accordingly, sales of *PENTCILLIN* are estimated at ¥6,400 million with sales of *OZEX* at ¥3,300 million.

In the Others category, sales for the full year are forecast at ¥10,400 million. Looking at its royalty income, the Company is estimating revenues of ¥1,000 million. This significant decline is attributed to the termination of royalty payments from Abbott Laboratories of the U.S.

On the earnings front, and in line with the aforementioned sales conditions, Taisho Pharmaceutical will make every effort to review its cost structure. On this basis, net income is forecast to total ¥29,000 million.

HUMAN RESOURCES

The total number of employees as of March 31, 2006 was 5,191, with the Self-Medication Operation Group accounting for 2,187 employees, the Prescription Pharmaceutical Operation Group accounting for 1,777 employees and 1,227 employees engaged in Group-wide operations.

Breakdown of Capital Expenditure

Taisho Pharmaceutical Co., Ltd. and its Consolidated Subsidiaries For the years ended March 31

	Millions of yen			
	2004	2005	**2006**	2007 (estimated)
Omiya Factory	¥ 1,521	¥ 792	**¥ 6,605**	¥ 7,000
Hanyu Factory	136	144	**195**	100
Okayama Factory	175	46	**1,860**	200
Research Center	1,218	1,958	**1,120**	1,200
Other	5,779	4,134	**3,617**	2,300
Total Capital Expenditure	¥ 8,829	¥ 7,074	**¥13,397**	¥10,800

Consolidated Balance Sheets

Taisho Pharmaceutical Co., Ltd. and its Consolidated Subsidiaries As of March 31, 2006 and 2005

	Millions of yen		Thousands of U.S. dollars (Note 3)
ASSETS	**2006**	2005	**2006**
Current assets:			
Cash and cash equivalents (Note 5)	**¥155,205**	¥147,205	**$1,321,231**
Marketable securities (Note 5 and Note 6)	**3,493**	11,267	**29,732**
Notes and accounts receivable, trade	**76,719**	78,920	**653,093**
Allowance for doubtful accounts	**(561)**	(631)	**(4,777)**
Inventories	**23,613**	22,905	**201,011**
Deferred income taxes (Note 11)	**8,160**	8,132	**69,465**
Other current assets (Note 4)	**4,528**	5,286	**38,552**
Total current assets	**271,157**	273,144	**2,308,307**
Investment securities (Note 6)	**276,614**	215,786	**2,354,764**
Property, plant and equipment, net (Note 7)	**99,042**	96,271	**843,126**
Intangible assets and other assets:			
Intangible assets	**10,759**	13,244	**91,585**
Deferred income taxes (Note 11)	**723**	8,695	**6,158**
Other assets	**6,136**	6,663	**52,240**
Total intangible assets and other assets	**17,618**	28,602	**149,983**
Total assets (Note 17)	**¥664,431**	¥613,803	**$5,656,180**

The accompanying notes are an integral part of these statements.

LIABILITIES AND SHAREHOLDERS' EQUITY	Millions of yen 2006	2005	Thousands of U.S. dollars (Note 3) 2006
Current liabilities:			
Short-term loans (Note 8)	**¥ 260**	¥ 205	**$ 2,213**
Notes and accounts payable, trade (Note 4)	**21,798**	20,371	**185,563**
Accrued income taxes (Note 11)	**7,237**	9,487	**61,611**
Accrued expenses	**7,875**	8,387	**67,039**
Other current liabilities (Note 11)	**20,555**	17,895	**174,974**
Total current liabilities	**57,725**	56,345	**491,400**
Long-term liabilities:			
Accrued retirement benefits (Note 9)	**18,764**	34,506	**159,733**
Deferred income taxes (Note 11)	**9,473**	27	**80,645**
Other long-term liabilities	**8,929**	4,011	**76,005**
Total long-term liabilities	**37,166**	38,544	**316,383**
Minority interests in consolidated subsidiaries	**2,176**	1,280	**18,528**
Shareholders' equity:			
Common stock:			
Authorized—			
2006: 1,174,959 thousand shares			
2005: 1,185,459 thousand shares			
Issued—			
2006: 320,465 thousand shares			
2005: 330,965 thousand shares	**29,804**	29,804	**253,720**
Additional paid-in capital	**14,935**	14,935	**127,140**
Retained earnings (Note 10)	**515,007**	506,798	**4,384,157**
Net unrealized gains on securities (Note 6)	**34,065**	13,951	**289,991**
Foreign currency translation adjustment	**(3,194)**	(4,906)	**(27,186)**
Treasury stock (Note 2-(14))			
(2006: 12,260,749 shares, 2005: 22,669,229 shares)	**(23,253)**	(42,948)	**(197,953)**
Total shareholders' equity	**567,364**	517,634	**4,829,869**
Commitments and contingent liabilities (Note 14 and Note 16)			
Total liabilities and shareholders' equity	**¥664,431**	¥613,803	**$5,656,180**

Consolidated Statements of Income

Taisho Pharmaceutical Co., Ltd. and its Consolidated Subsidiaries For the years ended March 31, 2006 and 2005

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2006	2005	2006
Net sales (Note 17)	¥271,408	¥279,437	$2,310,444
Cost of sales (Note 4 and Note 17)	86,687	84,855	737,951
Gross profit	184,721	194,582	1,572,493
Selling, general and administrative expenses (Note 12 and Note 17)	138,325	139,884	1,177,536
Operating income (Note 17)	46,396	54,698	394,957
Other income:			
Interest and dividends	4,382	3,847	37,305
Other (Note 4 and Note 13)	10,145	1,736	86,359
	14,527	5,583	123,664
Other expenses:			
Interest	5	5	40
Other (Note 13)	2,606	1,935	22,184
	2,611	1,940	22,224
Income before income taxes and minority interests	58,312	58,341	496,397
Income taxes (Note 11)	22,517	22,625	191,680
Income before minority interests	35,795	35,716	304,717
Minority interests in gain or (loss) of consolidated subsidiaries	(89)	227	(758)
Net income	¥ 35,884	¥ 35,489	$ 305,475

	Yen		U.S. dollars (Note 3)
	2006	2005	2006
Per share: (Note 2-(12)):			
Net income —Basic	¥ 116.18	¥ 114.15	$ 0.99
—Diluted	—	—	—
Cash dividends	30.00	25.00	0.26

The accompanying notes are an integral part of these statements.

Consolidated Statements of Shareholders' Equity

Taisho Pharmaceutical Co., Ltd. and its Consolidated Subsidiaries For the years ended March 31, 2006 and 2005

	Millions of yen							
	Number of shares	Common stock	Additional paid-in capital	Retained earnings	Net unrealized gains on securities	Foreign currency translation adjustment	Treasury stock	Comprehensive income
Balance as of March 31, 2004	340,965,510	¥29,804	¥14,935	¥498,173	¥13,852	¥(4,769)	¥(51,234)	
Dividends paid	—	—	—	(7,834)	—	—	—	
Bonuses to directors and corporate auditors	—	—	—	(87)	—	—	—	
Purchase of treasury stock	—	—	—	—	—	—	(10,657)	
Cancellation of treasury stock	(10,000,000)	—	—	(18,943)	—	—	18,943	
Net income	—	—	—	35,489	—	—	—	¥35,489
Unrealized gains on securities	—	—	—	—	99	—	—	99
Currency translation adjustment	—	—	—	—	—	(137)	—	(137)
Balance as of March 31, 2005	330,965,510	29,804	14,935	506,798	13,951	(4,906)	(42,948)	¥35,451
Dividends paid	**—**	**—**	**—**	**(7,707)**	**—**	**—**	**—**	
Bonuses to directors and corporate auditors	**—**	**—**	**—**	**(73)**	**—**	**—**	**—**	
Purchase of treasury stock	**—**	**—**	**—**	**—**	**—**	**—**	**(200)**	
Cancellation of treasury stock	**(10,500,000)**	**—**	**—**	**(19,895)**	**—**	**—**	**19,895**	
Net income	**—**	**—**	**—**	**35,884**	**—**	**—**	**—**	**¥35,884**
Unrealized gains on securities	**—**	**—**	**—**	**—**	**20,114**	**—**	**—**	**20,114**
Currency translation adjustment	**—**	**—**	**—**	**—**	**—**	**1,712**	**—**	**1,712**
Balance as of March 31, 2006	**320,465,510**	**¥29,804**	**¥14,935**	**¥515,007**	**¥34,065**	**¥(3,194)**	**¥(23,253)**	**¥57,710**

	Thousands of U.S. dollars (Note 3)						
	Common stock	Additional paid-in capital	Retained earnings	Net unrealized gains on securities	Foreign currency translation adjustment	Treasury stock	Comprehensive income
Balance as of March 31, 2005	$253,720	$127,140	$4,314,277	$118,763	$(41,763)	$(365,611)	
Dividends paid	**—**	**—**	**(65,612)**	**—**	**—**	**—**	
Bonuses to directors and corporate auditors	**—**	**—**	**(621)**	**—**	**—**	**—**	
Purchase of treasury stock	**—**	**—**	**—**	**—**	**—**	**(1,704)**	
Cancellation of treasury stock	**—**	**—**	**(169,362)**	**—**	**—**	**169,362**	
Net income	**—**	**—**	**305,475**	**—**	**—**	**—**	**$305,475**
Unrealized gains on securities	**—**	**—**	**—**	**171,228**	**—**	**—**	**171,228**
Currency translation adjustment	**—**	**—**	**—**	**—**	**14,577**	**—**	**14,577**
Balance as of March 31, 2006	**$253,720**	**$127,140**	**$4,384,157**	**$289,991**	**$(27,186)**	**$(197,953)**	**$491,280**

The accompanying notes are an integral part of these statements.

Consolidated Statements of Cash Flows

Taisho Pharmaceutical Co., Ltd. and its Consolidated Subsidiaries For the years ended March 31, 2006 and 2005

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2006	2005	2006
Cash flows from operating activities:			
Income before income taxes and minority interests	¥ 58,312	¥ 58,341	$ 496,397
Adjustments:			
Depreciation and amortization (Note 17)	12,809	13,502	109,045
Impairment loss on fixed assets	208	—	1,773
Interest and dividend income	(4,382)	(3,847)	(37,305)
Interest expenses	5	5	40
Gains from sales of investment securities	(8,591)	(40)	(73,137)
Loss on devaluation of investment securities	—	73	—
Gains from sales of property, plant and equipment	(3)	(24)	(29)
Loss on disposal of property, plant and equipment, net	575	319	4,892
Increase (decrease) in accrued retirement benefits	(15,745)	763	(134,031)
Increase in accrued directors' retirement benefits	63	26	534
Amortization of goodwill	18	22	157
Equity in net earnings of affiliated companies	638	650	5,431
Decrease (increase) in notes and accounts receivable, trade	2,290	(3,181)	19,494
Increase in inventories	(659)	(1,206)	(5,610)
Increase (decrease) in notes and accounts payable, trade	1,385	(794)	11,792
Increase in long-term liabilities	5,075	—	43,204
Other, net	3,055	2,110	26,009
	55,053	66,719	468,656
Interest and dividend income received	4,316	3,950	36,744
Interest paid	(5)	(5)	(40)
Income taxes paid	(20,877)	(27,485)	(177,726)
Net cash provided by operating activities	38,487	43,179	327,634
Cash flows from investing activities:			
Increase (decrease) in time deposits	6,768	(38,178)	57,614
Proceeds from sale/redemption of marketable securities	12,545	5,585	106,796
Payments for purchases of property, plant and equipment	(12,122)	(6,881)	(103,190)
Proceeds from sales of property, plant and equipment	694	805	5,905
Payments for purchases of intangible assets	(1,285)	(2,252)	(10,942)
Proceeds from sales of intangible assets	6	6	48
Payments for purchases of investment securities	(61,698)	(15,961)	(525,225)
Proceeds from sales of investment securities	38,010	3,073	323,569
Payments for long-term prepaid expenses	(331)	(362)	(2,814)
Other, net	49	1,666	418
Net cash used in investing activities	(17,364)	(52,499)	(147,821)
Cash flows from financing activities:			
Proceeds from short-term loans	345	335	2,937
Repayment of short-term loans	(290)	(395)	(2,469)
Issuance of common stock to minority shareholders	945	—	8,045
Cash dividends	(7,688)	(7,820)	(65,445)
Payments for purchases of treasury stock	(200)	(10,657)	(1,704)
Other, net	0	(845)	(2)
Net cash used in financing activities	(6,888)	(19,382)	(58,638)
Effect of exchange rate changes on cash and cash equivalents	404	(543)	3,437
Net increase (decrease) in cash and cash equivalents	14,639	(29,245)	124,612
Cash and cash equivalents at the beginning of the year	77,557	106,802	660,232
Cash and cash equivalents at the end of the year (Note 5)	¥ 92,196	¥ 77,557	$ 784,844

The accompanying notes are an integral part of these statements.

Notes to Consolidated Financial Statements

Taisho Pharmaceutical Co., Ltd. and its Consolidated Subsidiaries

1. BASIS OF PRESENTING THE CONSOLIDATED FINANCIAL STATEMENTS:

The accompanying consolidated financial statements of Taisho Pharmaceutical Co., Ltd. (the "Company") and its domestic and foreign subsidiaries (together, the "Companies") are basically English versions of those which have been filed with the Ministry of Finance and prepared in accordance with accounting principles and practices generally accepted in Japan, which are different in certain respects as to application and disclosure requirements from International Financial Reporting Standards. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements as well as reported amounts of revenues and expenses during the reporting periods.

The accompanying consolidated financial statements incorporate certain reclassifications and rearrangements in order to present these statements in a form which is more familiar to the readers of these statements outside Japan. In addition, the notes to the consolidated financial statements include information that is not required under generally accepted accounting principles and practices in Japan but is presented herein as additional information.

The figures shown in the consolidated financial statements have been rounded to the nearest million yen.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

(1) Consolidation and investments in affiliates

The consolidated financial statements include the accounts of the Company and all subsidiaries which the Company has the ability to control and in which it can exercise significant influence over operating and financial policies.

TAISHO ACTIVE HEALTH Co., Ltd., which is a 55% owned subsidiary of the Company and a 45% owned affiliate of Toyo Shinyaku Co., Ltd., was established in September 2005, and its accounts have been included in the 2006 consolidation.

All significant intercompany transactions and accounts and unrealized intercompany profits are eliminated on consolidation. All the consolidated subsidiaries, except for Taisho Toyama Pharmaceutical Co., Ltd., Mejiro Real Estate Co., Ltd., Shimoda Central Co., Ltd., and TAISHO ACTIVE HEALTH Co., Ltd. are included in the consolidated accounts with their accounts closed for their fiscal years ended December 31, 2005 and 2004, while the accounts of the four subsidiaries above are consolidated with their respective financial statements for the fiscal years ended March 31, 2006 and 2005. Material differences in intercompany transactions and accounts arising from the use of the different fiscal year-ends are appropriately adjusted for on consolidation.

Investments in 50% or less owned companies, over which the parent company does not have control, but has the ability to exercise significant influence, are accounted for by the equity method. The excess of the cost over the underlying net equity of investments in affiliates accounted for on an equity basis is deferred and amortized over the period in which future benefit of investments is estimated to continue. Consolidated net income includes the Company's equity in the current earnings of these equity companies after the elimination of unrealized intercompany profits.

Sanofi-Synthelabo-Taisho Pharmaceuticals Co., Ltd., established as a joint investment by the Company (49% investment in common shares) and Sanofi-Synthelabo (51% investment in common shares) was renamed Sanofi-Aventis-Taisho Pharmaceuticals Co., Ltd., on January 1, 2006. The Company sold its all stocks of Sanofi-Aventis-Taisho Pharmaceuticals Co., Ltd., on March 31, 2006, and it will be excluded from fiscal 2006 from the scope of affiliated companies, accounted for by the equity method.

The Company has purchased additional shares of Yomeishu Seizo Co., Ltd. in April 2006 and currently holds over 20%. As a result, it will be accounted for by equity method in the following fiscal years.

(2) Foreign currency translation

Foreign currency transactions are translated using foreign exchange rates prevailing at the transaction dates.

All monetary assets and liabilities denominated in foreign currencies, whether they are long term or short term, are translated into Japanese yen at the exchange rates prevailing at the balance sheet date. Resulting gains and losses are included in net profit or loss for the period.

All assets and liabilities of foreign subsidiaries and affiliates are translated at current rates at the respective balance sheet dates and all the income and expense accounts are translated at average rates for respective periods. Foreign currency translation adjustments are presented as a component of shareholders' equity in the consolidated financial statements.

(3) Financial instruments

a) Derivatives:

All derivatives are stated at fair value, with changes in fair value included in net profit or loss for the period in which they arise, except for derivatives that are designated as "hedging instruments."

b) Securities:

Securities held by the Company and its subsidiaries are classified into four categories.

Trading securities are stated at fair value, with changes in fair value included in net profit or loss for the period in which they arise.

Held-to-maturity debt securities are stated at cost after accounting for any premium or discount on acquisition, which is amortized over the period to maturity.

Investments of the Company in equity securities of non-consolidated subsidiaries and affiliates are accounted for by the equity method.

Other securities for which market quotations are available are stated at fair value. Net unrealized gains or losses on these securities are reported as a separate item in the shareholders' equity at a net-of-tax amount. Other securities for which market quotations are unavailable are stated at cost.

When the fair value of held-to-maturity debt securities or other securities has declined significantly and such impairment of the value is not deemed temporary, those securities are written down to the fair value and the resulting losses are included in net profit or loss for the period.

Trading securities and debt securities due within one year are presented as "current assets" and all other securities are presented as "investment securities."

Subscriptions to investment funds that are included in other investment securities are accounted for by the equity method on the basis of recent statements of earnings.

c) Hedge accounting:

Gains or losses arising from changes in the fair value of derivatives designated as "hedging instruments" are deferred as an asset or liability and included in net profit or loss in the same period in which the gains or losses on the hedged items or transactions are recognized.

Derivatives designated as hedging instruments by the Company are principally forward exchange and interest swap contracts. A hedged item is an asset, liability, firm commitment, or forecasted future transaction that exposes the enterprise to the risk of changes in fair value or changes in future cash flows and that, for hedge accounting purposes, is designated as being hedged.

The Company has a policy to utilize the above hedging instruments in order to reduce the Company's exposure to the risk of exchange and interest rate fluctuations. Thus, the Company's purchases of the hedging instruments are limited to, at maximum, the amounts of the hedged items.

The Company evaluates the effectiveness of its hedging activities by

reference to the accumulated gains or losses on the hedging instruments and the related hedged items from the commencement of the hedges.

(4) Allowance for doubtful accounts

An allowance for doubtful accounts is provided for estimated future losses based on past experience, and based on assessment of the collectability of individual receivables.

(5) Inventories

Inventories held by the Company are stated at cost, which is determined by the average method.

(6) Property, plant and equipment

Property, plant and equipment, including significant renewals and improvements, are capitalized at cost. Maintenance and repairs and minor renewals and betterments are charged to income. Depreciation is computed primarily using the declining-balance method at rates based on the estimated useful lives of the assets. In the case of retirement or disposal, the difference between the net book value and salvage or sales proceeds is charged or credited to income.

(7) Retirement benefits and pension plans

The lump-sum severance indemnity regulations of the Companies, which cover substantially all employees, provide for benefit payments determined by reference to each employee's current basic rate of pay, length of service period, qualification, evaluation and managerial post. Effective from April 1, 2005, the commencement of payment of employees' retirement benefit was changed from 55 to 60years old.

The accrued retirement benefits represent the actuarially calculated present value of projected benefit obligation in excess of the fair value of the plan assets except for, as permitted under the standard, the unrecognized actuarial differences and the unrecognized prior service cost which are amortized on a straight-line basis over the period of fifteen to seventeen years; that is, within the average remaining service period of employees. The unrecognized actuarial differences are amortized from the beginning of the subsequent year, while the unrecognized prior year service costs are amortized from the year in which they arise.

On July 1, 2005, a part of the lump-sum severance indemnity plan was transferred to the defined contribution pension plans. The settlement of the retirement benefit obligation resulting from the termination of defined benefit plan was accounted for by applying "Practical Guidelines for Accounting for Transition between Retirement Benefit Plans" (Financial Accounting Standards Implementation Guideline No. 1). The effect on the accounts by 759 million yen ($6,463 thousand) is presented, as "Gain on the settlement of defined benefit pension plan" in other income.

(8) Revenue recognition

Sales are generally recognized at the time the goods are delivered to customers.

(9) Finance leases

Finance leases, other than those where ownership of the lease assets is transferred to the lessee, are accounted for as operating leases.

(10) Income taxes

The provision for income taxes is computed based on the pre-tax income included in the consolidated statements of income. The asset and liability approach is used to recognize deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the reported amounts and the tax bases of assets and liabilities. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized.

(11) Appropriation of retained earnings

The appropriation of retained earnings reflected in the accompanying consolidated financial statements has been recorded after approval by the shareholders, as required both under the former Japanese Commercial Code and the new Corporation Law.

(12) Earnings per share information

The computation of net income and cash dividends per share is based on the weighted-average number of shares outstanding, excluding treasury stock during each period.

(13) Cash equivalents

For the purpose of the statement of cash flows, all highly liquid investments which are readily convertible into cash and/or which mature within three months or less are considered to be cash equivalents.

(14) Treasury stock

Treasury stock is stated at cost as a separate component of shareholders' equity in the accompanying consolidated balance sheets. Net gains on the resale of treasury stock are presented as additional paid-in capital in shareholders' equity in the accompanying consolidated balance sheets.

The Company retired 10,000 thousand shares of treasury stock on February 15, 2005 based on a resolution by board of directors on February 15, 2005. Consequently, the number of authorized shares of common stock is 1,185,459 thousand shares and that of issued common stock is 330,965 thousand shares as at March 31, 2005.

The board of directors resolved retirement of 10,500 thousand shares of treasury stock on May 24, 2005 and the Company cancelled 10,500 thousand treasury stocks on June 7, 2005. Accordingly, the amount of authorized common stock and the amount of issued common stock is 1,174,959 thousand shares and 320,465 thousand shares at March 31, 2006, respectively.

(15) Impairment of fixed assets

On August 9, 2002, the Business Accounting Council of Japan issued a new accounting standard entitled "Statement of Opinion on the Establishment of Accounting Standards for Impairment of Fixed Assets." Further, on October 31, 2003, the Accounting Standards Board of Japan issued Financial Accounting Standards Implementation Guidance No. 6 – "Application Guidance on Accounting Standards for Impairment of Fixed Assets." These standards are effective from fiscal years beginning April 1, 2005.

The Company adopted these standards in the fiscal year ended March 31, 2006. As a result, the Company charged impairment loss related to property, plant and equipment to income amounting to 208 million yen ($1,773 thousand), and income before income taxes and minority interests for the year ended March 31, 2006 decreased by the same amount, as compared with the amount which would have been reported if the previous standards had been applied consistently. The accumulated impairment loss is disclosed, and included in accumulated depreciation.

(16) Reclassifications

Certain accounts in the consolidated financial statements for the year ended March 31, 2005 have been reclassified to conform to the 2006 presentation.

3. UNITED STATES DOLLAR AMOUNTS:

The U.S. dollar amounts are included solely for convenience and have been translated at the rate of ¥117.47 = U.S.$1, the approximate exchange rate prevailing in the Japanese foreign exchange market as at March 31, 2006. This translation should not be construed as a representation that the yen amounts actually represent, or have been or could be converted into U.S. dollars at that rate.

4. RELATED PARTY TRANSACTIONS:

The Company has related party transactions with Toyama Chemical Co., Ltd, a public and listed company on the Tokyo Stock Exchange, around 22% of whose common shares are owned by the Company. In the 2003 fiscal year, the Company acquired the exclusive sales rights to certain ethical drugs from Toyama Chemical Co., Ltd. at 7,300 million yen. This drug is still subject to approval by Ministry of Health, Labour and Welfare. Taisho Toyama Pharmaceutical Co., Ltd. was established in October 2002 through a joint investment of the Company (55 % investment in common stock) and Toyama Chemical Co., Ltd. (45% investment in common stock) and acts as sales distributor and promoter of the ethical drug products developed by both the Company and Toyama Chemical Co., Ltd. For the 2006 and 2005 fiscal years, purchase of 12,098 million yen ($102,987 thousand) and 12,567 million yen were made from Toyama Chemical Co., Ltd. and the related balance of accounts payable, trade amounted to 6,334 million yen ($53,920 thousand) and 6,776 million yen as of March 31, 2006 and 2005, respectively.

Sanofi-Aventis-Taisho Pharmaceuticals Co., Ltd. was established through a joint investment of the Company (49% investment in common stock) and Sanofi-Aventis (51% investment in common stock) and manufactured and sold Ancaron to the Company. For the 2006 and 2005 fiscal years, purchase of 5,417 million yen ($46,113 thousand) and 4,659 million yen were made and the related balance of accounts payable, trade amounted to 1,350 million yen ($11,495 thousand) and 1,160 million yen, respectively. Other income was 1,272 million yen ($10,826 thousand) and 1,375 million yen and the related balance of other current assets amounted to 361 million yen ($3,076 thousand) and 605 million yen, as of March 31, 2006 and 2005, respectively.

5. CASH AND CASH EQUIVALENTS:

Cash and cash equivalents at March 31, 2006 and 2005 comprised the following:

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2006	2005	**2006**
Cash and time deposits with original maturity of three months or less	**¥155,205**	¥147,265	**$1,321,231**
Marketable securities	**3,493**	11,267	**29,732**
Subtotal	**158,698**	158,532	**1,350,963**
Cash and time deposits with original maturity of three months or less	**(63,170)**	(69,748)	**(537,755)**
Marketable securities with original maturity of three months or less	**(3,332)**	(11,227)	**(28,364)**
Total	**¥ 92,196**	¥ 77,557	**$ 784,844**

6. MARKETABLE SECURITIES AND INVESTMENT SECURITIES:

The following information relates to the aggregate book value and fair value of securities in 2006 and 2005.

i) Held-to-maturity securities whose fair value is readily determinable.

	Millions of yen		
March 31, 2006	Book value	Fair value	Unrealized gains (losses)
Securities whose fair values exceed their book values on the consolidated balance sheet			
(1) Government bonds, municipal bonds, etc.	**¥ —**	**¥ —**	**¥ —**
(2) Corporate bonds	**3,628**	**3,814**	**186**
Subtotal	**3,628**	**3,814**	**186**
Securities whose fair values do not exceed their book values on the consolidated balance sheet			
(1) Government bonds, municipal bonds, etc.	**—**	**—**	**—**
(2) Corporate bonds	**3,991**	**3,943**	**(48)**
Subtotal	**3,991**	**3,943**	**(48)**
Total	**¥7,619**	**¥7,757**	**¥ 138**

	Thousands of U.S. dollars (Note 3)		
March 31, 2006	Book value	Fair value	Unrealized gains (losses)
Securities whose fair values exceed their book values on the consolidated balance sheet			
(1) Government bonds, municipal bonds, etc.	**$ —**	**$ —**	**$ —**
(2) Corporate bonds	**30,885**	**32,468**	**1,583**
Subtotal	**30,885**	**32,468**	**1,583**
Securities whose fair values do not exceed their book values on the consolidated balance sheet			
(1) Government bonds, municipal bonds, etc.	**—**	**—**	**—**
(2) Corporate bonds	**33,977**	**33,566**	**(411)**
Subtotal	**33,977**	**33,566**	**(411)**
Total	**$64,862**	**$66,034**	**$ 1,172**

March 31, 2005	Millions of yen		
	Book value	Fair value	Unrealized gains (losses)
Securities whose fair values exceed their book values on the consolidated balance sheet			
(1) Government bonds, municipal bonds, etc.	¥ —	¥ —	¥ —
(2) Corporate bonds	6,569	6,863	294
Subtotal	6,569	6,863	294
Securities whose fair values do not exceed their book values on the consolidated balance sheet			
(1) Government bonds, municipal bonds, etc.	—	—	—
(2) Corporate bonds	1,599	1,591	(8)
Subtotal	1,599	1,591	(8)
Total	¥8,168	¥8,454	¥ 286

ii) Other securities whose fair value is readily determinable.

March 31, 2006	Millions of yen		
	Acquisition cost	Fair value	Unrealized gains (losses)
Other securities whose fair values exceed their carrying values on the consolidated balance sheet			
(1) Equity securities	¥ 46,423	¥102,811	¥ 56,388
(2) Government bonds, municipal bonds, etc.	2,244	2,327	83
(3) Corporate bonds	34,847	35,300	453
(4) Others	30,926	32,189	1,263
Subtotal	114,440	172,627	58,187
Other securities whose fair values do not exceed their carrying values on the consolidated balance sheet			
(1) Equity securities	503	461	(42)
(2) Government bonds, municipal bonds, etc.	3,532	3,400	(132)
(3) Corporate bonds	58,232	57,174	(1,058)
(4) Others	19,271	18,726	(545)
Subtotal	81,538	79,761	(1,777)
Total	¥195,978	¥252,388	¥ 56,410
Tax effect			(34,065)
Total			¥ 22,345

March 31, 2006	Thousands of U.S. dollars (Note 3)		
	Acquisition cost	Fair value	Unrealized gains (losses)
Other securities whose fair values exceed their carrying values on the consolidated balance sheet			
(1) Equity securities	$ 395,194	$ 875,213	$480,019
(2) Government bonds, municipal bonds, etc.	19,103	19,810	707
(3) Corporate bonds	296,643	300,502	3,859
(4) Others	263,264	274,016	10,752
Subtotal	974,204	1,469,541	495,337
Other securities whose fair values do not exceed their carrying values on the consolidated balance sheet			
(1) Equity securities	4,284	3,920	(364)
(2) Government bonds, municipal bonds, etc.	30,068	28,948	(1,120)
(3) Corporate bonds	495,719	486,708	(9,011)
(4) Others	164,046	159,412	(4,634)
Subtotal	694,117	678,988	(15,129)
Total	$1,668,321	$2,148,529	$480,208
Tax effect			(289,991)
Total			$190,217

Other securities whose fair value is readily determinable are recorded at fair value on the consolidated balance sheet at March 31, 2006.

March 31, 2005	Millions of yen		
	Acquisition cost	Fair value	Unrealized gains (losses)
Other securities whose fair values exceed their carrying values on the consolidated balance sheet			
(1) Equity securities	¥ 25,876	¥ 46,535	¥20,659
(2) Government bonds, municipal bonds, etc.	25,086	25,255	169
(3) Corporate bonds	80,833	82,000	1,167
(4) Others	31,068	33,007	1,939
Subtotal	162,863	186,797	23,934
Other securities whose fair values do not exceed their carrying values on the consolidated balance sheet			
(1) Equity securities	998	991	(7)
(2) Government bonds, municipal bonds, etc.	9,331	8,450	(881)
(3) Corporate bonds	2,012	2,011	(1)
(4) Others	–	–	–
Subtotal	12,341	11,452	(889)
Total	¥175,204	¥198,249	¥23,045

Other securities whose fair value is readily determinable are recorded at fair value on the consolidated balance sheet at March 31, 2005.

iii) Other securities sold in the current fiscal year.

March 31, 2006	Millions of yen	Thousands of U.S. dollars (Note 3)
Proceeds from sales of other securities	¥28,135	$239,506
Gain on sales of other securities	88	745
Loss on sales of other securities	1	9

March 31, 2005	Millions of yen
Proceeds from sales of other securities	¥46
Gain on sales of other securities	40
Loss on sales of other securities	—

iv) Securities whose fair value is not readily determinable.

	Book value	
March 31, 2006	Millions of yen	Thousands of U.S. dollars (Note 3)
Other securities		
(1) Unlisted equity securities	¥ 471	$ 4,011
(2) Bonds issued by domestic corporations	4,000	34,051
(3) Subscriptions to investment business associations	1,202	10,229
Total	¥5,673	$48,291

	Book value
March 31, 2005	Millions of yen
Other securities	
(1) Unlisted equity securities	¥ 457
(2) Bonds issued by domestic corporations	4,000
(3) Subscriptions to investment business associations	1,272
Total	¥5,729

v) Redemption schedule for other securities with a maturity date and held-to-maturity securities.

	Millions of yen			
March 31, 2006	Due 2007	Due 2008 – 2011	Due 2012 – 2016	Due after 2017
1. Bonds				
(1) Government bonds, municipal bonds, etc.	¥2,350	¥ 3,524	¥ —	¥ —
(2) Corporate bonds	3,350	37,281	15,000	—
2. Others				
(3) Others	—	—	—	—
Total	¥5,700	¥40,805	¥15,000	¥ —

	Thousands of U.S. dollars (Note 3)			
March 31, 2006	Due 2007	Due 2008 – 2011	Due 2012 – 2016	Due after 2017
1. Bonds				
(1) Government bonds, municipal bonds, etc.	$20,002	$ 30,003	$ —	$ —
(2) Corporate bonds	28,512	317,368	127,692	—
2. Others				
(3) Others	—	—	—	—
Total	$48,514	$347,371	$127,692	$ —

	Millions of yen			
March 31, 2005	Due 2006	Due 2007 – 2010	Due 2011 – 2015	Due after 2016
1. Bonds				
(1) Government bonds, municipal bonds, etc.	¥ 3,220	¥30,366	¥ —	¥ —
(2) Corporate bonds	9,615	23,719	7,000	—
2. Others				
(3) Others	—	—	—	—
Total	¥12,835	¥54,085	¥7,000	¥ —

7. PROPERTY, PLANT AND EQUIPMENT:

Property, plant and equipment at March 31, 2006 and 2005 consisted of the following:

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2006	2005	2006
Buildings and structures	¥ 116,322	¥ 114,253	$ 990,229
Machinery, equipment and vehicles	68,648	68,090	584,391
Other	29,246	28,592	248,967
At cost	214,216	210,935	1,823,587
Accumulated depreciation	(148,261)	(143,281)	(1,262,127)
Land	27,233	27,230	231,833
Construction in progress	5,854	1,387	49,833
	¥ 99,042	¥ 96,271	$ 843,126

8. SHORT-TERM LOANS:

Short-term loans at March 31, 2006 represented bank overdrafts which bore an average interest rate of 1.375%.

9. COST OF RETIREMENT AND SEVERANCE BENEFITS:

The funded status as at March 31, 2006 and 2005 was as follows:

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2006	2005	2006
(1) Benefit obligation	¥36,424	¥48,339	$310,067
(2) Plan assets	(22,912)	(8,573)	(195,046)
(3) Unfunded benefit obligation (1)+(2)	13,512	39,766	115,021
(4) Unrecognized prior service cost	5,550	660	47,249
(5) Unrecognized actuarial loss	(298)	(5,920)	(2,537)
Accrued retirement benefits (3)+(4)+(5)	¥18,764	¥34,506	$159,733

438 employees were transferred from Toyama Chemical Co., Ltd. (around 22% owned affiliated company) to Taisho Toyama Pharmaceutical Co., Ltd. (a subsidiary) on April 1, 2005. Consequently, the pension benefit obligation and unrecognized obligation increased by 649 million yen on that day.

Effective from April 1, 2005, the Company and Taisho Toyama Pharmaceutical Co., Ltd. determined an amendment to the employees' retirement benefit regulation based on the point which are granted depending on length of service periods, qualification, evaluation and managerial posts although employees' retirement benefits have been determined based on final salary at retirement in prior years. In addition, the commencement of payment of employees' retirement benefits was changed from 55 to 60years old. Consequently, on April 1, 2005 the pension benefit obligation decreased by 4,682 million yen and unrecognized prior service liabilities (negative position) increased by the same amount.

Effective July 1, 2005, a part of the defined benefit plan was transferred o contributory funded defined benefit pension plans and defined contribution pension plans. According to this change, pension benefit obligation decreased by 4,163 million yen ($ 35,438 thousand), unrecognized prior service liabilities (negative position) increased by 966 million yen ($8,223 thousand), and unrecognized actual loss increased by 590 million yen ($5,023 thousand).

The components of net retirement costs for the years ended March 31, 2006 and 2005 are as follows:

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2006	2005	**2006**
Service costs	**¥2,119**	¥2,951	**$18,041**
Interest costs	**826**	931	**7,028**
Expected return on plan assets	**(370)**	(174)	**(3,153)**
Amortization of prior service costs	**(394)**	(56)	**(3,351)**
Amortization of actuarial gain/loss	**714**	774	**6,083**
Retirement costs	**2,895**	4,426	**24,648**
Gain on the settlement of defined benefit pension plan	**(759)**	—	**(6,463)**
Others	**350**	—	**2,978**
Total	**¥2,486**	¥4,426	**$21,163**

Assumptions used for the years ended March 31, 2006 and 2005 were as follows:

	2006	2005
Discount rate	**2.0%**	2.0%
Expected return on plan assets	**3.0%**	3.0%
Method of attributing the projected benefits to periods of service	Straight-line basis	Straight-line basis
Period for amortization of prior service cost	**15-17 years**	15 years
Period for amortization of actuarial gain/loss	**15-17 years**	15-16 years

10. APPROPRIATION OF RETAINED EARNINGS:

The Japanese Commercial Code provides that an amount equal to at least 10% of cash dividends and bonuses to directors and statutory auditors shall be appropriated as a legal reserve until such reserve equals 25% of the capital stock amount. This reserve is not available for dividends but may be used to reduce a deficit or may be transferred to stated capital. Effective from October 1, 2001, such a reserve shall be provided until the sum of the capital surplus and legal reserve equals 25% of the stated capital. The balances of the legal reserve of the Company at March 31, 2006 and 2005, which are included in retained earnings in the accompanying consolidated balance sheet, were 7,451 million yen ($63,430 thousand) and 7,451 million yen, respectively.

Both under the former Japanese Commercial Code and the new Corporation Law, the appropriation of retained earnings for a fiscal year is made by a resolution of shareholders at a general meeting to be held after the balance sheet date, and the accounts for the year do not reflect such appropriation.

The proposed appropriation of retained earnings of the Company for the year ended March 31, 2006, which was approved on June 29, 2006 at the general shareholders' meeting is as follows:

	Millions of yen	Thousands of U.S. dollars (Note 3)
	2006	**2006**
Cash dividends at ¥30.00 ($0.26) per share	**¥9,246**	**$78,711**
Directors' and statutory auditors' bonuses	**73**	**621**
	¥9,319	**$79,332**

11. INCOME TAXES:

The components of income tax expenses were as follows:

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2006	2005	**2006**
Income taxes			
– Current payable	**¥18,625**	¥22,142	**$158,554**
– Deferred	**3,892**	483	**33,132**
	¥22,517	¥22,625	**$191,686**

Income taxes applicable to the Company and its domestic consolidated subsidiaries include (1) corporation tax, (2) enterprise tax and (3) inhabitants' tax which, in aggregate, represent a statutory tax rate of approximately 40.5 per cent, effective from April 1, 2004.

On March 31, 2003, the Japanese National Diet approved various changes to the calculation of the statutory local enterprise tax for companies with capital in excess of 100 million yen, effective April 1, 2004. Under the amended legislation, the enterprise tax is the sum of three tax components: a) an income-based component, b) a value-added component and c) a capital-based component.

The significant components of deferred tax assets and liabilities as of March 31, 2006 and 2005 were as follows:

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2006	2005	**2006**
Deferred tax assets:			
Enterprise taxes	**¥ 668**	¥ 691	**$ 5,689**
Accrued expenses	**2,476**	2,691	**21,078**
Research expenses, etc.	**2,367**	2,594	**20,152**
Accrued retirement benefits for directors, statutory auditors and executive officers	**644**	618	**5,481**
Accrued employees retirement benefits	**7,329**	13,495	**62,393**
Accrued bonuses	**1,578**	1,347	**13,432**
Long-term liabilities	**2,091**	–	**17,798**
Prepaid research expenses	**974**	1,254	**8,295**
Operating loss carryforwards for tax purposes	**163**	341	**1,390**
Other	**7,028**	5,915	**59,820**
Gross deferred tax assets	**25,318**	28,946	**215,528**
Less: Valuation allowance	**(202)**	(559)	**(1,720)**
Total deferred tax assets	**25,116**	28,387	**213,808**
Deferred tax liabilities:			
Net unrealized gains on securities	**(23,566)**	(9,333)	**(200,612)**
Deferred gain on sales of real property	**(2,136)**	(2,241)	**(18,183)**
Other	**(4)**	(13)	**(36)**
Total deferred tax liabilities	**(25,706)**	(11,587)	**(218,831)**
Net deferred tax assets (liabilities)	**¥ (590)**	¥ 16,800	**$ (5,023)**

The valuation allowance mainly relates to the deferred tax assets of foreign consolidated subsidiaries with tax loss carryforwards that are not expected to be realized in the near future.

Net deferred tax assets included in the consolidated balance sheets were as follows:

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2006	2005	**2006**
Current assets – deferred income taxes	**¥ 8,160**	¥ 8,132	**$ 69,465**
Other assets – deferred income taxes	**723**	8,695	**6,158**
Short-term liabilities – other	**(0)**	—	**(1)**
Long-term liabilities – other	**(9,473)**	(27)	**(80,645)**
Net deferred tax assets (liabilities)	**¥ (590)**	¥16,800	**$ (5,023)**

At March 31, 2006, no deferred income taxes have been provided on the undistributed earnings of foreign subsidiaries not expected to be remitted in the foreseeable future. The tax loss carryforwards of consolidated foreign subsidiaries at March 31, 2006 amounted to approximately 403 million yen ($3,432 thousand) and these are available to offset against the future taxable income of such foreign subsidiaries. These carryforwards expire at various dates and their realization is dependent on such foreign subsidiaries generating sufficient taxable income prior to the expiration of the tax loss carryforwards.

Although realization is not assured, management believes that it is more likely than not that all of the deferred tax assets less the valuation allowance will be realized. The amount of such net deferred tax assets considered realizable, however, could change in the near future if estimates of future taxable income during the carryforward period change.

Reconciliation for 2006 and 2005 fiscal years is as follows.

	March 31 2006	March 31 2005
Statutory tax rate	**40.5%**	40.5%
(Reconciliation)		
Entertainment expenses	**1.9**	1.8
Dividend income	**(0.4)**	(0.1)
Research expenses	**(4.2)**	(4.2)
Equity in net losses of affiliated companies	**0.4**	0.5
Valuation allowance	**0.2**	0.4
Others	**0.2**	(0.1)
Effective income tax rate	**38.6%**	38.8%

12. RESEARCH AND DEVELOPMENT EXPENSES:

Research and development expenses included in selling, general and administrative expenses totaled 23,072 million yen ($196,409 thousand) and 23,221 million yen for the years ended March 31, 2006 and 2005, respectively.

13. OTHER INCOME AND EXPENSES:

Other income and expenses for the years ended March 31, 2006 and 2005 consist of the following:

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2006	2005	**2006**
Other income:			
Gain on sales of property, plant and equipment	**¥ 3**	¥ 24	**$ 29**
Rental income of real estate	**108**	110	**920**
Gain on sales of investment securities	**89**	40	**758**
Gain on sales of investment securities to affiliated company	**8,496**	—	**72,328**
Gain on the settlement of defined benefit pension plan	**759**	—	**6,463**
Others	**690**	1,562	**5,861**
	¥10,145	¥1,736	**$86,359**

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2006	2005	**2006**
Other expenses:			
Devaluation losses on investment securities	**¥ 1**	¥ 26	**$ 9**
Loss on disposal of property, plant and equipment	**575**	319	**4,892**
Equity in net losses of affiliated companies	**638**	650	**5,431**
Impairment loss on fixed assets	**208**	-	**1,773**
Others	**1,184**	940	**10,079**
	¥2,606	¥1,935	**$22,184**

14. LEASES:

Leases that transfer substantially all the risks and rewards of ownership of the assets are accounted for as capital leases. Leases that do not transfer ownership of the assets at the end of the lease term are accounted for as operating leases in accordance with accounting principles and practices generally accepted in Japan. Certain information on such lease contracts of the Company and its consolidated subsidiaries, as a lessee, is shown below.

Finance leases other than those which do not transfer ownership of properties to lessees are as follows:

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2006	2005	**2006**
Tools, instruments and furniture	**¥ 8,084**	¥ 9,975	**$ 68,813**
Software	**11,159**	11,039	**94,994**
Others	**120**	122	**1,026**
At cost – subtotal	**¥ 19,363**	¥ 21,136	**$164,833**
Accumulated depreciation	**(10,662)**	(10,084)	**(90,762)**
Total	**¥ 8,701**	¥ 11,052	**$ 74,071**

The present values of future lease payments of the Companies, excluding the amounts representing interest, at March 31, 2006 and 2005 are as follows:

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2006	2005	2006
(Lessee)			
Current obligation	¥3,081	¥ 3,743	$26,226
Long-term obligation	5,779	7,509	49,198
Present values of future lease payment	¥8,860	¥11,252	$75,424

Lease payments and amounts representing depreciation and interest, at March 31, 2006 and 2005 are as follows:

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2006	2005	2006
Lease payments	¥4,009	¥4,440	$34,125
Amount representing depreciation	¥3,680	¥4,189	$31,327
Amount representing interests	¥ 307	¥ 238	$ 2,610

15. DERIVATIVE FINANCIAL INSTRUMENTS:

The Company and its consolidated foreign subsidiaries utilize derivative financial instruments selectively, to hedge foreign exchange risk and floating interest exchange risk.

As of March 31, 2006 and 2005, there are no contract amounts outstanding for derivatives except for those held for "hedge accounting" purposes as described in Note 2 (3) c) preceding.

16. CONTINGENT LIABILITIES:

Based upon information currently available, the Company and its consolidated subsidiaries have no significant pending lawsuits.

17. SEGMENT INFORMATION:

(1) Industry segment information

The Company and its subsidiaries are engaged principally in the following two industrial segments:

Self-medication: OTC products, consumer goods for household and general use and other products.

Prescription pharmaceutical: Ethical drugs

The segment information of the Company and its subsidiaries for the years ended March 31, 2006 and 2005 is presented below:

	Millions of yen				
March 31, 2006	Self-medication	Prescription pharmaceutical	Total	Elimination/ Corporate	Consolidated
I. Net sales:					
(1) Outside customers	¥174,832	¥96,576	¥271,408	¥ —	¥271,408
(2) Inter-segment	—	—	—	—	—
Total	174,832	96,576	271,408	—	271,408
Operating expenses	141,229	83,783	225,012	—	225,012
Operating profit	¥ 33,603	¥12,793	¥ 46,396	¥ —	¥ 46,396
II. Assets, depreciation and capital expenditure:					
Assets	¥232,502	¥115,499	¥348,001	¥316,430	¥664,431
Depreciation	9,336	3,473	12,809	—	12,809
Capital expenditure	9,291	4,461	13,752	—	13,752

	Thousands of U.S. dollars (Note 3)				
March 31, 2006	Self-medication	Prescription pharmaceutical	Total	Elimination/ Corporate	Consolidated
I. Net sales:					
(1) Outside customers	$1,488,311	$822,133	$2,310,444	$ —	$2,310,444
(2) Inter-segment	—	—	—	—	—
Total	1,488,311	822,133	2,310,444	—	2,310,444
Operating expenses	1,202,261	713,226	1,915,487	—	1,915,487
Operating profit	$ 286,050	$108,907	$ 394,957	$ —	$ 394,957
II. Assets, depreciation and capital expenditure:					
Assets	$1,979,245	$983,225	$2,962,470	$2,693,711	$5,656,181
Depreciation	79,482	29,563	109,045	—	109,045
Capital expenditure	79,094	37,975	117,069	—	117,069

	Millions of yen				
March 31, 2005	Self-medication	Prescription pharmaceutical	Total	Elimination/ Corporate	Consolidated
I. Net sales:					
(1) Outside customers	¥183,417	¥96,020	¥279,437	¥ —	¥279,437
(2) Inter-segment	—	—	—	—	—
Total	183,417	96,020	279,437	—	279,437
Operating expenses	144,402	80,337	224,739	—	224,739
Operating profit	¥ 39,015	¥15,683	¥ 54,698	¥ —	¥ 54,698
II. Assets, depreciation and capital expenditure:					
Assets	¥225,638	¥119,140	¥344,778	¥269,025	¥613,803
Depreciation	10,104	3,398	13,502	—	13,502
Capital expenditure	6,178	1,414	7,592	—	7,592

(2) Geographic area information and export sales information

As the total sales by consolidated subsidiaries outside Japan and the total export sales overseas are less than 10 % of the consolidated net sales, information relating to geographic area and export sales has been omitted.

ChuoAoyama PricewaterhouseCoopers

PRICEWATERHOUSECOOPERS

Kasumigaseki Bldg. 32nd Floor
3-2-5, Kasumigaseki, Chiyoda-ku,
Tokyo 100-6088, Japan

Report of Independent Auditors

June 29, 2006

To the Board of Directors
of Taisho Pharmaceutical Co., Ltd.

We have audited the accompanying consolidated balance sheets of Taisho Pharmaceutical Co., Ltd. and its subsidiaries as of March 31, 2006 and 2005, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the two years in the period ended March 31, 2006, all expressed in Japanese yen. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Taisho Pharmaceutical Co., Ltd. and its subsidiaries as of March 31, 2006 and 2005, and the consolidated results of their operations and their cash flows for each of the two years in the period ended March 31, 2006, in conformity with accounting principles generally accepted in Japan.

ChuoAoyama PricewaterhouseCoopers
(Certified Public Accountants)

Corporate Data

(As of July 1, 2006)

COMPANY NAME: Taisho Pharmaceutical Co., Ltd.

DATE OF FOUNDATION: October 12, 1912

PAID-IN CAPITAL: ¥29,804 million

NUMBER OF EMPLOYEES: 5,191 (As of March 31, 2006)

HOME PAGE: http://www.taisho.co.jp/

BOARD OF DIRECTORS:

Chairman of the Board
Shoji Uehara*

President
Akira Uehara*

Executive Vice Presidents
Akira Ohira*
Hisataka Hotta*

Managing Director
Hideyuki Waki

Executive Directors
Yoshiaki Sasaki
Kunihiro Kitamura

Corporate Auditors
Masahiro Furuhashi
Satoshi Toyama
Toshio Morikawa**
Takayuki Tsukuda**

* *Representative Director*
** *External auditor as stipulated by Article 2.1 of the Corporation Law*

DIRECTORY:

HEAD OFFICE
24-1, Takada 3-chome, Toshima-ku, Tokyo 170-8633, Japan
Telephone: 81-3-3985-1111
Facsimile: Public Relations Section: 81-3-3985-6485
International Division: 81-3-3980-6624
(Self-Medication Operation Group)
Self-Medication Licensing Division: 81-3-3988-2963
(Prescription Pharmaceutical Operation Group)
Business Strategy Division: 81-3-3985-0716

BRANCH OFFICES
Sapporo, Sendai, Nagoya, Osaka, Kanazawa, Hiroshima, Shikoku, Fukuoka

OMIYA FACTORY
403, Yoshino-cho 1-chome, Kita-ku, Saitama-shi, Saitama 331-9520, Japan
Telephone: 81-48-663-1111 Facsimile: 81-48-664-9400

RESEARCH CENTER
403, Yoshino-cho 1-chome, Kita-ku, Saitama-shi, Saitama 331-9530, Japan
Telephone: 81-48-663-1111 Facsimile: 81-48-652-7254

OKAYAMA FACTORY
33-2, Taiheidai, Shouou-cho, Katsuta-gun, Okayama 709-4321, Japan
Telephone: 81-868-38-6131 Facsimile: 81-868-38-5342

HANYU FACTORY
603-27, Komatsudai 1-chome, Hanyu, Saitama 348-8540, Japan
Telephone: 81-48-563-1121 Facsimile: 81-48-563-2152

Major Subsidiaries and Affiliates

(As of July 1, 2006)

Name	Location	Capitalization/ Amount Invested	Business Area	Parent Company Ownership
DOMESTIC				
Taisho Toyama Pharmaceutical Co., Ltd.	Tokyo, Japan	JPY 2,000,000,000	Sales of prescription pharmaceuticals	55%
Taisho Business Research Institute Co., Ltd.	Tokyo, Japan	JPY 50,000,000	Information processing services	100%
Taisho Pharmaceutical Logistics Co., Ltd.	Saitama, Japan	JPY 30,000,000	Management and operation of transport services for Taisho Pharmaceutical and Taisho Toyama Pharmaceutical	100%
Taisho Okinawa Co., Ltd.	Okinawa, Japan	JPY 50,000,000	Sales of Taisho Pharmaceutical products in Okinawa Prefecture	100%
Taisho M.T.C. Co., Ltd.	Tokyo, Japan	JPY 400,000,000	Manufacture in Fukuoka Prefecture of raw materials for medicines and quasi-drugs, and their domestic and overseas sales	60%
TAISHO ACTIVE HEALTH Co., Ltd.	Tokyo, Japan	JPY 100,000,000	Development and contract manufacture of health foods, quasi-drugs and skin care products	55%
Taisho Kosei Service Co., Ltd.	Tokyo, Japan	JPY 10,000,000	Sales of Taisho Pharmaceutical products, insurance agent, printing service, procurement and sales of all product types	100%
Mejiro Real Estate Co., Ltd.	Tokyo, Japan	JPY 600,000,000	Leasing, maintenance, possession and management of real estate	100%
Shimoda Central Co., Ltd.	Tokyo, Japan	JPY 100,000,000	Hotel management	100%
OVERSEAS				
Taisho Pharmaceutical (Taiwan) Co., Ltd.	Taipei, Taiwan	TWD 200,000,000	Manufacture and sales of Taisho Pharmaceutical products in Taiwan	86.6%
Taisho Pharmaceutical California Inc.	Torrance, CA, U.S.A.	USD 41,050,000	Manufacture (commisioned) and sales of Taisho Pharmaceutical products in the United States	100%
Taisho Pharmaceutical (M) SDN. BHD.	Selangor, Malaysia	MYR 24,380,000	Manufacture and sales of Taisho Pharmaceutical products in Malaysia	100%
Taisho Pharmaceutical Asia (M) SDN. BHD.	Selangor, Malaysia	MYR 26,500,000	Central control of operations in the ASEAN region, market development, business guidance, and sales of food products	100%
Taisho Pharmaceuticals (Philippines), Inc.	Makati, Philippines	PHP 18,900,000	Manufacture (commissioned) and sales of Taisho Pharmaceutical products in the Philippines	100%
PT. Taisho Indonesia	Jakarta, Indonesia	IDR 42,920,000,000	Manufacture and sales of Taisho Pharmaceutical products in Indonesia	100%
Taisho Co., Ltd. Shanghai	Shanghai, China	CNY 132,621,000	Manufacture and sales of Taisho Pharmaceutical products in China	85%
Taisho Pharmaceutical (Europe) Ltd.	London, U.K.	GBP 20,000,000	Manufacture (commissioned) and sales of Taisho Pharmaceutical products in the U.K.	100%
Taisho Vietnam Co., Ltd.	Khanh Hoa Pro., Vietnam	VND 136,806,000,000	Manufacture and sales of Taisho Pharmaceutical products in Vietnam	100%
Taisho Pharmaceutical (H.K.) Ltd.	Hong Kong, China	HKD 163,000,000	Sales of Taisho Pharmaceutical products in Hong Kong	100%
Osotspa Taisho Co., Ltd.	Bangkok, Thailand	THB 15,000,000	Sales of Taisho Pharmaceutical products in Thailand	49%
Taisho Pharmaceutical R&D Inc.	Morristown NJ, U.S.A.	USD 4,000,000	Development of prescription pharmaceuticals in the United States	100%
Taisho Hizon Manufacturing Inc.	Antipolo City, Philippines	PHP 17,000,000	Commissioned manufacture of products for Taisho Pharmaceuticals (Philippines), Inc.	50%

Investor Information

(As of March 31, 2006)

COMMON STOCK:

Authorized: 1,174,959,000
(As of June 29, 2006)
Issued: 320,465,510
Number of shareholders: 40,632

GENERAL MEETING OF SHAREHOLDERS: Held annually in June

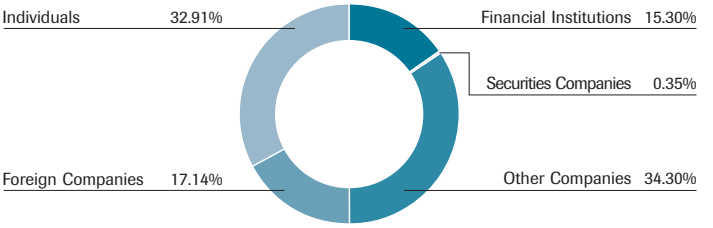
LISTINGS: Tokyo Stock Exchange

TICKER SYMBOL NUMBER: 4535

STOCK TRANSFER AGENT: Mitsubishi UFJ Trust and Banking Corporation
4-5, Marunouchi 1-Chome,
Chiyoda-ku,
Tokyo 100-8212, Japan

HEADQUARTERS: 24-1, Takada 3-chome,
Toshima-ku,
Tokyo 170-8633, Japan

DISTRIBUTION OF SHAREHOLDERS

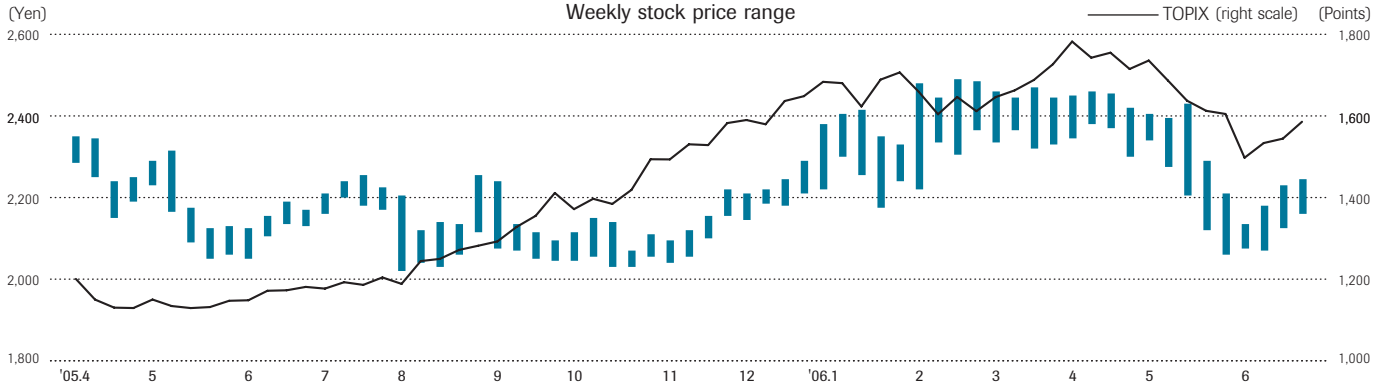


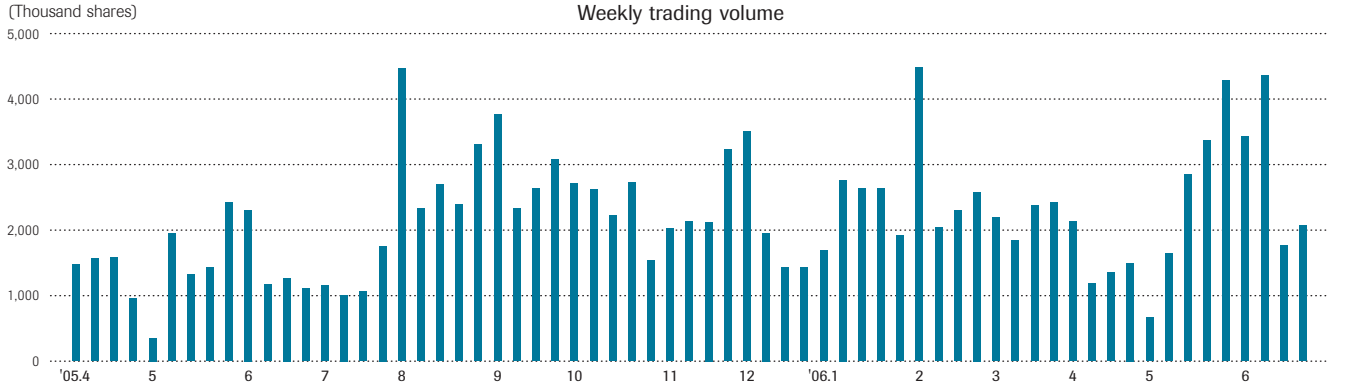
MAJOR SHAREHOLDERS

Shares Held Shareholders *	Number of Voting Rights (Thousands)	Percentage of Voting Rights (%)
Uehara Memorial Foundation	43,000	13.42
Shoji Uehara	36,614	11.43
Northern Trust Company (AVFC) Sub-Account American Client	13,798	4.31
Sumitomo Chemical Co., Ltd.	12,133	3.79
Sumitomo Mitsui Banking Corporation	10,000	3.12
The Bank of Tokyo-Mitsubishi UFJ, Ltd.	10,000	3.12
Uehara Museum of Modern Art Foundation	10,000	3.12
Akira Uehara	7,145	2.23
Japan Trustee Services Bank, Ltd.**	6,345	1.98
Mellon Bank Treaty Client Omnibus	6,132	1.91

**Excluding Taisho Pharmaceuticals, which held 12,261 thousand shares (3.83% of voting rights) of treasury stock as of March 31, 2006*
***Trust Account*

STOCK DATE (TSE) (April 2005 – June 2006)





Cautionary Statement with Respect to Forward-Looking Statements

Statements made in this annual report with respect to Taisho Pharmaceutical's current plans, estimates, strategies and beliefs and other statements that are not historical facts are foward-looking statements about the future performance of the Taisho Pharmaceutical Group. These statements are based on management's assumptions and beliefs in light of the information currently available to it and therefore readers should not place undue reliance on them. The Taisho Pharmaceutical Group cautions readers that a number of important factors including but not limited to changes in general economic conditions could cause actual results to differ materially from those discussed in the forward-looking statements.

TAISHO PHARMACEUTICAL CO., LTD.

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(Prescription Pharmaceutical Operation Group)
Business Strategy Division: 81-3-3985-0716
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