



SANTEN PHARMACEUTICAL CO., LTD.

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SANTEN PHARMACEUTICAL CO., LTD.
ANNUAL REPORT 2001

Year ended March 31, 2001

天機に参与する

“Act with the Sanction of Heaven*”

We first ask ourselves, “What are our principles?”

In accordance with these principles, we decide clearly what actions to take, then act promptly and appropriately.

Based on these principles, we apply our unique wisdom and organizational capability in our areas of expertise to improve the well-being of patients, their loved ones, and by serving them, contribute to society as a whole.

* This credo, from a famous Chinese classic of the fifth century, describes how a saint harmonized the heavenly order and the earthly society. This is the derivation of the name Santen. This is our credo.

Profile

Since its founding more than 110 years ago, Santen has been dedicated to innovations in eye and health care. As an integrated pharmaceutical company, Santen is involved in research and development, production and sale of prescription and over-the-counter (OTC) pharmaceuticals. Santen concentrates its managerial resources in ophthalmic and anti-rheumatic pharmaceuticals and is committed to conducting basic studies of diseases and their pathologies and developing new products that meet the needs of medical professionals and their patients. Sales to medical institutions and pharmaceutical retailers are promoted through use of the Company’s extended information network and experience in our specialties.

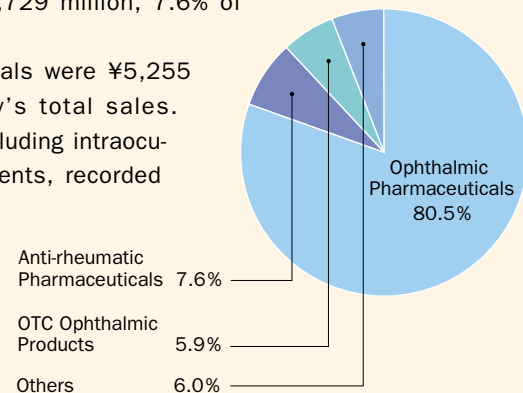
In the rapidly changing pharmaceutical industry, Santen is striving to become a world-class company that provides maximum value to shareholders.

In the fiscal year ended March 2001, the Company achieved sales of ¥88,449 million, operating income of ¥16,518 million and net income of ¥7,714 million.

Sales of ophthalmic pharmaceuticals, the Company’s largest business segment, were ¥71,231 million, 80.5% of the Company’s total sales.

Sales of anti-rheumatic pharmaceuticals, Santen’s second largest business, were ¥6,729 million, 7.6% of the Company’s total sales.

Sales of OTC pharmaceuticals were ¥5,255 million, 5.9% of the Company’s total sales. Ophthalmic medical devices, including intraocular lenses and surgical instruments, recorded sales of ¥1,144 million.



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Forward-Looking Statements

This annual report contains forward-looking statements regarding the Company’s plans, outlook, strategies and results for the future. All forward-looking statements are based on judgments derived from the information available to the Company at the time of publication.

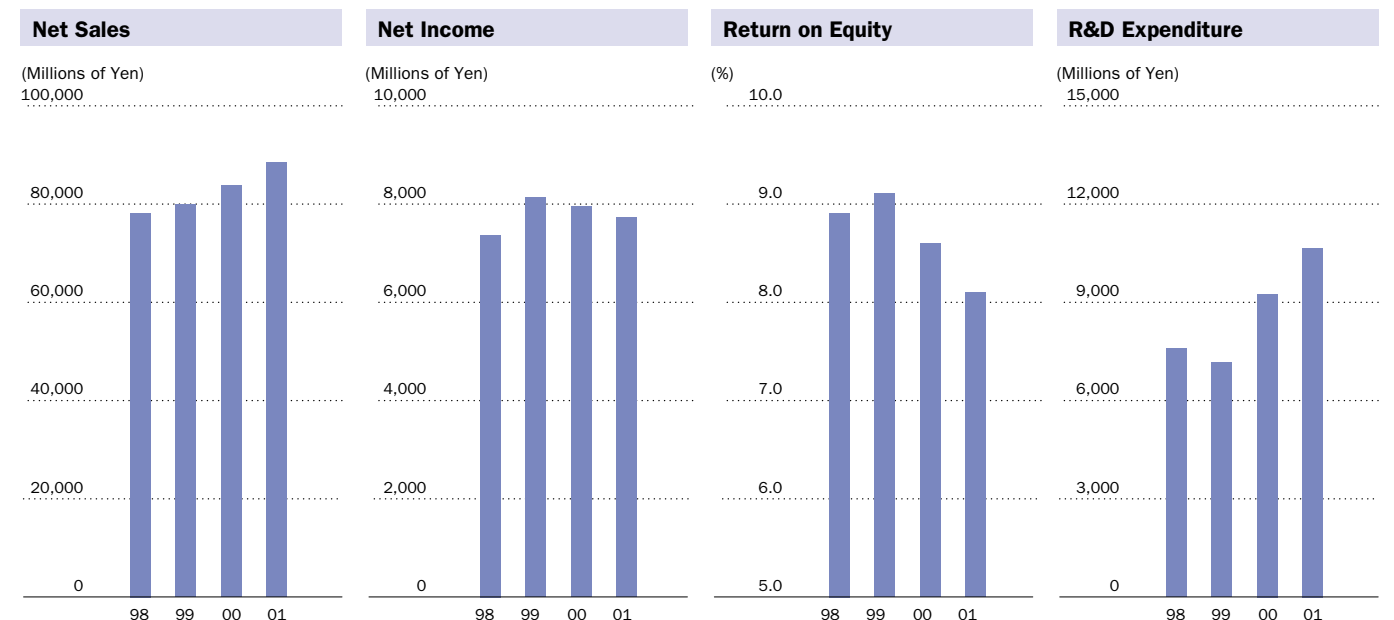
Certain risks and uncertainties could cause the Company’s actual results to differ materially from any projections presented in this report. These risks and uncertainties include, but are not limited to, the economic circumstances surrounding the Company’s businesses; competitive pressures; related laws and regulations; product development programs; and changes in exchange rates

FINANCIAL HIGHLIGHTS

Santen Pharmaceutical Co., Ltd. and Subsidiaries
Years ended March 31, 2001 and 2000

	Millions of yen, except per share information		Percentage of previous year 2001/2000	Thousands of U.S.dollars, except per share information
	2001	2000		2001
For the year:				
Net sales	¥ 88,449	¥ 83,577	+5.8%	\$ 713,873
Net income	7,714	7,941	-2.9	62,258
R&D expenditure	10,511	9,221	+14.0	84,833
Capital expenditures	4,943	2,510	+96.9	39,894
Depreciation and amortization	5,683	5,725	-0.7	45,871
Per share data (yen and dollars):				
Net income	¥ 81.32	¥ 83.54	-2.7%	\$ 0.66
Cash dividends	20.00	12.00	+66.7	0.16
At year-end:				
Total assets	¥ 153,243	¥ 149,968	+2.2%	\$ 1,236,826
Total shareholders’ equity	94,834	95,669	-0.9	765,407
Return on equity (ROE)	8.1%	8.6%	—	—

Note: 1. U.S.dollar amounts have been translated from yen, for convenience only, at the rate prevailing on March 30, 2001. of ¥123.90 to U.S.\$1.
2. Net sales in 2001 includes royalty income which was presented as “Other” in “Other income” in 2000



The fiscal year ended March 2001 (FY2000) marked significant progress in Santen's efforts to become a world-class company. Santen consolidated its number-one position in the Japanese ophthalmic market with the launch of two new products; Cravit for the treatment of ophthalmic infections and Livostin for the treatment of ocular allergies. The Company also achieved a major milestone in its geographic business expansion with its direct market entry into the U.S. ophthalmic market with three products; Betimol for the treatment of glaucoma, Alamast for the treatment of ocular allergies and Quixin (Japanese product name: Cravit). The Company continued to increase its investment in research and development (R&D) focused on the treatment of ophthalmic and rheumatic diseases. And, in fiscal 2000, Santen continued to implement organizational changes designed to improve corporate governance and maximize shareholder value. These actions have helped Santen make significant strides toward establishing itself as a world-class enterprise.

Business Performance Outline

Santen's consolidated net sales increased in fiscal 2000 despite difficult conditions. In April 2000, the revised National Health Insurance Drug Price Standard went into effect, resulting in an average 7% drop in Japanese drug prices. In addition, Santen was the subject of an extortion attempt in June 2000, and, in accordance with Santen's principle of placing the highest priority on consumer safety, all OTC eyedrops were recalled as a precautionary measure. Despite these difficulties, consolidated net sales increased 5.8% to ¥88,449 million.

Gross profit grew at a faster rate, 7.2%, due to a more favorable product mix and lower depreciation costs in manufacturing. The Company used the funds generated by the growth in sales and gross profit to invest in the future as we concluded several R&D agreements to expand our R&D pipeline and to invest in the sales and marketing resources needed for overseas business expansion. The increase in R&D and overseas selling and marketing expenses, combined with the extraordinary loss resulting from the temporary recall of all OTC eyedrops, led to a 2.9% decrease in net income to ¥7,714 million. Santen's cash flow and balance sheet remains strong and Santen returned over ¥6.6 billion to shareholders, including ¥5.1 billion for stock repurchases and ¥1.5 billion in dividend payments.

Domestic Business

Focusing on our strengths in ophthalmic and anti-rheumatic pharmaceuticals

The demand for prescription ophthalmic pharmaceuticals has increased significantly as an aging society has resulted in an increase in the number of glaucoma and cataract patients, and the widespread use of personal computers has increased the incidence of dry eye syndrome. With our broad portfolio of pre-

scription ophthalmic products covering practically all eye diseases known in Japan, and our strong team of medical representatives, Santen was able to maintain its number-one position in the Japanese ophthalmic market with an overall market share of 42.9% as of March 2001. Santen remains committed to improving patients' lives and will continue to satisfy the expectations of medical professionals by creating increasingly effective new drugs. Our attention is focused on treatments for corneal disease and anti-infective, anti-glaucoma and anti-allergic ophthalmics.

Significant events in fiscal 2000 included the launch of Cravit Ophthalmic Solution in April 2000. Cravit is the next generation quinolone and the successful launch, combined with sales of Tarivid, helped Santen to maintain its number one position in the anti-infective market with 81% market share. We also launched Livostin for the treatment of itch associated with ocular allergies in January 2001 and expect it to become our best selling anti-allergy product within the next fiscal year. Sales of Hyalein, a treatment for corneal diseases caused by dry eye syndrome, continued to show steady growth with an increase of 15.9% over prior year.

The aging population has also given rise to greater numbers of rheumatic patients. By providing medications for rheumatoid arthritis, Santen has been able to help improve patients' quality of life and maintain its number-two position in the anti-rheumatic market with 28% market share.

Overseas Business

Strong growth through business expansion in the U.S., Europe and Asia

We will continue to grow our business in Japan but we expect a large portion of our future growth will result from expanding our market presence in other parts of the world. Although this expansion requires considerable up-front expenses, we feel that it is essential to the future growth and profitability of the company.

Santen achieved a significant milestone in this area in fiscal 2000 with our entry into the U.S. market. The Company now has three products on the market in the U.S.: an anti-infective product, Quixin (Japanese product name: Cravit); an anti-allergy product, Alamast (Japanese product name: Alegysal); and an anti-glaucoma product, Betimol. Santen began direct promotion of these products to ophthalmologists in fiscal 2000 and finalized co-promotion agreements with partners to reach other key prescribers including pediatricians, general practitioners and allergists.

Santen continues to have a strong presence in the Northern and Eastern European ophthalmic markets. We are currently conducting clinical trials in Europe on Hyalein and also completed registration filings for Alamast and Quixin. We expect growth in Europe will come from the launch of these new products along with further expansion in the Western European markets.

We continued to expand our presence in Asia with the



opening of new offices in China and South Korea and are actively working to register new products throughout the area.

Research and Development

Innovation in ophthalmology and rheumatology

Santen's strength resides in its R&D efforts in the therapeutic fields of ophthalmology and rheumatology. Our focus is on the discovery of new molecules and the development of ophthalmic solutions from known molecules. We have strengthened our R&D capability in the areas of glaucoma, corneal and retinal diseases and drug delivery systems (DDS). These efforts have helped the Company to develop a strong R&D pipeline and achieve excellent business performance.

We increased R&D expenditures by 14.0% to ¥10,511 million in fiscal 2000 and will continue to increase R&D spending in fiscal 2001. In addition to increasing our spending on R&D, we are making efforts to improve productivity and streamline the development of products that will have a significant impact on patients' quality of life. We have made significant progress in the last few years in developing a global R&D organization by integrating the efforts of our groups in Japan, the U.S., Finland and Germany. Also, a number of recent developments in the life sciences such as combinatorial chemistry, high throughput screening, and structure-based drug design have helped our research teams accelerate the investigation of compounds and increase our productivity.

Santen continues to actively pursue technological alliances and collaboration projects with the world's leading companies and research centers. In fiscal 2000, the Company entered into in-licensing agreements with Adolor Corporation

for ADL2-1294 (analgesic ophthalmic solution) and Nippon Organon K.K. for Lomerizine HCl (anti-glaucoma treatment). We also finalized an agreement with Centocor, Inc. for anti-APO-1 antibody, a biological agent representing a new mechanism of action in the treatment of serious rheumatological disorders. We believe that our emphasis on R&D, along with our strong market position, will help us in our goal to become the most effective and valued partner for companies that want to out-license products for use in ophthalmology or rheumatology.

Innovation of Management

Adapting to change

In the 21st century social change will accelerate at an unprecedented rate, bringing about significant changes in the business environment, consumers' outlooks and lifestyles. Santen's focus in this constantly changing world is to encourage management to balance long-term strategy with the need to anticipate and quickly adapt to changes. To foster such management, Santen is creating an environment that is both flexible and creative. We have been working to streamline the organization structure by flattening the corporate hierarchy and creating flexible teams to work on projects. In addition, we recently established the Santen Innovation Project to enhance employees' knowledge, motivation and leadership skills at all levels of the organization.

Santen has also been changing its organization to improve corporate governance and increase managerial accountability. Recent actions include the appointment of outsiders to the corporate governance structure and the formation of an Executive Compensation Committee which also includes individuals from outside the company. Santen is committed to increasing corporate value by creating a management structure that is increasingly adaptable to market trends and operates with greater corporate transparency.

Santen will continue to concentrate its managerial resources on business sectors where it can most effectively exert its competitive edge, thereby consolidating and improving its market position. Santen will continue to use its outstanding R&D capabilities to achieve its primary goal of providing to the world products and services that improve patients' quality of life.

August 2001

Takakazu Morita
President & Chief Executive Officer

Santen has been making improvements in the areas of corporate governance, risk management and human resources development in order to maximize shareholder value.

Corporate Governance

Santen has introduced a number of changes to its organization in order to clarify managerial responsibilities, streamline decision making and insure that business operations are conducted in accordance with company standards. The following changes were implemented to help Santen move beyond the traditional Japanese corporate structure and become a world class organization.

● **Balanced Scorecard**

Santen introduced the Balanced Scorecard system to help ensure that all executive officers' goals are in accordance with the overall corporate goals. All Santen directors set individual objectives addressing the areas of Financial Performance, Customer Service, Internal Business Process, and Learning and Growth. Their performance is then evaluated using the balanced scorecard system. Employing this performance measurement system helps everyone in the company remain focused on maximizing corporate value.

● **Management Advisory Committee**

Santen established a management advisory committee with responsibility for strategic planning and corporate governance. The committee includes individuals from outside the company in order to gain the perspective of other business leaders.

● **Executive Officer System**

In order to clarify managerial roles, the company appointed a number of executive officers with the responsibility of ensuring that business operations are carried out promptly and in adherence with management decisions.

● **Executive Compensation Committee**

Santen firmly believes in performance-based compensation. The company established an executive compensation committee to determine fair compensation levels and monitor the appropriateness of compensation payment systems. This committee also includes individuals from outside the Company who provide expertise in global compensation programs.

● **Stock Option Plan**

The Company introduced a stock option plan as part of its evaluation/compensation system. The plan is designed to enhance director motivation for achieving objectives and

advancing the Company's business performance, thereby contributing to corporate value.

Risk Management

All activities carry a certain amount of risk, although causes and seriousness vary. How a company avoids risk or meets a serious challenge is closely related to its corporate culture and the quality of its management. Santen emphasizes the importance of all employees thoroughly understanding its Corporate Philosophy and insures that all actions reflect that philosophy.

In June 2000, a bottle of eyedrops contaminated with a foreign substance was sent to Santen in an extortion attempt. Santen reacted to this situation with an immediate disclosure to the public of all relevant information, and immediately recalled all its OTC eyedrops from the market. All decisions were made by a crisis management committee led by the president. All of their actions were based on our belief that customer safety is Santen's first priority. To prevent similar incidents from occurring in the future, Santen developed and rapidly introduced a new tamper-resistant wrapping for all OTC eyedrops.

**Human Resource Development
Greater Organization Capability and
Higher Employee Motivation**

Santen's objectives in this changing business environment are to develop a flexible, creative organization and provide all employees with the skills and motivation to meet individual and corporate objectives. The Company's organizational guidelines are: developing clear strategies; creating targets and a vision that supports Santen's basic policy; and pursuing innovation by creating new products, services and processes. Our initiative is to continually learn from the world's best practices and apply them in our jobs on a daily basis.

Santen is redesigning its organizational structure by flattening the corporate hierarchy and moving towards project teams with superior lateral communication and flexibility. These actions will allow us to best use our resources and more readily adapt to fluctuations in the business environment.

Santen is also active in human resource development to ensure that employees can fulfill higher responsibilities by exercising good judgment and acting independently, while appreciating their contribution to society through their work. The Santen Innovation Project is designed to enhance employee motivation and to develop corporate leaders and employees of the highest caliber.



Sitting from left: Katsuhiko Waga, Masahiro Mita, Takakazu Morita, Kunihiko Shimotsu, Akira Kurokawa
Standing from left: Toshiaki Nishihata, Takeo Yamaoka, Akira Maeda, Kyoichi Shimomura, Merwin Jerold Hansen, Yukinobu Kadobe, Ichiro Otokozaawa, Hiroshi Abe, Kenji Iwamoto

Board of Directors

- Takakazu Morita**
President & CEO
Head of Corporate Management and Ophthalmic Research Division
- Masahiro Mita**
Managing Director
Head of Corporate and Regulatory Affairs
- Kunihiko Shimotsu**
Managing Director
Corporate
- Merwin Jerold Hansen**
Director, Corporate Officer
President of Santen Incorporated
- Katsuhiko Waga**
Director, Corporate Officer
Head of Product Supply Division
- Akira Kurokawa**
Director, Corporate Officer
Head of Sales & Marketing Division, Prescription Pharmaceuticals

Corporate Officers

- Kyoichi Shimomura**
Corporate Officer
Head of Development Research Division
- Yukinobu Kadobe**
Corporate Officer
Head of Clinical Development Division
- Toshiaki Nishihata**
Corporate Officer
Head of R&D Strategic Integration Division and QA, QC & Environmental Auditing Division
- Akira Maeda**
Corporate Officer
Head of sales & Marketing Division-OTC Products
- Kenji Iwamoto**
Corporate Officer
Head of Asia Division

Corporate Auditors

- Syushi Sakamoto**
Corporate Auditor
- Takashi Ishida**
Corporate Auditor
- Koji Hori**
Corporate Auditor
- Kosei Furukawa**
Corporate Auditor

(As of June 28, 2001)



SALES AND MARKETING

Prescription Ophthalmic Pharmaceuticals

Ophthalmic Pharmaceuticals

● Japan

In fiscal year 2000, the revised National Health Insurance Drug Price Standard went into effect on April 1, resulting in an average 7% drop in official pharmaceutical drug prices. This revision regularly occurs once every two years and generally tends to reduce drug prices; however, the average 7% price reduction was especially large. Santen anticipated these price reductions and, by marketing effectively both new and current products, increased fiscal 2000 ophthalmic pharmaceutical sales by 8.4% to ¥67,919.

In April 2000, Santen launched Cravit (active ingredient: levofloxacin), a highly effective next-generation quinolone anti-infective ophthalmic solution and successor to Santen's Tarivid (active ingredient: ofloxacin). Featuring a broad anti-infective spectrum and an exceptional ability to penetrate ophthalmic tissue, Cravit quickly gained the reputation among opinion leaders as the best-in-class treatment for conjunctivitis, keratitis, and other ophthalmic infections. Cravit quickly became the number-two ophthalmic anti-infective with first-year sales of ¥8,543 million. Tarivid remained the number-one anti-infective in ophthalmology with sales of ¥11,639 million.

In fiscal year 2000 we continued to see a great increase in the use of personal computers and the popularity of the Internet. This increase in the use of personal computers has been accompanied by an increase in the incidence of dry eye syndrome, which generally is caused by an insufficiency of tears bathing the eye. Symptoms of dry eye may range from mild redness and discomfort to serious corneal disease.

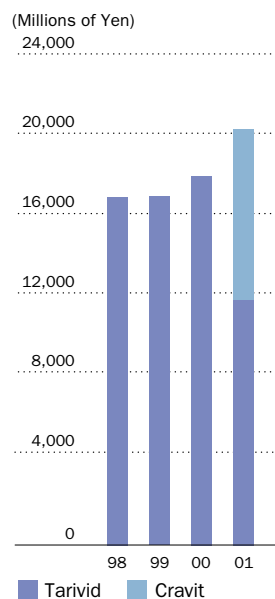
To treat the corneal diseases, Santen developed Hyalein (active ingredient: sodium hyaluronate). Hyalein features superior viscoelasticity and both protects the cornea and effectively repairs corneal epithelium damage resulting in a significant improvement in the quality of life for patients suffering from dry eyes. In order to help raise awareness of dry eye and create marketplace pull, Santen launched a highly effective newspaper ad campaign that explained the syndrome. The campaign reached dry eye sufferers across the country and helped Hyalein sales grow 15.9% to ¥10,758 million.

In January 2001, the Company launched Livostin, an anti-allergy ophthalmic solution featuring a strong H-1 receptor antagonist effect. Combined sales of Livostin, Alegysal and Zaditen totaled ¥6,938 million in fiscal 2000.

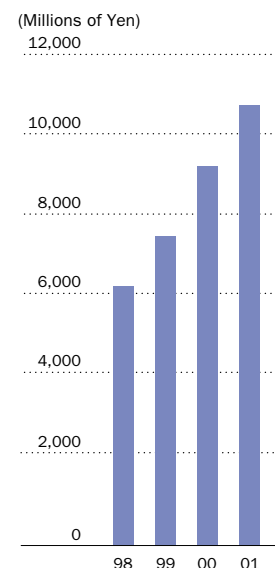
Glaucoma is the second leading cause of blindness and affects primarily people over 40 years old. Although it is a serious disease, glaucoma can be effectively treated with pharmaceuticals that lower the build-up of pressure in the eye. As the Japanese population ages, the market for anti-glaucoma ophthalmics continues to grow rapidly. To better serve this market's needs, Santen launched Timoptol-XE (active ingredient: timolol maleate) a once-a-day gel formulation of Timoptol, a twice-a-day solution. Sales of both drugs totaled ¥7,997 million in fiscal 2000.

Backing up the launch of these new products is Santen's impressive force of over 400 medical representatives. Each of these MRs, as they are known in Japan, carries a portable computer, through which product information is accessed and presentations made to medical professionals. In fact, one reason for the great success of Cravit in FY 2000 was the MRs' ability to communicate key visuals and messages to doctors through presentation software.

Sales of Cravit and Tarivid



Sales of Hyalein



This large and effective sales force is the Company's premier means of communicating its messages, but the MRs are supported by a strong system of information services. In addition to providing information on its products, the company produces a wide range of free medical information-pamphlets, posters, videos, and a Web site-for use by medical professionals and their patients. The company also conducts seminars and symposia offering a wide range of information to medical professionals.

● Overseas

In fiscal 2000, Santen achieved a milestone when it started direct marketing and selling of prescription ophthalmic pharmaceuticals in the U.S.A. In July 2000 Santen launched its first product: Alamast (active ingredient: Pemirolast potassium), a mast cell stabilizer marketed in Japan as Alegysal. This was quickly followed by the launch of Quixin (active ingredient: levofloxacin; marketed as Cravit in Japan) in November 2000. Quixin is the latest-generation quinolone and is highly effective in treating bacterial conjunctivitis and other ophthalmic infections. In January 2001, the Company began direct promotion of Betimol (active ingredient: timolol hemihydrate), a beta blocker used in the treatment of glaucoma.

Santen promotes its products directly to ophthalmologists and optometrists in the U.S. with its own sales team. In addition, the Company has entered into co-promotion agreements with partners to promote its products to pediatricians, primary care physicians, oto-laryngologists and allergists.

In Europe, Santen has focused on the Northern and Eastern European ophthalmic markets. The company promotes its products in more than 30 countries, including all Nordic and Baltic countries and Russia. We expect sales growth in this region will come from the launch of products already proven to be competitive in Japan, as well as further geographic expansion in Western European markets.

In Asia, Santen markets its products in ten countries and districts: China, Hong Kong, Taiwan, South Korea, the Philippines, Thailand, Malaysia, Singapore, Vietnam, and Indonesia. To complement its Beijing office, in April 2000 the Company opened an office in Guangzhou. In July 2000, the company established Korea Santen Pharmaceutical Co., Ltd., a wholly owned subsidiary operating in South Korea. Santen has been active in pursuing official registration for its products throughout Asia. The registration of Cravit was completed in Hong Kong in November 2000 and in South Korea in April 2001.



Santen Incorporated (California)



Santen Oy (Finland)



Anti-rheumatic Pharmaceuticals

As of fiscal year 2000, the number of Japanese people suffering from rheumatoid arthritis was estimated to be 700,000 and, as the population ages, this number will continue to grow. For the treatment of this serious disease, the Company currently offers AzulifidineEN (active ingredient: salazosulfapyridine) and Rimatil (active ingredient: bucillamine), both of which are disease modifying anti-rheumatic drugs (DMARDs). Featuring strong anti-rheumatic and anti-infective effects as well as a quick onset of action, in FY 2000 Azulifidine had sales of ¥2,349 million, a 12.1% increase over the previous year's results. Rimatil features superior efficacy and is becoming Japan's standard anti-rheumatic drug among DMARDs with sales of ¥4,380 in fiscal 2000. The Company also seeks to improve patients' quality of life by offering a wide range of information for use by doctors and their patients.

OTC Pharmaceuticals

Since the launch of Daigaku eye drops in 1897, Santen has been committed to the development, production, and marketing of excellent over-the-counter pharmaceuticals. Focusing chiefly on ophthalmics, the Company has brought many innovative, consumer-oriented products to the market. For example, Santen was the first company to use plastic containers for ophthalmic products in Japan.

Santen works closely with retailers in Japan to help increase sales. Plans are tailored to individual store location conditions in a planning process that fully incorporates Santen's belief that "stores are the battlefield of advertising". Santen also helps retailers by maintaining a large number of product lines specifically targeting customer groups. The Company's OTC ophthalmic solutions include Sante de u Plus E, containing natural Vitamin E in addition to Vitamin B12; Sante 40 series, targeting middle-aged consumers for the relief of blurred vision and eye fatigue; and Sante FX Neo, with a stronger refreshing feeling at instillation, targeting young consumers. To further enrich its product portfolio, the Company commenced sale of Sante Eyesupli in fiscal 2000, targeting health conscious, middle-aged female consumers.



Fiscal year 2000, however, was a difficult period for this business. At the beginning of FY 2000, Santen's OTC business faced the substantial challenges of a sluggish economy and continued price deflation. In June, the Company had to deal with an extraordinary situation when an attempt was made to extort money from the company by a person threatening to tamper with its OTC products. (The police soon apprehended this individual, and no evidence of actual tampering was ever found.)

Holding customer safety and trust above all, the Company reacted quickly to the situation and immediately recalled all of its OTC products from the marketplace. Further, to help restore and maintain customer trust, the Company quickly improved the tamper-resistance of its entire OTC product line. Due to the product recall, however, sales of OTC pharmaceuticals declined 24.5% to ¥5,255 million in fiscal 2000.

Ophthalmic Devices

Santen also competes in the ophthalmic device business with the sale of phacoemulsifier machines for cataract surgery, intraocular lenses and surgical instruments.

In fiscal 2000, the Company commenced sale of foldable silicon intraocular lenses and microkeratomes boosting sales in this business sector to ¥1,144 million, a 12.4% increase over the previous year. Santen's business affiliates, Phacor and Lenstec are engaged in R&D for cataract surgery equipment and intraocular lenses, respectively. The products from these groups will allow us to continue to provide ophthalmic surgeons with excellent technologies and products to use in cataract and refractive surgeries.



Microkeratome



PRODUCTION AND LOGISTICS

Domestic and Overseas Production Facilities

Santen has manufacturing facilities in Japan (Osaka, Noto and Shiga) and Finland. The plant in Osaka manufactures BSS Plus (ophthalmic irrigating solution), eye ointments and other pharmaceuticals. The Noto plant, Santen's largest manufacturing facility, manufactures prescription ophthalmic pharmaceuticals including Cravit, Hyalein and Kary Uni, and all OTC ophthalmic solutions. Flumetholon, Pivalephrine and other ophthalmic suspensions and dissolve-and-use type eyedrops are manufactured at the Shiga plant. The manufacturing plant in Finland produces prescription ophthalmic pharmaceuticals for the American and European markets.



Noto Plant

Production System Yielding Unsurpassed Quality Products

Santen has pioneered a number of technologies designed to improve pharmaceutical manufacturing. We introduced BlowFillSeal technology (simultaneous blow molding and filling) into our ophthalmic solution manufacturing process in 1977, establishing a sterilized packaging system based on this new technology. In 1992, we adopted the Tip & Cap System, which enabled higher production quality and advanced user-friendliness. The Bottle Pack System was adopted four years later, leading to productivity improvement.

In fiscal 2000, we started productivity improvement projects at the Noto and Shiga plants. We are actively working to reduce production costs by constantly reviewing the efficiency of existing systems and processes, including system operation rates and filling system yield percentages. Santen plans to further improve productivity by reducing product supply lead-time, and promoting "Zero Claim Initiatives."

In June 2000, Santen was the target of an extortion attempt that began when a bottle of eye-drops maliciously mixed with foreign substances was delivered to the Company with an extortion letter. Within two weeks from the onset of the crime, Santen introduced a new system into the Noto Manufacturing Plant to provide tamper-resistant wrapping for all OTC eye drops.





RESEARCH AND DEVELOPMENT

One of Santen's key goals is to create pharmaceuticals that improve patients' quality of life, and to do so as efficiently and speedily as possible. With this in mind, researchers at Santen are dedicated to the development of ophthalmic and anti-rheumatic drugs that dramatically and positively impact patients' quality of life. Their research efforts are focused on the fields of ophthalmic therapeutics, and bone and articulation therapeutics, with special attention given to anti-rheumatic treatments.

Research and Development—Ophthalmology

Santen's ophthalmic pharmaceutical R&D comprises two main areas: new molecule development and the development of ophthalmic solutions from known molecules. An example of the latter is Santen's development of Hyalein (active ingredient: sodium hyaluronate) for the treatment of keratoconjunctival disorders. Long used in the treatment of arthritis as well as in cataract removal and other surgeries, sodium hyaluronate was well known for its viscoelastic and moisture-retaining properties. Aware of this molecule's therapeutic value, Santen's R&D team developed Hyalein ophthalmic solution, which is now being used to treat corneal illnesses across Japan.

The development of Hyalein is also an example of Santen's customer-oriented approach to R&D. The Company noted that the needs of dry eye patients were largely unmet. In order to ensure patients' and medical professionals' needs would be fulfilled, Santen carefully studied the needs of dry eye patients, compiled a vast database of information regarding possible treatment regimens, and after a careful analysis of this information developed Hyalein to meet the needs of patients and doctors.

Most of the company's research into ophthalmic therapeutics takes place at the Nara Research and Development Center, Santen's R&D nucleus. At the center, researchers continuously engage not only in R&D itself, but also work on projects that seek to improve the quality and speed of research and development. Currently, researchers are focusing on three major long-term improvement goals: improvement of molecule search protocols; improvement of overall R&D quality, volume, and speed; and improvement of the R&D-Clinical Development interface.

The world-class facilities at the Nara Research and Development Center are one of Santen's main strengths in R&D, but they are not the sole strength. Santen also maintains a strong network of relationships with research institutions and hospitals both in and outside Japan. Through collaborating with renowned ophthalmic researchers and physicians around the world, Santen aims not only to improve its own expertise in ophthalmic treatments, but also to raise the world standard of knowledge in this important area.



Nara Research and Development Center

To reinforce its new drug pipeline as well as further focus on its long-term R&D improvement goals, in May 1999 Santen R&D undertook a complete review of its organizational structure and greatly revamped its research procedures. This project continued into FY 2000 and the outcome was an R&D structure with strong leadership and clearly defined tasks that will lead to improvements in overall R&D efficiency and quality. Santen's ophthalmic researchers are now divided into three major groups specializing in glaucoma, corneal inflammatory diseases, and the retina. In addition to those three groups, which engage primarily



in therapeutic molecule search, there are two groups specializing in drug delivery systems and pharmacokinetics. Members from all five groups form flexible teams that investigate not just the constituent parts of a new drug, but also the drug as a whole: molecule, DDS, pharmacokinetic impact, and, especially, overall impact on the disease, healthy tissue, and total quality of life.

In the world today, the spotlight is on genomic drug discovery, a pioneering field capable of changing medical care and pharmaceuticals as we know them. Santen is at the forefront of introducing genomic drug discovery-related technologies into ophthalmic pharmaceutical R&D through its alliances with experts and other advanced research institutes.

Research and Development—Rheumatology

Santen's cutting-edge research in the area of rheumatology has resulted in the development of Rimatil (active ingredient: bucillamine), a widely prescribed oral medication. Santen's has also achieved wide recognition for its research into immunosuppression and the treatment of cartilage deterioration.

In the search for molecules to treat such rheumatological disorders as arthritis, Santen employs the latest in computerized research technologies. Combinatorial chemistry (CC) allows the simultaneous synthesizing of multiple compounds and high throughput screening (HTS) allows

the fast screening of multiple samples by computer-controlled robots. Santen's combined use of these two powerful technologies allows for the quick creation of potential therapeutic molecules and their subsequent examination.

In addition, Santen's researchers employ structure-based drug design (SBDD), to designing drug structures by means of computer software. And, as in the area of ophthalmology, Santen is also conducting genomic drug research that may lead to new anti-rheumatic treatments.

Global Clinical Development

Santen has structured its clinical group to leverage its strengths in Japan, the U.S., and Europe. The integration of these groups has allowed Santen's researchers to quicken the pace of clinical development. Fiscal year 2000 was very productive for Santen's clinical development team. In Japan, Santen filed new drug applications in February 2001 for ophthalmic green 25 mg for intravenous injection, a diagnostic agent for chorioretinal diseases; and in April 2001, Santen filed a new drug application for Tiopronin, a Cystinuria treatment. In the United States, Santen received FDA approval for Quixin (marketed as Cravit in Japan) in August 2000, in UK, we received MCA approval in August 2001. New drug applications have also been filed for Quixin and Alamast in Europe. Other products in late stage development include DE-076 (Cyclosporine) an immunosuppressive ophthalmic solution and DE-081 an anti-inflammatory ophthalmic solution. Other products in clinical trials include Hyalein (a treatment for dry eye syndrome) in Europe phase II trials and Quixin 1.5% anti-infective in U.S. phase III trials.



The library of Nara Research and Development

Business Development

Santen has established a global network of companies helping it achieve its R&D goals. This network comprises pharmaceutical companies, universities, research centers, venture businesses and fine-chemical manufacturers, each playing a role in the creation of new therapies.

The development of ophthalmic and anti-rheumatic pharmaceuticals requires diverse technological knowledge. Through in-licensing and collaborative development, Santen has combined necessary technologies, enhanced its R&D capabilities, and maximized the value of its product portfolio. In April 2000, Santen concluded a licensing agreement with Adolor Corporation for an analgesic ophthalmic solution with a unique mechanism of action; this drug is expected to improve quality of care for the increasing number of patients undergoing various eye surgeries.

In December 2000, Santen entered into a licensing agreement with Nippon Organon K.K. for anti-glaucoma treatment (lomerizine HCl); this drug also has a unique mechanism of action that is attracting the attention of physicians.

In the area of rheumatology, Santen in February 2001 signed a licensing agreement with Centocor, Inc. for a product employing the anti-APO-1 antibody, a biological agent that yet again represents a new mechanism of action and could thus become a new way to treat serious rheumatological disorders.

● Japan

Stage	Trade name/code No. (Generic name)	Indication	Original / in-licensing	Notes
Launched, April 2000	Cravit (Levofloxacin)	Bacterial conjunctivitis	Daiichi Pharmaceutical	Applied Daiichi's antibiotic to ophthalmic treatment
Approved in June 2001	Detantol (Bunazosin)	Glaucoma	Eisai	New anti-glaucoma agent featuring aqueous outflow promotion by α 1-blocker
NDA filed	Ophrhagreen for Intravenous Injection (Indocyanin green)	Diagnosis of chorioretinal disease	Daiichi Pharmaceutical	The determination of the most effective therapy for age-related macular degeneration and rare or intractable diseases
	DE-007 (Tiopromin)	Cystinuria	Original	Line extension of Santen's Tiora / Orphan drug
Phase III	DE-074 (Fibronectin)	Persistent corneal epithelial defect	Japan Chemical Research	Orphan drug
Phase II	DE-076 (Cyclosporine)	kerato-conjunctivitis	Licensed-in	A new agent for vernal keratoconjunctivitis with new action mechanism (Orphan drug)
	DE-081 (Apafant)	Allergic conjunctivitis	Licensed-in	Platelet aggregation factor antagonist
Preparing for bridging study	DE-087 (Brimonidine)	Glaucoma	Allergan	Marketed in USA by Allergan Inc. as "Alpha-gan"

● USA

Stage	Trade name/code No. (Generic name)	Indication	Original / in-licensing	Notes
Launched, July 2000	Alamast (Pemirolast)	Allergic conjunctivitis	Mitsubishi Tokyo Pharmaceutical	Marketed in Japan as "Alegysal"
Launched, November 2000	Quixin 0.5% (Levofloxacin)	Bacterial conjunctivitis	Daiichi Pharmaceutical	Marketed in Japan as "Cravit"
Phase III	Quixin 1.5% (Levofloxacin)	Bacterial corneal ulcer	Daiichi Pharmaceutical	Line extension of Quixin

● Europe

UK

Stage	Trade name/code No. (Generic name)	Indication	Original / in-licensing	Notes
Approved in August 2001	Quixin 0.5% (Levofloxacin)	Bacterial conjunctivitis	Daiichi Pharmaceutical	Scheduled to apply through the Mutual Recognition Procedure in EU countries except UK
Phase II	Hyalin (Hyaluronic acid)	Kerato-conjunctival epithelial disorder	Original	Marketed in Japan as "Hyalein"

France

Stage	Trade name/code No. (Generic name)	Indication	Original / in-licensing	Notes
NDA filed under mutual recognition	Alamast (Pemirolast)	Allergic conjunctivitis	Mitsubishi Tokyo Pharmaceutical	Marketed in Japan as "Alegysal"

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Corporate Citizenship Activities

People enjoy beauty and express their feelings with their eyes. Santen aims to contribute to society by "protecting the joy of sight". As part of our corporate citizenship activities, we provide financial and material support to eye-care-related organizations and social welfare groups throughout the world. The Company provides support to the Helen Keller Foundation for Research and Education, the Japan Eye Bank Association and the Japan National Society for the Prevention of Blindness. We also provide scholarships to ophthalmologists in China and donate pharmaceuticals to the Vietnam Blind Association and the Mercy Ships. In addition to ongoing philanthropic activities, Santen has also provided financial support and drugs to sufferers of earthquakes and natural disasters including victims of the 1995 Hanshin Great Earthquake, the volcanic eruption on Miyake Island and the tragic earthquakes in Colombia and India.

Environmental Initiatives

Santen is committed to ecological protection and environmental conservation. Santen established its Basic Environmental Policy in 1998 and has since undertaken a broad range of activities under the five guiding principles of: developing and improving an environmental management system; compliance with all environmental laws and regulations; promoting natural resource conservation, energy saving, and recycling; implementing training for environmental awareness enhancement; and environment-related information disclosure.



Santen established its own environmental management system, applicable to its headquarters, all research centers and branch offices in Japan, and commenced the operation of this system in April 2001. Under this new system, environmental activities are promoted by reducing electricity, gas and other utility consumption for natural energy saving, and by strictly separating recyclables from waste for natural resource conservation.

We have established a goal of obtaining ISO 14001 certification, an international standard for environmental management systems, for all our manufacturing plants in Japan. This certification was granted to the Shiga plant in December 1999 and the Osaka plant in June 2001 and preparations are in progress for certification of the Noto plant.

Basic Environmental Policy

To hand down the Earth to our next generation in its best form, Santen in the 21st century will make greater environmental contributions in tandem with international undertakings, to meet global environmental challenges. In the strong consciousness of corporate citizenship, individuals working at all Santen group companies will be unceasing in their activities to protect, conserve and improve the natural environment. All Santen group companies and environmental management implementation teams must deeply understand this Policy, develop environmental plans to embody this Policy, and operate and maintain the Company's environmental management system to attain the goal set forth in this Policy.

Five-year Summary

Years ended March 31

	Millions of yen, except per share information					Thousands of U.S.dollars, except per share information
	2001	2000	1999	1998	1997	2001
For the year:						
Net sales	¥ 88,449	¥ 83,577	¥ 79,639	¥ 77,957	¥ 75,216	\$ 713,873
Cost of sales	33,385	32,195	32,746	31,278	27,552	269,449
Selling, general and administrative expenses	38,546	33,894	30,294	30,535	27,984	311,109
Operating income	16,518	17,488	16,599	16,144	19,680	133,315
Interest expense	430	462	588	654	624	3,474
Income before income taxes	15,521	14,422	15,969	14,917	18,913	125,269
Net income	7,714	7,941	8,105	7,323	8,998	62,258
Capital expenditures	4,943	2,510	3,443	5,898	16,725	39,894
Depreciation and amortization	5,683	5,725	6,314	6,674	4,202	45,871
R&D expenditures	10,511	9,221	7,335	7,731	6,213	84,833
Per share data (yen and dollars):						
Net income	¥ 81.32	¥ 83.54	¥ 85.27	¥ 77.06	¥ 105.32	\$ 0.66
Cash dividends, applicable to period	20.00	12.00	12.00	12.00	12.00	0.16
At year-end:						
Current assets	¥ 88,025	¥ 82,218	¥ 78,018	¥ 70,892	¥ 69,065	710,455
Net property, plant and equipment	36,684	37,416	39,638	43,425	47,278	296,076
Total assets	153,243	149,968	144,913	138,822	140,226	1,236,826
Short-term borrowings and long-term debt	25,482	26,491	27,496	31,219	31,807	205,664
Total shareholders' equity	94,834	95,669	88,950	81,998	75,759	765,407

Note: 1. U.S.dollar amounts have been translated from yen, for convenience only, at the rate prevailing on March 30, 2001. of ¥123.90 to U.S.\$1.
2. See Note 2.xii) and 10 of Notes to Consolidated Financial Statements in respect of per share data.
3. Net sales in 2001 includes royalty income which was presented as "Other" in "Other income" until the previous year.

OVERVIEW

Net sales increased by ¥4,872 million (5.8%) to ¥88,449 million mainly due to strong sales of prescription ophthalmic pharmaceuticals. Sales included ¥78,878 million prescription pharmaceuticals, ¥5,255 million over-the-counter (OTC) pharmaceuticals, ¥1,144 million ophthalmic medical devices and ¥3,172 million other.

Operating income decreased by ¥970 million (5.5%) to ¥16,518 million as an increase in gross profit was offset by higher selling, marketing and research and development (R&D) expenses.

Net income declined ¥227 million (2.9%) to ¥7,714 million as the impact of an increase in the effective tax rate was partially offset by reductions in other expenses. Details of operational results are discussed in the following section.

● **Sales**

[Prescription Pharmaceuticals]

Sales of prescription pharmaceuticals increased by ¥5,710 million (7.8%) to ¥78,878 million.

“Ophthalmic Pharmaceuticals”

Prescription ophthalmic pharmaceutical sales increased 8.6% to ¥71,231 million in FY2000. Japan sales increased 8.4% due, in part, to the successful launch of Cravit, an anti-infective ophthalmic solution, in April 2000; and Livostin, an anti-allergic ophthalmic solution, in January 2001. Sales of Hyalein, a keratoconjunctival treatment, and Timoptol-XE, an anti-glaucoma solution introduced in November 1999, also showed strong growth in FY2000.

Sales in overseas markets increased 13.2% to ¥3,312 million. Santen entered the U.S. ophthalmic market in FY2000 with three product launches. Alamast, an anti-allergy solution, was launched in July 2000; Quixin, an anti-infective solution, was launched in November 2000 and we began direct sales of Betimol, an anti-glaucoma solution, in January 2001. Strong marketing activities in Europe resulted in increased sales in FY2000 despite the weakness of the yen against the Euro and sluggish economic conditions in Russia and Eastern Europe.

“Anti-rheumatic Pharmaceuticals”

Sales of anti-rheumatic pharmaceuticals increased 6.7% to ¥6,729 million with due to sales growth of AzulfidineEN and Rimatil. AzulfidineEN, a disease modifying anti-rheumatic drug (DMARDs), posted strong sales growth and is quickly becoming the first choice DMARDs for early stage rheumatics.

[OTC Pharmaceuticals]

In the first half of FY 2000, Santen voluntarily recalled all OTC products from the market following an extortion threat. Product supply resumed following introduction of improved tamper-proof packaging technology and, in an effort to restore sales levels, the sales organization was reinforced to emphasize proposal-type marketing to retailers. In February 2001, “Sante Eyesupli” was launched targeting middle-aged, health-conscious women. Despite these efforts, sales in the OTC business segment declined 24.5% to ¥5,255 million due to impact of the recall.

[Medical Devices]

Sales of medical devices grew 12.4% to ¥1,144 million thanks to efforts augmenting the sales organization and solid sales of the Microkeratome introduced in September 2000.

[Other]

Sales of other products grew 30.7% to ¥3,172 million primarily due to increased contract production in the U.S. In addition, royalty income was re-classed from other income to net sales in FY2000.

● **Cost of Sales, and Selling, General and Administrative Expenses**

The ratio of cost of sales to net sales improved 0.8 percentage points to 37.7% due to a favorable change in product mix along with decreased depreciation of manufacturing equipment.

Selling, general and administrative expenses increased by ¥4,652 million (13.7%) to ¥38,546 million mainly due to the start-up of direct ophthalmic pharmaceutical sales in the U.S., increased promotion spending in Japan related to new product launches and higher investments in R&D. R&D expenses increased by 14.0% to ¥10,511 million as we continued to expand our global development activities and entered into technical alliances with three companies for prescription ophthalmic and anti-rheumatic pharmaceuticals.

● **Operating Income**

Combination of the above items resulted in a ¥970 million (5.5%) decline in operating income to ¥16,518 million in FY 2000. Operating margin decreased from 20.9% in the previous year, to 18.7% in FY 2000.

● **Other Income and Deductions**

Other income decreased by ¥93 million (5.5%) to ¥1,599 million in FY2000 due to the re-class of royalty income to net sales.

Other deductions were reduced by ¥2,162 million (45.4%) to ¥2,596 million. FY2000 other deductions included ¥907 million expenses related to the OTC eye drops recall and ¥446 million loss due to the revaluation of golf membership rights to current market prices. The improvement in other deductions was due, in part, to certain one-time events in the prior year; FY1999 other deductions included losses from Princeton Notes and a write-off related to a change in the accounting standard for retirement benefit.

● **Income Taxes**

Income taxes increased by ¥1,326 million (20.5%) to ¥7,807 million. The effective tax rate increased from 44.9% in FY1999 to 50.3% due to higher revenue growth in Japan with a relatively high tax rate.

● **Net Income**

Income before income taxes increased over prior year. However, net income decreased by ¥227 million (2.9%) to ¥7,714 million due to the increased tax liability in FY2000.

The ratio of net sales dropped from 9.5% in the previous year to 8.7% and return on equity dropped from 8.6% to 8.1%.

Net income per share for the year was ¥81.32, compared with ¥83.54 in FY1999. Diluted net income per share was ¥75.01, compared with ¥77.04 in the prior year.

LIQUIDITY and CAPITAL RESOURCES

● **Funding and Management of Liquidity**

Companies are committed to securing necessary funds for business operations and maintaining proper liquidity of funds and a proper balance sheet. We have concluded credit line commitment agreements with financial institutions so that we can quickly acquire funds as needed. The liquidity of funds on hand is also maintained at a proper level, for optimally efficient use of funds.

Cash requirements in FY2000 were provided from operations.

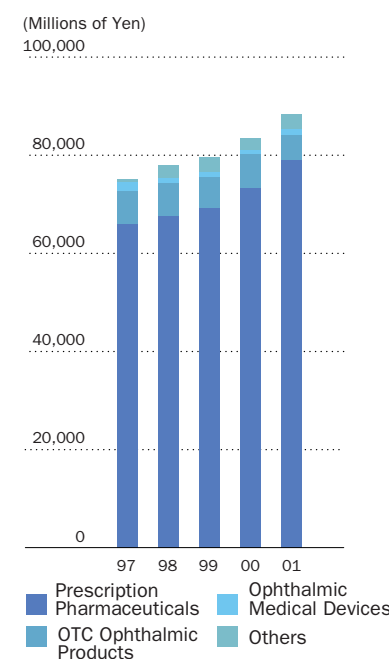
In addition, Santen used retained earnings to repurchase 2,387 thousand shares at ¥5,085 million, which were then retired.

● **Assets, Liabilities, Shareholder's Equity**

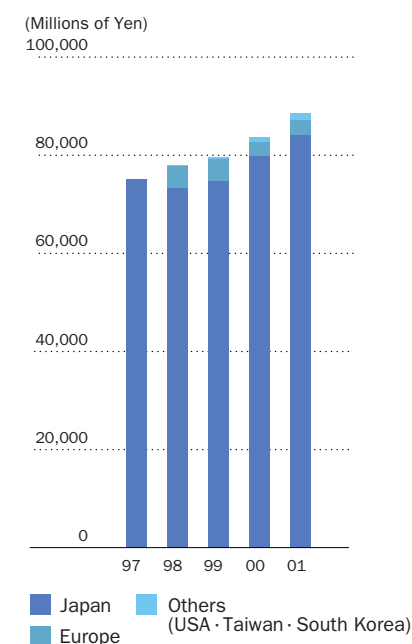
Total assets increased by ¥3,275 million (2.2%) from the previous year to ¥153,243 million.

The increase in current assets resulted from an increase in trade

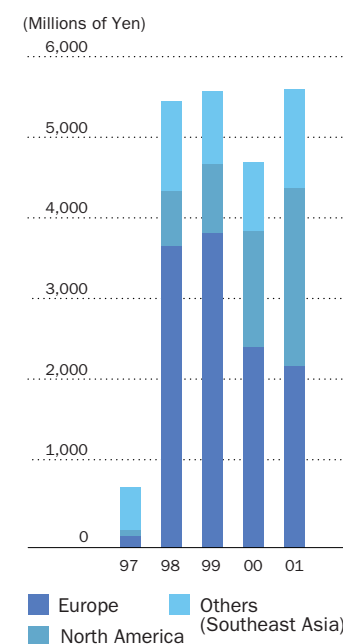
Sales by Division



Sales by Geographic Areas



Overseas Sales



receivables due to sales growth, and an increase in cash and cash equivalents resulting from the investment of increased funds in time deposits. Trade receivables include ¥5,992 million not collected on the closing date of FY2000 because it was a financial holiday.

Property, plant and equipment decreased as the capital invested in production facilities for prescription pharmaceuticals and research and development (¥3,039 million) was less than total depreciation expenses in FY2000.

Investments and other assets increased due to changes in Japanese accounting standards. Short-term investments valued at ¥2,065 million were reclassified to investment securities, and a profit of ¥2,224 million was recorded for the valuation of securities at year-end market prices.

Total current and non-current liabilities increased by ¥4,110 million (7.6%) to ¥58,409 million. Current liabilities increased due to payables associated with purchases of fixed assets, advertising expenses and sales rebates.

Non-current liabilities following the repayment of long-term debts.

Total shareholders' equity decreased by ¥835 million (0.9%) to ¥94,834 million. Net income increased to ¥7,714 million, but

retained earnings decreased due to the repurchase and retirement of our shares in the amount of ¥5,085 million, and increased dividend payments of ¥381 million to shareholders. In FY2000, ¥2,224 million after-tax profit was recorded as valuation variance of other securities following the market price evaluation of investment securities at year-end. Due to changes in Japanese accounting standards, foreign currency translation adjustments were reclassified from assets to shareholders' equity in FY2000. The ratio of shareholders' equity to total assets dropped from 63.8% in FY1999 to 61.9%. Shareholders' equity per share, based on the number of outstanding shares as of the end of the year, increased from ¥1,006 in the previous year to ¥1,023.

CASH FLOW

Cash generated from operating activities during the year totaled ¥6,832 million. However, with ¥3,172 million expended for investing activities and ¥7,193 million for financing activities, cash and cash equivalents at the end of the year decreased by ¥3,173 million to ¥30,555 million.

● Cash Flows from Operating Activities

Cash flow from operating activities decreased from the previous year by ¥2,540 million, mainly due to the ¥5,992 million in trade receivables that were not collected on the closing date of the

year due to the financial holiday. Excluding this effect, cash flow from operating activities was ¥12,824 million in FY2000.

● Cash Flows from Investing Activities

Cash flow from investing activities decreased from the previous year by ¥4,009 million due to increased capital expenditures, including production facility improvements, and decreased short-term investments.

● Cash Flows from Financial Activities

Cash flow from financial activities decreased by ¥3,376 million, due to the use of retained earnings to repurchase and retire our shares.

FORECAST OF CONSOLIDATED RESULTS

The revision of the Japanese National Health Insurance Drug Price Standard that was originally scheduled for April 2001 has been postponed. However, we expect conditions in Japan will remain difficult as the introduction of a fixed rate system for medical charges for the aged may discourage the elderly from seeing doctors, and personal consumption is expected to remain weak due to the economic situation in Japan.

Prescription pharmaceutical sales in Japan will show solid growth

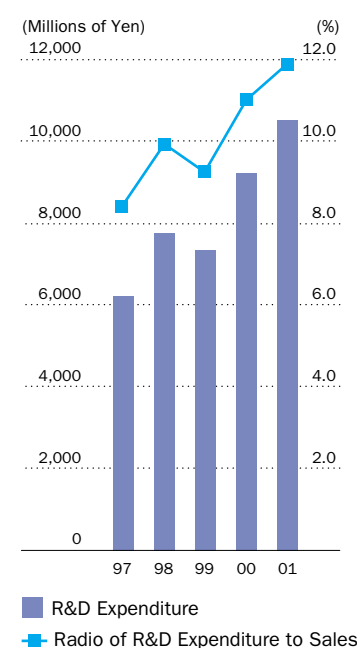
due to new product launches. Sales in overseas markets will also increase, due to the full-year inclusion of sales results for new products launched in FY 2000, as well as market expansion in Asia and Europe.

Sales in the OTC pharmaceuticals segment are expected to increase as we continue to recover from the temporary drop in sales caused by the FY2000 recall.

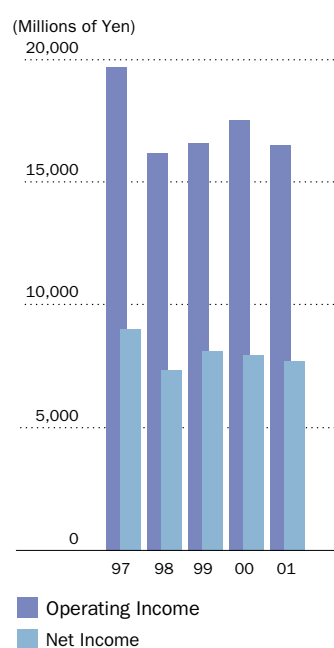
Santen will continue to invest in overseas business expansion and increased R&D activities. We will continue to increase marketing and sales expenditures in the U.S. to establish a solid sales organization and achieve new product penetration in the market as quickly as possible. Research and development expenses will also increase as we will continue to strengthen research and development activities both in and outside Japan, actively promote strategic licensing of our technology, and continue collaboration with other companies on joint development projects.

Although we will continue to invest in overseas business expansion and increased R&D activities, we expect net income to increase in FY 2001 due to the higher sales growth both in and outside Japan.

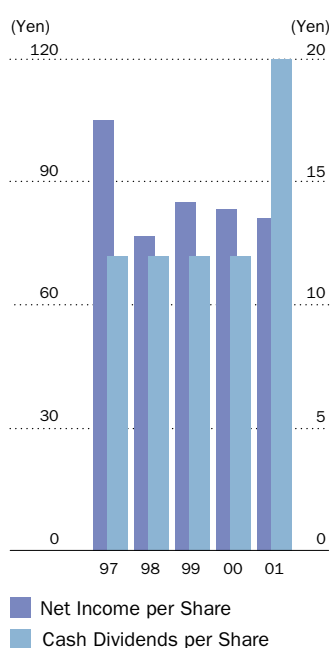
R&D Expenditure and The Ratio of R&D Expenditure to Sales



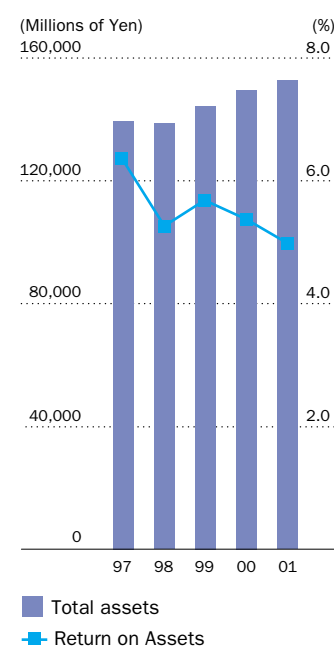
Operating Income and Net Income



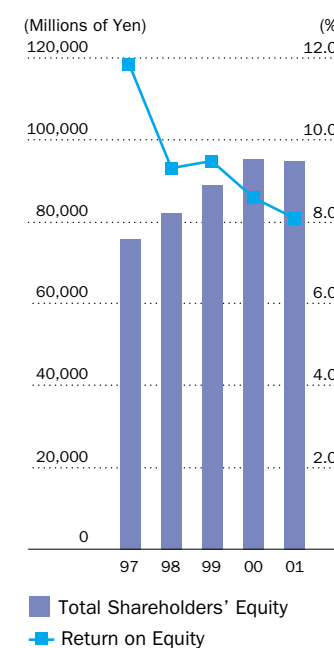
Net Income per Share and Cash Dividends per Share



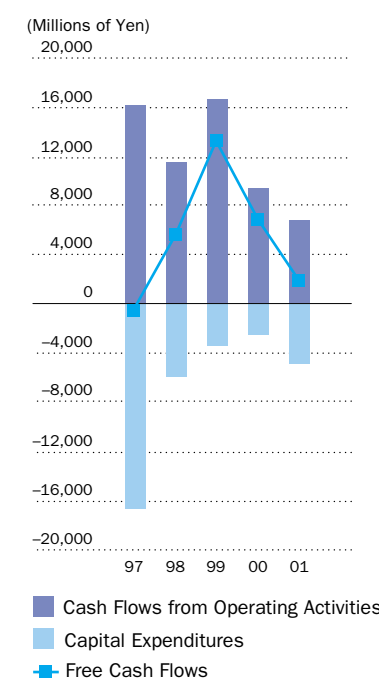
Total assets and Return on Assets



Total Shareholders' Equity and Return on Equity



Free Cash Flows



CONSOLIDATED BALANCE SHEETS

Santen Pharmaceutical Co., Ltd. and Subsidiaries
As of March 31, 2001 and 2000

ASSETS	Millions of yen		Thousands of U.S. dollars [Note 3]
	2001	2000	2001
Current assets:			
Cash and cash equivalents	¥ 30,555	¥ 33,728	\$ 246,611
Short-term investments [Note 4].....	1,241	3,706	10,018
Trade receivables:			
Notes	1,037	1,421	8,373
Accounts	39,884	30,494	321,904
Less allowance for doubtful receivables.....	(94)	(140)	(763)
Net trade receivables	40,827	31,775	329,514
Inventories [Note 6].....	11,986	11,183	96,742
Deferred tax assets [Note 13].....	2,412	1,419	19,470
Other current assets.....	1,004	407	8,100
Total current assets.....	88,025	82,218	710,455
Property, plant and equipment [Note 7]:			
Land	10,988	11,032	88,688
Buildings and structures	35,557	35,313	286,980
Machinery and equipment	10,955	11,055	88,419
Tools, furniture and vehicles.....	9,579	8,874	77,311
Construction in progress	1,750	178	14,125
Total	68,829	66,452	555,523
Less accumulated depreciation	(32,145)	(29,036)	(259,447)
Net property, plant and equipment	36,684	37,416	296,076
Investments and other assets:			
Investments in and advances to affiliates.....	433	429	3,495
Investment securities [Note 4].....	12,972	9,911	104,693
Goodwill.....	1,556	1,804	12,559
Other intangibles	3,225	3,429	26,031
Deferred tax assets [Note 13].....	1,826	2,569	14,739
Other assets.....	8,522	8,571	68,778
Total investments and other assets.....	28,534	26,713	230,295
Foreign currency translation adjustments [Note 2.x]:			
Total assets [Note 14].....	¥ 153,243	¥ 149,968	\$ 1,236,826

See accompanying notes to consolidated financial statements.

CONSOLIDATED BALANCE SHEETS

Santen Pharmaceutical Co., Ltd. and Subsidiaries
As of March 31, 2001 and 2000

LIABILITIES AND SHAREHOLDERS' EQUITY	Millions of yen		Thousands of U.S. dollars [Note 3]
	2001	2000	2001
Current liabilities:			
Current portion of long-term debt [Note 8]	¥ 989	¥ 1,008	\$ 7,979
Trade accounts payable	6,900	5,077	55,690
Other payables	11,007	7,211	88,841
Accrued expenses	3,594	4,243	29,006
Income taxes payable [Note 13]	4,641	3,823	37,457
Other current liabilities.....	210	597	1,695
Total current liabilities.....	27,341	21,959	220,668
Noncurrent liabilities:			
Long-term debt [Note 8]	24,493	25,483	197,685
Retirement and severance benefits [Note 9].....	5,306	5,604	42,824
Deferred tax liabilities [Note 13]	38	41	309
Other liabilities	1,231	1,212	9,933
Total noncurrent liabilities	31,068	32,340	250,751
Shareholders' equity [Note 10 and 11]:			
Common stock, ¥50 (\$0.40) par value:			
Authorized-157, 613 thousand shares (160,000 thousand shares in 2000)			
Issued-92,721 thousand shares (95,075 thousand shares in 2000)	6,206	6,180	50,086
Additional paid-in capital	6,900	6,875	55,692
Retained earnings	83,735	82,664	675,831
Unrealized holding gains on securities	1,290	—	10,409
Foreign currency translation adjustments [Note 2.x])	(3,256)	—	(26,279)
Total shareholders' equity	94,875	95,719	765,739
Treasury stock at cost:			
17,669 shares in 2001 and 22,626 shares in 2000	(41)	(50)	(332)
Total shareholders' equity	94,834	95,669	765,407
Total liabilities and shareholders' equity.....	¥ 153,243	¥ 149,968	\$ 1,236,826

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF INCOME

Santen Pharmaceutical Co., Ltd. and Subsidiaries
For the years ended March 31, 2001 and 2000

	Millions of yen		Thousands of U.S. dollars [Note 3]
	2001	2000	2001
Net sales [Note 14]	¥ 88,449	¥ 83,577	\$ 713,873
Cost of sales [Notes 7 and 9]	33,385	32,195	269,449
Gross profit	55,064	51,382	444,424
Selling, general and administrative expenses [Notes 7, 9 and 12]	38,546	33,894	311,109
Operating income [Note 14]	16,518	17,488	133,315
Other income (deductions):			
Interest and dividend income	579	565	4,676
Interest expense	(430)	(462)	(3,474)
Loss on valuation of securities	—	(1,126)	—
Impairment losses on golf membership rights	(446)	—	(3,599)
Amortization of unfunded portion of retirement benefit obligation	—	(2,038)	—
Expenses for the withdrawal of OTC products	(907)	—	(7,319)
Other, net	207	(5)	1,670
Income before income taxes	15,521	14,422	125,269
Income taxes [Note 13]:			
Current	8,973	8,508	72,423
Deferred	(1,166)	(2,027)	(9,412)
Net income	¥ 7,714	¥ 7,941	\$ 62,258

Per share data [Note 2.xii]:	Yen		U.S. dollars (Note 3)
	2001	2000	2001
Net income	¥ 81.32	¥ 83.54	\$ 0.66
Net income-diluted	75.01	77.04	0.61
Cash dividends, applicable to period	20.00	12.00	0.16

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

Santen Pharmaceutical Co., Ltd. and Subsidiaries
For the years ended March 31, 2001 and 2000

	Thousands Number of shares issued	Millions of yen					Treasury stock
		Common stock	Additional paid-in capital	Retained earnings	Unrealized holding gains on securities	Foreign curren- cy translation adjustments	
Balance as of March 31, 1999	95,075	¥ 6,180	¥ 6,875	¥ 75,924	¥ —	¥ —	¥ (50)
Net income	—	—	—	7,941	—	—	—
Cash dividends paid, ¥12 per share [Note 10]	—	—	—	(1,140)	—	—	—
Bonuses to directors and corporate auditors	—	—	—	(61)	—	—	—
Balance as of March 31, 2000	95,075	6,180	6,875	82,664	—	—	(50)
Net income	—	—	—	7,714	—	—	—
Unrealized holding gains on securities [Note 4]	—	—	—	—	1,290	—	—
Foreign currency translation adjustments [Note 2.x]	—	—	—	—	—	(3,256)	—
Cash dividends paid, ¥16 per share [Note 10]	—	—	—	(1,521)	—	—	—
Bonuses to directors and corporate auditors	—	—	—	(37)	—	—	—
Exercise of stock options [Note 11]	33	26	25	—	—	—	—
Repurchase of treasury stock, net [Note 10]	—	—	—	—	—	—	9
Retirement of treasury stock [Note 10]	(2,387)	—	—	(5,085)	—	—	—
Balance as of March 31, 2001	92,721	¥ 6,206	¥ 6,900	¥ 83,735	¥ 1,290	¥ (3,256)	¥ (41)

	Thousands of U.S. dollars [Note 3]					
	Common stock	Additional paid-in capital	Retained earnings	Unrealized holding gains on securities	Foreign curren- cy translation adjustments	Treasury stock
Balance as of March 31, 2000	\$ 49,881	\$ 55,487	\$ 667,183	\$ —	\$ —	\$ (404)
Net income	—	—	62,258	—	—	—
Unrealized holding gains on securities [Note 4]	—	—	—	10,409	—	—
Foreign currency translation adjustments [Note 2.x]	—	—	—	—	(26,279)	—
Cash dividends paid, \$0.13 per share [Note 10]	—	—	(12,275)	—	—	—
Bonuses to directors and corporate auditors	—	—	(299)	—	—	—
Exercise of stock options [Note 11]	205	205	—	—	—	—
Repurchase of treasury stock, net [Note 10]	—	—	—	—	—	72
Retirement of treasury stock [Note 10]	—	—	(41,036)	—	—	—
Balance as of March 31, 2001	\$ 50,086	\$ 55,692	\$ 675,831	\$ 10,409	\$ (26,279)	\$ (332)

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Santen Pharmaceutical Co., Ltd. and Subsidiaries
For the years ended March 31, 2001 and 2000

	Millions of yen		Thousands of U.S. dollars [Note 3]
	2001	2000	2001
Cash flows from operating activities:			
Net income before income taxes	¥ 15,521	¥ 14,422	\$ 125,269
Depreciation and amortization	5,683	5,725	45,871
Increase (decrease) in retirement and severance benefits	(330)	1,617	(2,661)
Interest and dividend income.....	(579)	(565)	(4,676)
Interest expense	430	462	3,474
Loss on valuation of securities	—	1,126	—
Impairment losses on golf membership rights.....	446	—	3,599
(Increase) in trade receivables.....	(8,372)	(2,352)	(67,571)
(Increase) in inventories.....	(765)	(2,198)	(6,174)
Increase (decrease) in accounts payables	1,813	(843)	14,630
Other, net	1,081	1,116	8,724
Subtotal.....	14,928	18,510	120,485
Interest and dividend income received	529	526	4,271
Interest expense paid	(406)	(462)	(3,279)
Income taxes paid	(8,219)	(9,202)	(66,337)
Net cash provided by operating activities.....	6,832	9,372	55,140
Cash flows from investing activities:			
Capital expenditures	(4,943)	(2,510)	(39,894)
Payments for purchase of investment securities	(708)	(2,529)	(5,712)
Proceeds from sale of investment securities	1,976	1,610	15,950
Payments for purchase of short-term investments.....	(3,421)	(8,945)	(27,609)
Proceeds from sale of short-term investments	3,867	14,522	31,208
Proceeds from collection of loans receivable	159	516	1,278
Other, net	(102)	(1,827)	(824)
Net cash provided by (used in) investing activities.....	(3,172)	837	(25,603)
Cash flows from financing activities:			
Decrease in short-term borrowings, net	—	(2,000)	—
Repayment of long-term debt.....	(654)	(648)	(5,280)
Repurchase of treasury stock, net	(5,081)	(19)	(41,008)
Dividends paid	(1,520)	(1,140)	(12,270)
Other, net	62	(10)	504
Net cash (used in) financing activities	(7,193)	(3,817)	(58,054)
Effect of exchange rate changes on cash and cash equivalents.....	360	(237)	2,911
Net increase (decrease) in cash and cash equivalents.....	(3,173)	6,155	(25,606)
Cash and cash equivalents at beginning of year.....	33,728	27,573	272,217
Cash and cash equivalents at end of year.....	¥ 30,555	¥ 33,728	\$ 246,611

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Santen Pharmaceutical Co., Ltd. and Subsidiaries
For the years ended March 31, 2001 and 2000

1. Basis of Presentation of Consolidated Financial Statements:

The accompanying consolidated financial statements have been prepared from the consolidated financial statements issued for domestic reporting purposes in Japan. Santen Pharmaceutical Co., Ltd. (the "Company") and all domestic subsidiaries maintain their accounts and records in accordance with the provisions set forth in the Japanese Commercial Code (the "Code") and in conformity with accounting principles and practices generally accepted in Japan, which may differ in some material respects from accounting principles and practices generally accepted in countries and jurisdictions other than Japan, and the accounts and records of its foreign subsidiaries in conformity with those of the countries of their domicile.

In preparing these consolidated financial statements, however, certain reclassifications have been made to the consolidated financial statements, which were originally issued and filed with the Director of the Kanto Local Finance Bureau for domestic reporting purposes in Japan, in order to present them in a form which is more familiar to readers outside Japan. In addition, the notes to the consolidated financial statements include additional information, which is not required under accounting principles and practices generally accepted in Japan but is presented herein as additional information.

Change in accounting method

In 2001, the Company and its subsidiaries (together the "Companies") changed the presentation of royalty income, which had been classified as other income, to include it in sales since royalty income is deemed to be a result of the main operating activities of the Companies and the amount become significant.

This change in accounting method resulted in operating income being ¥208 million (\$1,680 thousand) higher for the year ended March 31, 2001 than would have been if the prior method had been used.

The Companies have accounted for provision for sales return, which has been included in accrued expenses in the consolidated balance sheets, for loss on returned goods based on the net trade receivables at the end of the fiscal year. The Companies changed the method of accounting for provision for sales return from the method which was in accordance with corporate tax laws to the estimated loss on returned goods, in order to reflect the actual status more accurately.

This change in accounting method resulted in operating income being ¥31 million (\$249 thousand) less for the year ended March 31, 2001 than would have been if the prior method had been used.

In 2000, as described in Note 2, the Company has changed the method of accounting for retirement and severance benefits of its employees, in order to provide a better measurement of financial position and operating results and to strengthen their financial position.

This change in accounting method resulted in operating income being ¥110 million (\$1,035 thousand) less, and income before income taxes being ¥2,147 million (\$20,231 thousand) less for the year ended March 31, 2000 than would have been if the prior method had been used.

2. Summary of Significant Accounting Policies

i) Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Companies. All significant intercompany balances and transactions are eliminated in consolidation.

Investments in affiliated companies are stated at cost, because the Companies' equity in earnings of these companies is not significant.

ii) Use of estimates

The preparation of the consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

iii) Short-term investments, investment securities and golf membership rights (see Note 4)

Until March 31, 2000, listed securities included in short-term investments and investment securities had been carried at the lower of cost or market value, cost being determined by the moving average method. Other investments were carried at cost or less.

Effective April 1, 2000, the Company and all domestic subsidiaries adopted the new Financial Accounting Standard on Accounting for Financial Instruments, which was issued by the Financial Accounting Deliberation Council. In accordance with the new standard, securities are classified into three categories; trading, held-to-maturity, or other securities.

Based on this classification, all trading securities and, any held-to-maturity and other securities with a maturity of less than one year, are included in current assets. All other securities are included in investment securities as noncurrent assets. As a result of the adoption of this standard in the current year, short-term investments decreased by ¥2,065 million (\$16,666 thousand) and investment securities increased by ¥2,065 million (\$16,666 thousand).

Those classified as other securities with a market value would be reported at fair value with unrealized gains, net of related taxes reported in equity. Other securities with no market value are carried at cost. The cost is determined by the moving average method.

In addition, the new standard requires the recognition of an impairment loss on golf membership rights, included in other assets, on the consolidated balance sheet, when the market value has permanently declined.

As a result of the adoption of this standard in the current year, income before income taxes decreased by ¥365 million (\$2,945 thousand).

iv) Derivative instruments (see Note 5)

Derivative instruments are accounted for using deferral hedge accounting. Deferral hedge accounting requires unrealized gains or losses to be deferred as liabilities or assets. Foreign exchange contracts that meet the criteria are accounted for under the allocation method. The allocation method requires recognized foreign currency receivables or payables to be translated using the corresponding foreign exchange contract rates. Interest rate swaps that meet the criteria are accounted for under the special method, as regulated in the accounting standard, as if

the interest rates under interest rate swaps were originally applied to underlying borrowings. The Company has also developed a hedging policy to control various aspects of derivative instruments including authorization levels and transaction volumes. Based on this policy, the Company hedges, within certain scopes, the exposure risk arising from fluctuations in foreign currency exchange rates, interest rates, and price of securities. The Company reviews the effectiveness of all hedging policies to take account of the cumulative cash flows and any changes in the market.

v) Inventories

Inventories are stated at cost, determined principally by the average method.

vi) Property, plant and equipment

Property, plant and equipment is stated at cost. Depreciation is computed over the estimated useful lives of the assets by the declining-balance method for the Company and all domestic subsidiaries and by the straight-line method for all foreign subsidiaries.

In accordance with the amendments of the Japanese tax regulations in the 1998 fiscal year, the Company and all domestic subsidiaries changed their method of deprecation for buildings (other than leasehold improvements) which were acquired on or after April 1, 1998 to the straight-line method.

The principal estimated useful lives are as follows:

Buildings and structures	3 to 60 years
Machinery and equipment	4 to 15 years
Tools, furniture and vehicles	2 to 20 years

vii) Goodwill

Goodwill, which represents the excess of purchase price over the fair value of net assets acquired, is amortized on a straight-line basis over a period of ten years.

viii) Leases (see Note 7)

In Japan, finance leases other than those that are deemed to transfer the ownership of the leased assets to lessees are accounted for by a method similar to that applicable to ordinary operating leases.

ix) Retirement and severance benefits (see Note 9)

Employees of the Company and all domestic subsidiaries are generally entitled to lump-sum severance and, in certain cases, annuity payments on retirement, based on current rates of pay, length of service and certain other factors. A portion of the prescribed benefit plan is covered by funded defined benefit pension plans.

Effective April 1, 1999, the Company changed its accounting method for retirement and severance benefits and pension costs to provide for retirement and severance benefit liabilities, which consist of projected benefit obligations for service rendered to date less fair value of pension plan assets as of the balance sheet date.

Prior to April 1, 1999, the Company provided for retirement and severance benefit liabilities, which consisted of provision for unfunded lump-sum severance plan payments, which would exist if all employees voluntarily terminated their employment at the balance sheet date, and actuarial net present value of pension obligations calculated by using the actual long-term market rate of return less pension assets. The cumulative effect of this change in accounting method as of April 1, 1999 was ¥2,037 million (\$19,196 thousand) and was charged to other expenses in the consolidated statements of income for the year ended March 31, 2000.

Effective from the year ended March 31, 2001, the Companies adopted the new Accounting Standard for Retirement Benefits which was issued by the Financial Accounting Deliberation Council. In accordance with this standard, the allowance for retirement benefits for employees is provided based on the estimated retirement benefit obligation and the pension assets. This change does not affect the consolidated financial statements for the year ended March 31, 2001. Actuarial gains and losses are amortized, from the year in which the actuarial gains and losses are incurred, using the straight-line method, over the estimated average remaining service years of employees.

In addition, the Company has an unfunded retirement benefit plan for directors and corporate auditors. The amounts required under the plan have been fully accrued. Accrued severance indemnities for the members of the board and corporate auditors of the Company are provided based on internal regulations that are similar to those for employees. The accrued provision for severance indemnities of the members of the board and corporate auditors is not funded.

A foreign subsidiary has a defined contribution plan covering substantially all of their employees. The amounts contributed under the plan have been accrued.

x) Foreign currency translation

Current receivables and payables denominated in foreign currencies are translated at the rate of exchange prevailing on the balance sheet date, except for those items covered by forward exchange contracts. Until March 31, 2000, noncurrent receivables and payables, carried in foreign currencies, had been translated at the rate when acquired or incurred or at the forward contract rate, except when significant unrealized exchange losses were incurred and recovery of them was not probable in the future. Income and expenses are converted at historical rates. Foreign exchange gains and losses are credited or charged to income.

Effective from the year ended March 31, 2001, the Company and all domestic subsidiaries adopted the revised Accounting Standard for Foreign Currency Transactions which was issued by the Financial Accounting Deliberation Council. The revised Accounting Standard for Foreign Currency Transactions requires all monetary assets and liabilities denominated in foreign currencies to be translated at the rate of exchange prevailing on the balance sheet date, except for those items covered by forward exchange contracts. This change does not significantly affect the consolidated financial statements for the year ended March 31, 2001.

Financial statements of foreign subsidiaries are translated into Japanese yen at year-end rates for all assets and liabilities and at weighted average rates for income and expense accounts. Adjustments resulting from the translation of financial statements were reflected under the caption, "Foreign currency translation adjustments", a separate component of assets or liabilities until March 31, 2000. In the current year, "Foreign currency translation adjustments" are included in "Shareholders' equity", as a result of the amendment to the Regulations Concerning Terminology, Forms and Preparation Method of Consolidated Financial Statements.

xi) Research and Development and Computer Software(see Note 12)

Effective April 1, 1999, the Companies adopted the Accounting Standard for Research and Development Cost, etc. which was issued by the Financial Accounting Deliberation Council.

Research and development expenditure is charged to income when incurred.

Expenditure relating to computer software developed for internal use is charged to income when incurred except if it contributes to the generation of income or to future cost savings. Such expenditure is capitalized as an asset and is amortized using the straight-line method over its estimated useful life, five years.

xii) Net income and dividends per share (see Note 10)

The computation of basic net income per share is based on the weighted average number of shares of common stock outstanding during each period. The average number of shares used in the computation is 94,855 thousand and 95,051 thousand for the years ended March 31, 2001 and 2000, respectively.

The diluted net income per share assumes full conversion of outstanding convertible bonds at the beginning of the year (or at the time of issuance, if after the beginning of the year) with an applicable adjustment for related net-of-tax interest expense, and full exercise of outstanding warrants at the end of the year. The average number of shares used in the computation is 104,063 thousand and 104,270 thousand for the years ended March 31, 2001 and 2000, respectively.

Cash dividends per share shown in the accompanying consolidated statements of income are the amounts applicable to the respective years.

xiii) Income taxes (see Note 13)

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and foreign tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

xiv) Cash and cash equivalents

Cash and cash equivalents mainly include cash in hand, deposits held at call with banks and all highly liquid debt investments, generally with a maturity of three months or less, that are readily convertible to known amounts of cash and are so near maturity that they present insignificant risk of changes in value because of changes in interest rates.

3. Translation into United States Dollars:

The accompanying consolidated financial statements are expressed in Japanese yen and, solely for the convenience of the reader, have been translated into United States dollars at the rate of ¥123.90=US\$1, the approximate exchange rate prevailing on March 30, 2001. The translation should not be construed as a representation that the Japanese yen have been, could have been, or could in the future be converted into United States dollars at that rate or any other rate.

4. Short-term Investments and Investment Securities

At March 31,2000, book value, market value and net unrealized gains of quoted securities are as follows:

	Millions of yen			
	March 31, 2000			
	Book (Carrying amount)	Gross unrealized gains	Gross unrealized losses	Market value
Current				
Equity securities	¥ 406	¥ 121	¥ (1)	¥ 526
Other securities	1,350	—	(279)	1,071
	<u>1,756</u>	<u>121</u>	<u>(280)</u>	<u>1,597</u>
Non current				
Equity securities	3,510	2,457	(4)	5,963
Bonds and debentures	200	4	—	204
	<u>3,710</u>	<u>2,461</u>	<u>(4)</u>	<u>6,167</u>
	<u>¥ 5,466</u>	<u>¥ 2,582</u>	<u>¥ (284)</u>	<u>¥ 7,764</u>

The following is a summary of held-to-maturity debt securities and other securities at March 31, 2001:

	Millions of yen			
	March 31, 2001			
	Held-to-maturity debt securities			
	Book (Carrying amount)	Gross unrealized gains	Gross unrealized losses	Estimated fair value
Bonds and debentures	¥ 4,595	¥ 29	¥ (14)	¥ 4,610
	Other securities			
	Cost	Gross unrealized gains	Gross unrealized losses	Book value (Estimated fair value)
Equity securities	¥ 4,605	¥ 2,456	¥ (87)	¥ 6,974
Bonds and debentures	200	—	(1)	199
Other securities	1,158	2	(146)	1,014
	<u>¥ 5,963</u>	<u>¥ 2,458</u>	<u>¥ (234)</u>	<u>¥ 8,187</u>

Thousands of U.S. dollars				
March 31, 2001				
Held-to-maturity debt securities				
	Book (Carrying amount)	Gross unrealized gains	Gross unrealized losses	Estimated fair value
Bonds and debentures	\$ 37,083	\$ 238	\$ (110)	\$ 37,211
Other securities				
	Cost	Gross unrealized gains	Gross unrealized losses	Book value (Estimated fair value)
Equity securities	\$ 37,165	\$ 19,830	\$ (704)	\$ 56,291
Bonds and debentures	1,614	—	(12)	1,602
Other securities	9,350	12	(1,181)	8,181
	\$ 48,129	\$ 19,842	\$ (1,897)	\$ 66,074
Millions of yen		Thousands of U.S. dollars		
	Bonds and debentures	Other securities	Bonds and debentures	Other securities
Due within one year	¥ 548	¥ 1,000	\$ 4,421	\$ 8,071
Due after one year through five years	4,058	418	32,752	3,375
Due after five years through ten years	—	402	—	3,240
Due after ten years	—	—	—	—
	¥ 4,606	¥ 1,820	\$ 37,173	\$ 14,686

5. Derivative instruments

The Company principally utilizes derivative instruments such as foreign exchange contracts, interest rate swaps, currency interest rate swaps, currency options and equity options to hedge the exposure risk arising from fluctuations in foreign currency exchange rates, interest rates and market price of securities.

The Company is exposed to the risk that the counterparties will not be able to fully satisfy their obligations under contracts, risks in relation to fluctuations in foreign currency exchange rates and interest rates, and market price of securities. The Company believes that the risk, that the counterparties will not be able to fully satisfy their obligations under contracts, is minimum because contracts have been made with counterparties who have been thoroughly assessed.

The interest rate swap contracts outstanding at March 31, 2001 and 2000 are as follows:

Millions of yen						
		2001			2000	
Currency	Notional amounts	Market value	Unrealized gain (loss)	Notional amounts	Market value	Unrealized gain (loss)
Variable-rate into fixed-rate Obligations	Yen	¥ 1,000	¥ (60)	¥ (60)	¥ 1,000	¥ (52)
Fixed-rate into fixed-rate Obligations	US\$	—	—	—	4,738	(164)
Fixed-rate into fixed-rate Obligations	DM	—	—	—	1,000	(7)

Thousands of U.S. dollars			
2001			
Currency	Notional amounts	Market value	Unrealized gain (loss)
Variable-rate into fixed-rate Obligations	Yen	\$ 8,071	\$ (481)
Fixed-rate into fixed-rate Obligations	US\$	—	—
Fixed-rate into fixed-rate Obligations	DM	—	—

6. Inventories

Inventories at March 31, 2001 and 2000, consisted of the following:

		Millions of yen		Thousands of U.S. dollars
		2001	2000	2001
Merchandise		¥ 2,563	¥ 2,448	\$ 20,689
Finished goods		6,746	6,336	54,449
Work in process and semi-finished goods		979	863	7,902
Raw materials and supplies		1,698	1,536	13,702
		¥ 11,986	¥ 11,183	\$ 96,742

7. Leases

Finance leases, except for those in which ownership is deemed to be transferred to the lessee, were accounted for as operating leases. Equivalent purchase amount, accumulated depreciation and future minimum lease payments on an "as if capitalized" basis at March 31, 2001 and 2000 are as follows:

		Millions of yen		Thousands of U.S. dollars
		2001	2000	2001
Machinery and equipment:				
Equivalent purchase amount	¥	10,389	¥ 10,265	\$ 83,847
Equivalent accumulated depreciation amount		8,317	6,255	67,120
Equivalent balance at year-end		2,072	4,010	16,727
Tools				
Equivalent purchase amount		311	149	2,512
Equivalent accumulated depreciation amount		128	84	1,037
Equivalent balance at year-end		183	65	1,475
Total:				
Equivalent purchase amount		10,700	10,414	86,359
Equivalent accumulated depreciation amount		8,445	6,340	68,157
Equivalent balance at year-end	¥	2,255	¥ 4,074	\$ 18,202
Future minimum lease payments				
Due within one year		1,792	2,151	14,461
Due after one year		588	2,113	4,749
	¥	2,380	¥ 4,264	\$ 19,210

Lease payments, equivalent depreciation and equivalent interest expense for the years ended March 31, 2001 and 2000 are as follows:

		2001	2000	2001
Lease payments	¥	2,302	¥ 2,259	\$ 18,584
Equivalent depreciation	¥	2,128	¥ 2,087	\$ 17,177
Equivalent interest expense	¥	111	¥ 174	\$ 898

Future minimum rents under non-cancellable operating leases at March 31, 2001 and 2000 consist of the following:

		Millions of yen		Thousands of U.S. dollars
		2001	2000	2001
Due within one year	¥	56	¥ 34	\$ 452
Due after one year		396	402	3,199
	¥	452	¥ 436	\$ 3,651

8. Long-term Debt

Long-term debt at March 31, 2001 and 2000 consists of the following:

		Millions of yen		Thousands of U.S. dollars
		2001	2000	2001
Unsecured yen loans from domestic banks, due in installments through 2011, interest 2.15% to 5.60%	¥	3,662	¥ 4,254	\$ 29,556
Unsecured loans from governmental institutions, due in installments through 2010, interest 0.00% to 0.50%		485	548	3,915
Unsecured yen loans from an insurance company, due in installments through 2002, interest 3.45%		1,000	1,000	8,071
Unsecured convertible bonds, due in installments through 2003, interest 0.8%		19,945	19,945	160,977
Other		390	744	3,145
Total		25,482	26,491	205,664
Less: Current portion shown in current liabilities		(989)	(1,008)	(7,979)
	¥	24,493	¥ 25,483	\$ 197,685

The 0.8 per cent convertible bonds maturing in 2003 are convertible into approximately 9,184 thousand shares of common stock at ¥2,171.80 per share on March 31, 2001 at the option of the holders. The conversion price of bonds is subject to adjustment for certain subsequent events such as the issue of common stock at less than par value and stock splits.

As is customary in Japan, long-term bank loans are made under general agreements which provide that additional security and guarantees for present and future indebtedness will be given upon request of the bank under certain circumstances, and that the bank shall have the right, as the obligations become due, or in the event of their default, to offset cash deposits against such obligations due to the bank. To date, the Company has not received such a request from its banks.

The aggregate annual maturates of long-term debt at March 31, 2001 are as follows:

Years ending March 31	Millions of yen	Thousands of U.S. dollars
2003	¥ 1,446	\$ 11,672
2004	20,361	164,334
2005	416	3,358
2006	416	3,358
2007 and thereafter	1,854	14,963
Total	<u>¥ 24,493</u>	<u>\$ 197,685</u>

9. Retirement and Severance Benefits

The following tables set forth the details of benefit obligation, plan assets and funded status of the Companies at March 31, 2001.

	Millions of yen	Thousands of U.S. dollars
For employees:		
Benefit obligation at end of year	¥ (9,651)	\$ (77,892)
Fair value of plan assets at end of year	4,187	33,790
Funded status (Benefit obligation in excess of plan assets)	(5,464)	(44,102)
Unrecognized actuarial loss	405	3,271
For directors and corporate auditors:		
Accrued retirement benefit	(247)	(1,993)
Retirement and severance benefits recognized in the consolidated balance sheets	<u>¥ (5,306)</u>	<u>\$ (42,824)</u>

Note: All domestic subsidiaries have adopted the permitted alternative treatment, accrual for 100% of the amount required if all employees were to voluntarily terminate their employment as of the balance sheet date, prescribed by the accounting standard for retirement benefits for small business entities.

Retirement and severance costs of the Companies included the following components for the year ended March 31, 2001.

	Millions of yen	Thousands of U.S. dollars
For employees:		
Service cost	¥ 603	\$ 4,869
Interest cost	273	2,199
Expected return on plan assets	(120)	(972)
Recognized actuarial loss	31	252
Welfare pension cost paid	326	2,634
Net periodic benefit cost	<u>¥ 1,113</u>	<u>\$ 8,982</u>
For directors and corporate auditors:		
Accrual for retirement benefit	¥ 32	\$ 258

Assumptions used in the accounting for retirement and severance benefits for the year ended March 31, 2001 are as follows:

Discount rate	3.00%
Expected return on plan assets	3.00%

10. Shareholders' equity:

Under the Code, at least 50% of the issue price of new shares, with a minimum of the par value thereof, is required to be designated as stated capital. The portion, which is to be designated as, stated capital is determined by resolution of the Board of Directors. Proceeds in excess of the amounts designated as stated capital have been credited to additional paid-in capital.

The Code provides that an amount equal to at least 10% of cash payments for appropriation of retained earnings with respect to each fiscal period be appropriated to a legal reserve until such reserve equals 25% of the stated capital. Legal reserve, which is included in retained earnings, amounted to ¥1,473 million (\$11,889 thousand) and ¥1,317 million as of March 31, 2001 and 2000, respectively. This reserve is not available for dividends, but may be used to reduce a deficit by resolution of the shareholders or may be transferred to stated capital by resolution of the Board of Directors.

Cash dividends charged to retained earnings during the years ended March 31, 2001 and 2000 represent dividends paid out during the years. The accompanying consolidated financial statements do not include any provision for the semi-annual dividend of ¥10 (\$0.08) per share, aggregating ¥927 million (\$7,482 thousand) which was approved at the Company's shareholders' meeting on June 28, 2001 in respect of the year ended March 31, 2001.

Under the Code, the amount available for dividends is based on retained earnings as recorded on the Company's book. At March 31, 2001, retained earnings recorded on the Company's book were ¥83,735 million (\$675,831 thousand). Such retained earnings included ¥80,069 million (\$646,239 thousand) which are designated, as general reserves but are available for distribution as future dividends subject to approval by shareholders and legal reserve requirements. Unrealized holding gains on securities, net of related taxes is not available for dis-

tribution as dividends and bonuses to directors and corporate auditors.

Under the Company's articles of incorporation, it is possible for the Company to repurchase and retire common shares, limited to 9,500,000 shares, by using the Company's retained earnings subject to the resolution of the Board of Directors. During the years ended March 31, 2001, the Company repurchased and retired 2,387,000 shares with aggregate value of ¥5,085 million (\$41,036 thousand). Consequently, the number of common shares which may be repurchased and retired subject to the resolution of the Board of Directors under the Company's articles of incorporation as of March 31, 2001 is 7,113,000 shares.

11. Stock Options

The Company has stock-based compensation plans under which stock options are granted annually to directors and executive officers at the market price on the date of grant. The grants are fully exercisable after two years and span ten years.

Information concerning option activities and balances is as follows:

	Number of shares	Weighted average exercise price	
		Yen	U.S. dollars
Balance outstanding, March 31,1998	—	—	—
Granted	106,000	1,540	12.43
Exercised	33,000	1,540	12.43
Balance outstanding, March 31,1999	73,000	1,540	12.43
Granted	66,000	2,480	20.02
Balance outstanding, March 31,2000	139,000	1,986	16.03
Granted	60,000	2,705	21.83
Balance outstanding, March 31,2001	<u>199,000</u>	<u>2,203</u>	<u>17.78</u>

12. Research and Development Expenditure

Research and development expenditure charged to income for the years ended March 31, 2001 and 2000 amounted to ¥10,511 million (\$ 84,833 thousand) and ¥9,221 million, respectively.

13. Income Taxes

The Company and its domestic subsidiaries are subject to a number of taxes based on earnings which, in the aggregate, resulted in an average normal tax rate of approximately 42.0 % for the years ended March 31, 2001 and 2000. Foreign subsidiaries are subject to income taxes of the countries in which they operate.

The effective rates for the years ended March 31, 2001 and 2000 differ from the normal tax rates for the following reasons:

	2001	2000
Normal tax rate	42.0%	42.0%
Unrecognized deferred tax of an overseas subsidiary	4.8	—
Change in valuation allowance allocated to income tax expenses	3.0	—
Expenses not deductible for tax purposes	2.3	2.1
Others	(1.8)	0.8
Effective tax rate	<u>50.3%</u>	<u>44.9%</u>

The tax effects of temporary differences and tax loss carryforwards that give rise to significant portions of the deferred tax assets and deferred tax liabilities at March 31, 2001 and 2000 are presented below:

	Millions of yen		Thousands of U.S. dollars
	2001	2000	2001
Deferred tax assets:			
Retirement and severance benefits	¥ 1,453	¥ 1,641	\$ 11,727
Accrued expenses	1,125	299	9,081
Accrued enterprise taxes	440	356	3,553
Tax loss carryforwards	413	—	3,332
Loss on valuation of securities	208	416	1,680
Other	2,163	1,495	17,456
Total gross deferred tax assets	5,802	4,207	46,829
Less valuation allowance	(463)	—	(3,735)
Net deferred tax assets	<u>5,339</u>	<u>4,207</u>	<u>43,094</u>
Deferred tax liabilities:			
Net unrealized holding gains on securities	(934)	—	(7,537)
Reserve for special depreciation	(181)	(208)	(1,461)
Other	(24)	(52)	(196)
Total gross deferred tax liabilities	(1,139)	(260)	(9,194)
Net deferred tax assets	<u>¥ 4,200</u>	<u>¥ 3,947</u>	<u>\$ 33,900</u>

Net deferred tax assets at March 31, 2001 and 2000 are reflected in the accompanying consolidated balance sheets under the following captions:

	Millions of yen		Thousands of U.S. dollars
	2001	2000	2001
Current assets—deferred tax assets	¥ 2,412	¥ 1,419	\$ 19,470
Investments and other assets—deferred tax assets	1,826	2,569	14,739
Non current liabilities—deferred tax liabilities	(38)	(41)	(309)
Net deferred tax assets	<u>4,200</u>	<u>3,947</u>	<u>33,900</u>

14. Segment information

The Companies operate predominantly in a single industry segment, the production and marketing of Pharmaceuticals.

Intercompany sales between geographic areas are recorded at cost plus a mark up and intercompany sales and profits are eliminated on consolidation. Corporate assets are composed mainly of cash and cash equivalents, short-term investments and investment securities.

Information by geographic area and overseas sales are as follows:

	Millions of yen		Thousands of U.S. dollars
	2001	2000	2001
Net Sales:			
Japan:			
External customers	¥ 84,138	¥ 79,782	\$ 679,080
Intersegment	295	16	2,385
Total	<u>84,433</u>	<u>79,798</u>	<u>681,465</u>
Europe:			
External customers	3,017	2,908	24,349
Intersegment	863	403	6,968
Total	<u>3,880</u>	<u>3,311</u>	<u>31,317</u>
Other:			
External customers	1,294	887	10,444
Intersegment	4,600	2,651	37,124
Total	<u>5,894</u>	<u>3,538</u>	<u>47,568</u>
Corporate and Eliminations	<u>(5,758)</u>	<u>(3,070)</u>	<u>(46,477)</u>
Consolidated	<u>88,449</u>	<u>83,577</u>	<u>713,873</u>
Operating income (loss):			
Japan	24,461	22,392	197,427
Europe	(2,307)	(117)	(18,625)
Other	45	(52)	366
Corporate and Eliminations	<u>(5,681)</u>	<u>(4,735)</u>	<u>(45,853)</u>
Consolidated	<u>16,518</u>	<u>17,488</u>	<u>133,315</u>
Assets:			
Japan	94,170	89,973	760,047
Europe	19,447	21,784	156,957
Other	3,676	2,481	29,672
Corporate and Eliminations	<u>35,950</u>	<u>35,730</u>	<u>290,150</u>
Consolidated	<u>153,243</u>	<u>149,968</u>	<u>1,236,826</u>
Overseas sales:			
Europe	2,252	2,489	18,177
North America	2,206	1,437	17,806
Other	1,238	863	9,987
Total	<u>5,696</u>	<u>4,789</u>	<u>45,970</u>
Consolidated net sales	<u>88,449</u>	<u>83,577</u>	<u>713,873</u>
Percentage of overseas sales to consolidated net sales	<u>6.4%</u>	<u>5.7%</u>	<u>6.4%</u>

As described in Note 1, effective April 1, 2000, the Companies changed the method of accounting for royalty income. The effect of the change was to increase operating income of Japan by ¥491 million (\$3,960 thousand).

As described in Note 1, effective April 1, 2000, the Companies changed the method of accounting for provision for sales return. The effect of the change was to decrease operating income of Japan by ¥31 million (\$249 thousand).

As described in Note 2.iii), effective April 1, 2000, the Company and all domestic subsidiaries adopted the new Financial Accounting Standard on Accounting for Financial Instruments. Application of this standard decreased the assets in Japan by ¥1,380 million (\$11,134 thousand), and increased corporate assets by ¥2,391 million (\$19,297 thousand).

Overseas sales represent the total amount of export sales of the Company and domestic subsidiaries and sales of overseas subsidiaries (intercompany sales between consolidated subsidiaries were eliminated upon consolidation).

The Board of Directors and Shareholders
Santen Pharmaceutical Co., Ltd.

We have audited the consolidated balance sheets of Santen Pharmaceutical Co., Ltd. and its consolidated subsidiaries as of March 31, 2001 and 2000, and the related consolidated statements of income, shareholders' equity, and cash flows for the years then ended, all expressed in yen. Our audits were made in accordance with auditing standards, procedures and practices generally accepted and applied in Japan and, accordingly, included such tests of the accounting records and other auditing procedures as we considered necessary in the circumstances.

As described in Notes 1 and 2 to the consolidated financial statements, Santen Pharmaceutical Co., Ltd. and its consolidated subsidiaries changed the presentation of royalty income and the calculation method of provision for sales return in the year ended March 31, 2001, and the method of accounting for retirement and severance benefits of its employees in the year ended March 31, 2000.

In our opinion, the accompanying consolidated financial statements, expressed in yen, present fairly the financial position of Santen Pharmaceutical Co., Ltd. and its consolidated subsidiaries at March 31, 2001 and 2000, and the results of their operations and their cash flows for the years then ended, in conformity with accounting principles and practices generally accepted in Japan consistently applied during the periods except for the changes, with which we concur, in the methods of accounting discussed in the preceding paragraph.

As described in Note 2 to the consolidated financial statements, Santen Pharmaceutical Co., Ltd. and its consolidated subsidiaries adopted new accounting standards for employees' retirement and severance benefits, financial instruments and translation of foreign currency transactions effective April 1, 2000 and new accounting standards for consolidation, research and development costs effective April 1, 1999 in the preparation of its consolidated financial statements.

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended March 31, 2001 are presented solely for the convenience of the reader. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 3 to the consolidated financial statements.

Century Ota Showa Co.

Osaka, Japan
June 28, 2001

See note 1 to the consolidated financial statements which explains the basis of preparing the consolidated financial statements of Santen Pharmaceutical Co., Ltd. and its consolidated subsidiaries under Japanese accounting principles and practices.

MAJOR FACILITIES AND SUBSIDIARIES

Major Offices, Laboratories and Manufacturing Plants

Corporate Headquarters

9-19, Shimoshinjo 3-chome, Higashiyodogawa-ku,
Osaka 533-8651, Japan
TEL: 06-6321-7000

Central Research Laboratories

9-19, Shimoshinjo 3-chome, Higashiyodogawa-ku,
Osaka 533-8651, Japan
TEL: 06-6321-7030

Nara Research and Development Center

8916-16, Takayama-cho, Ikoma-shi, Nara 630-0101, Japan
TEL: 0743-79-4501

Osaka Manufacturing Plant

9-19, Shimoshinjo 3-chome, Higashiyodogawa-ku,
Osaka 533-8651, Japan
TEL: 06-6321-7070

Noto Manufacturing Plant

2-14, Aza-Shikinami, Shio-machi, Hakui-gun, Ishikawa
929-1494, Japan
TEL: 0767-29-2666

Shiga Manufacturing Plant

348-3, Aza-Suwa, Oaza-Shide, Taga-cho, Inukami-gun,
Shiga 522-0314, Japan
TEL: 0749-48-2900

Sapporo Office

2-1, Kitasanjo-nishi 28-chome, Chuo-ku, Sapporo 064-0823, Japan
TEL: 011-642-9481

Sendai Office

15, Kitame-machi 1-chome, Aoba-ku, Sendai 980-0023, Japan
TEL: 022-261-2141

Tokyo Office

14-1, Kyobashi 2-chome, Chuo-ku, Tokyo 104-0031, Japan
TEL: 03-5250-0310

Nagoya Office

901, Tokugawa 1-chome, Higashi-ku, Nagoya 461-0025, Japan
TEL: 052-932-8911

Osaka Office

9-19, Shimoshinjo 3-chome, Higashiyodogawa-ku,
Osaka 533-8651, Japan
TEL: 06-6321-7100

Hiroshima Office

19, Komachi 3-chome, Naka-ku, Hiroshima 730-0041, Japan
TEL: 082-244-2561

Fukuoka Office

8-6, Hakataekiminami 1-chome, Hakata-ku,
Fukuoka 812-0016, Japan
TEL: 092-411-0119

Major Subsidiaries

Santen Distribution Co., Ltd.

1011-1, Oaza-Godo, Omi-cho, Sakata-gun, Shiga 521-0072, Japan
TEL: 0749-52-4026 FAX: 0749-52-6080

Claire Co., Ltd.

348-3, Aza-Suwa, Oaza-Shide, Taga-cho, Inukami-gun, Shiga
522-0314, Japan
TEL: 0749-48-2234 FAX: 0749-48-2239

Santen Incorporated

555 Gateway Drive, Napa, California 94558, U.S.A.
TEL: +1-707-254-1750 FAX: +1-707-254-1755

Santen Pharmaceutical Support GmbH

Hauptstrasse 41, 82327 Tutzing, Germany
TEL: +49-8158-9969-0 FAX: +49-8158-9969-60

Taiwan Santen Pharmaceutical Co., Ltd.

5F-2, No.139, Sung-chiang Rd., Taipei, Taiwan, R.O.C.
TEL: +886-2-2506-1909 FAX: +886-2-2506-6740

Santen Oy

Niittyhaankatu 20, P.O.Box 33 FIN-33721 Tampere, Finland
TEL: +358-3-284-8111 FAX: +358-3-318-1900

Santen Pharmaceutical Korea, Co., Ltd.

Room 1403, Center Building, 91-1, Sogong-dong, Chung-ku,
Seoul, South Korea
TEL: +82-2-754-1434 FAX: +82-2-754-2929

INVESTORS INFORMATION

(As of March 31, 2001)

Corporate Headquarters

: Santen Pharmaceutical Co., Ltd.

9-19, Shimoshinjo 3-chome, Higashiyodogawa-ku, Osaka 533-8651, Japan

TEL: 06-6321-7007

FAX: 06-6321-8400

Email: ir@santen.co.jp

Established

: 1890

Paid-in Capital

: ¥6,205 million

Shares

: Authorized Shares 157,613,000

Issued Shares 92,720,849

Number of Shareholders

: 4,812

Stock Exchange Listing

: Tokyo, Osaka

Transfer Agent

: The Toyo Trust and Baking Co., Ltd.

6-3, Fushimicho 3-chome, Chuo-ku, Osaka 541-8502, Japan

TEL: 06-6229-3011

Major Offices

: Sapporo, Sendai, Tokyo, Nagoya, Osaka, Hiroshima, Fukuoka

Manufacturing Plants

: Osaka, Noto, Shiga

Laboratories

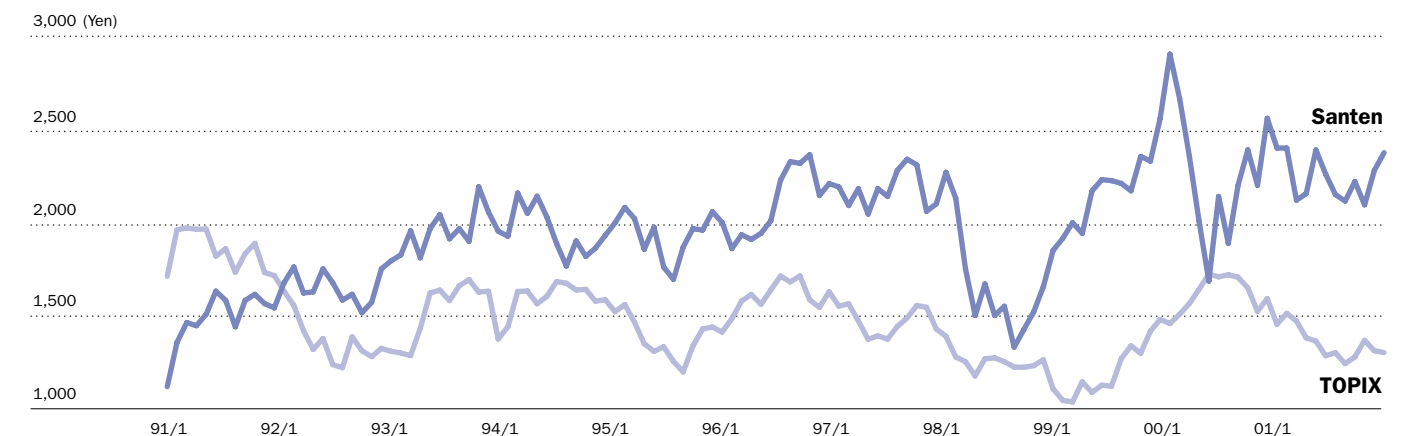
: Central Research Laboratories, Nara Research and Development Center

Number of Employees

: 2,167

Stock price range

(Closing price basis at the end of each month)



	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001*
High (Yen)	1,710	1,850	2,227	2,186	2,111	2,400	2,490	2,200	2,975	2,800	2,410
Low (Yen)	1,033	1,149	1,762	1,721	1,579	1,860	1,400	1,235	1,675	1,659	1,973

* Stock price from January to June

Santen: Stock price at Osaka Securities Exchange

TOPIX: Tokyo stock price index