SANTEN PHARMACEUTICAL CO., LTD.

ANNUAL REPORT 2006

Year Ended March 31, 2006

Toward a New Stage

CONTENTS

A CAUTION CONCERNING 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, changes in related laws and regulations, status of product development programs, and changes in exchange rates.

PROFILE

Santen Pharmaceutical Co., Ltd. specializes in the research, development, manufacturing and marketing of ophthalmic and anti-rheumatic pharmaceuticals to protect and improve people's eyesight and health. We have created innovative pharmaceuticals for all types of ophthalmic disorders and provide information tailored to clinical needs. As a result, we lead Japan's market for prescription ophthalmics, which represent nearly 80 percent of our net sales. With marketing and development bases in Japan, the United States and Europe, backed by first-rate R&D capabilities, we aim to increase our corporate value as a world-class company that delivers unique products worldwide.

Toward a New Stage

Deeply aware of the sanctity of human life, we apply our unique capabilities and technologies in our areas of expertise to contribute to the health and quality of life of patients and their loved ones, and society as a whole.

Financial Highlights

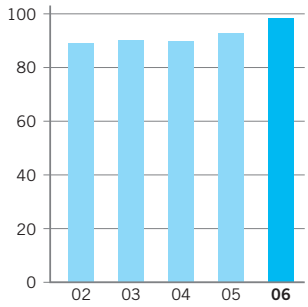
Years ended March 31

	1997	1998	1999	2000	2001
For the year:					
Net sales	¥ 75,216	¥ 77,957	¥ 79,639	¥ 83,577	¥ 88,449
Operating income	19,680	16,144	16,599	17,488	16,518
Net income	8,998	7,323	8,105	7,941	7,714
R&D expenditures	6,213	7,731	7,335	9,221	10,511
Capital expenditures	16,725	5,898	3,443	2,510	4,943
Depreciation and amortization	4,202	6,674	6,314	5,725	5,683
Per share data (yen and U.S. dollars)**:**					
Net income—basic	¥ 105.32	¥ 77.06	¥ 85.27	¥ 83.54	¥ 81.32
Net income—diluted	99.87	71.01	78.63	77.04	75.01
Shareholders' equity (BPS)	877.12	862.88	935.71	1,006.48	1,022.99
Cash dividends, applicable to period	12.00	12.00	12.00	12.00	20.00
At year-end:					
Total assets	¥140,226	¥138,822	¥144,913	¥ 149,968	¥ 153,243
Long-term debt	31,807	31,168	27,496	26,491	25,482
Total shareholders' equity	75,759	81,998	88,950	95,669	94,834
Return on equity (ROE) (%)	11.9	9.3	9.5	8.6	8.1
Number of employees	1,910	2,010	2,037	2,093	2,167
	1997	**1998**	**1999**	**2000**	**2001**

Notes: 1. U.S. dollar amounts have been translated from yen, solely for the convenience of the reader, at the rate of ¥117.47 to U.S.$1 prevailing on March 31, 2006.
2. See Notes 2. 14) and 11 of Notes to Consolidated Financial Statements in respect of per share data.
3. Net sales in the six years ended March 31, 2006 to 2001 include royalty income which was presented as "Other, net" in "Other income (expenses)" through the fiscal year ended March 31, 2000.
4. Figures in parentheses indicate a decrease.

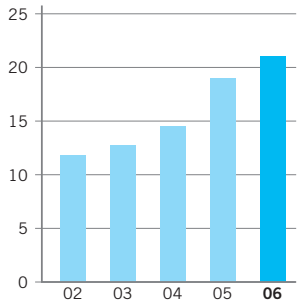
Net sales

(Billions of yen)



Operating income

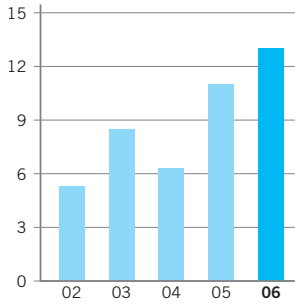
(Billions of yen)



				Millions of yen	Change	Thousands of U.S. dollars
2002	2003	2004	2005	2006	2005/2006	2006
¥ 88,966	¥ 90,253	¥ 89,858	¥ 92,696	**¥ 98,398**	6.2%	**$ 837,643**
11,790	12,697	14,524	18,982	**20,995**	10.6	**178,725**
5,306	8,503	6,321	11,023	**13,023**	18.1	**110,855**
12,187	12,719	11,853	12,620	**13,971**	10.7	**118,935**
6,586	7,046	3,226	4,907	**2,106**	(57.1)	**17,931**
5,334	4,311	4,521	4,750	**4,824**	1.6	**41,073**
¥ 57.34	¥ 93.67	¥ 71.65	¥ 125.85	**¥ 150.26**	19.4%	**$ 1.28**
53.07	85.97	71.64	125.71	**150.01**	19.3	**1.28**
1,048.51	1,104.21	1,176.83	1,249.32	**1,368.27**	9.5	**11.65**
20.00	20.00	40.00	50.00	**60.00**	20.0	**0.51**
¥ 152,103	¥ 147,148	¥ 150,238	¥ 139,980	**¥ 150,458**	7.5%	**$1,280,824**
24,467	23,047	12,686	6,882	**5,614**	(18.4)	**47,791**
95,101	97,126	103,500	108,240	**118,637**	9.6	**1,009,938**
5.6	8.8	6.3	10.4	**11.5**		
2,463	2,500	2,335	2,308	**2,312**		
2002	2003	2004	2005	2006	2005/2006	2006

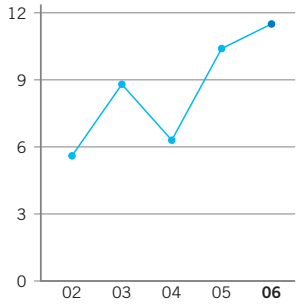
Net income

(Billions of yen)



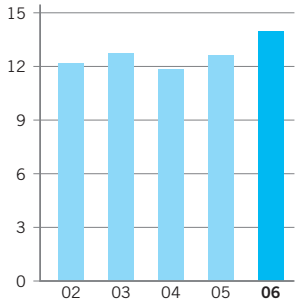
Return on equity (ROE)

(%)



R&D expenditures

(Billions of yen)



New Senior Management

Takakazu Morita
Chairman and
Chief Executive Officer

Akira Kurokawa
President and
Chief Operating Officer

At the first meeting of the Board of Directors subsequent to the Annual General Meeting of Shareholders held on June 27, 2006, Takakazu Morita commenced his new position of Chairman of the Board and CEO of Santen, and Akira Kurokawa assumed the role of President and COO.

Prior to this, as President of Santen, Mr. Morita had been responsible for determining business policies and strategy (the CEO role) as well as the execution of business strategy (the COO role). Following the shift to this new management system, Mr. Morita will chair the Board of Directors in his new capacity, taking responsibility for strategic decision-making and business execution supervision. Mr. Kurokawa assumes responsibility for execution of business strategy, and will oversee the day-to-day business of Santen. This functional separation serves to clarify each role. The aim of the move is to facilitate faster decision-making and business execution in the face of increasingly complex business issues created by a rapidly changing business environment.

Going forward, we remain committed to Santen's core value, "We are focused on specific areas of expertise, such as eye care, developing our unique capabilities and technologies, and contributing to the health and quality of life of patients and their loved ones, and society as a whole." To this end, we aim to continue achieving consistent and stable gains in performance.

Message From Senior Management

Building From a Platform of Record Performance Toward a New Global Enterprise

Record sales and profits in fiscal 2005

We posted record sales and profits in fiscal 2005 (the year ended March 31, 2006). We boosted sales and profits in year-on-year terms through a combination of growth in our prescription pharmaceuticals business and various initiatives designed to increase profitability.

The increasingly aged population in Japan led to an increase in the number of patients receiving treatment which underpinned growth in the Japanese prescription ophthalmics market in fiscal 2005. Revenue growth was led by treatments for glaucoma and corneal disorders. Overseas prescription ophthalmics markets also grew strongly in Europe, the U.S. and Asia.

Based on the market demand for effective therapeutic agents, we expanded our sales of numerous products in Japan, including treatments for glaucoma, corneal disorders, as well as anti-rheumatic drugs. In terms of new products, we received manufacturing and marketing approval in Japan for *PAPILOCK* Mini ophthalmic solution 0.1% for the treatment of vernal keratoconjunctivitis which we launched in January 2006. Our sales in overseas markets also grew steadily, led by operations in Europe and Asia.

In the R&D area we filed an application with the Japanese regulatory authorities in July 2006 to gain manufacturing and marketing approval for DE-085, a treatment for glaucoma and ocular hypertension, which is one of our core therapeutic segments. We also made further progress in initiating clinical trials and expanded our pipeline of drug candidates in other therapeutic segments, including retinal conditions and corneal and conjunctival disorders.

For fiscal 2005, we posted consolidated net sales of ¥98.4 billion, an increase of 6.2% over the previous year. Operating income rose 10.6% in year-on-year terms to ¥21.0 billion, marking a third straight year of double-digit growth. Although continuing investments in R&D and sales expenses led to an increased level of spending in these areas, we were able to achieve a net reduction in the cost-of-sales ratio as a result of a more profitable product mix, increased production volumes and programs designed to generate cost efficiencies. Net income rose 18.1% to ¥13.0 billion, chiefly reflecting higher operating income along with a lower effective corporate tax rate.

At the 94th Annual General Meeting of Shareholders held on June 27, 2006, we received approval for the payment of a year-end cash dividend of ¥35 per share. Including the interim dividend, this brought total dividends applicable to fiscal 2005 to ¥60 per share, an increase of ¥10 compared with the previous year.

Targets of 2003–2005 Medium-term Management Plan exceeded

Fiscal 2005 was the final year of Santen's 2003–2005 Medium-term Management Plan which aimed to establish the foundation for our next phase of growth while ensuring sufficient earnings power. The three key objectives of the 2003–2005 Medium-term Management Plan were to improve profitability, boost R&D capabilities, and reinforce our organizational strength. Over the plan's three-year period, we made substantial progress in each of these three areas.

In terms of improving profitability, a key achievement was the rapid restoration of profitability at our U.S. operations through the establishment of a sales partnership with Johnson & Johnson Vision Care, Inc. (JJVCI) in the U.S. Elsewhere, our switch to the new *Dimple Bottle* as the container for prescription ophthalmic pharmaceuticals not only improved patient utility and helped to differentiate the Santen brand, but also enabled us to improve manufacturing productivity.

Boosting R&D capabilities was focused on accelerating the development of new products and focusing resources to increase the number and quality of new drug development candidates. In the first area, we managed to reduce the length of the clinical trial phase for major development projects to approximately five years, while also shortening the preclinical

phase to approximately 18 months. Aiming to fill the clinical development pipeline, we made steady progress in advancing key projects in the core therapeutic areas of glaucoma and corneal disorders and we also succeeded in boosting the number of drug candidates entering the clinical stage.

Strengthening our corporate governance was a major accomplishment in this three-year plan period. We have also focused on human resource development and initiatives to augment the management capabilities of our organization and in each of these areas we have achieved positive results.

As a result of these efforts, our financial performance has improved across the board. Our results in fiscal 2005 exceeded the initial plan targets in terms of sales, operating income, net income and return on equity (defined as net income divided by shareholders' equity).

Embarking on the 2006–2010 Medium-term Management Plan toward a new stage of Santen's development

We have formulated the 2006–2010 Medium-term Management Plan to guide the growth of Santen over the next five years. During the previous Medium-term Management Plan, we were successful in increasing the efficiency with which we manage our overall business. The main goals of the next five-year period are to set the stage for accelerated growth and to develop and expand our operations in specific regions.

Specifically, our aims are to further Santen's global development by creating a strong pipeline of new drug candidates and by actively developing operations in regions where we can maximize our strengths. To this end, we have established four medium-term strategic policies. These are: first, to enhance the global strategic product pipeline through internal discovery and development, joint development projects and in-licensing efforts; second, to generate growth mainly in Japan, Northern/Eastern Europe, Russia and China while focusing activities in the U.S. market on clinical and business development; third, to strengthen manufacturing bases; and fourth, to strengthen the human resource and organizational capabilities on a global basis. By implementing strategies and initiatives based on these policies in R&D, sales, production, organizational and personnel areas, we aim to achieve solid growth over the five-year planning period.

Under the new senior management, we hope to fulfill the expectations of shareholders and other stakeholders by steadily achieving the aims of our new medium-term management plan. At the same time, Santen continues to be dedicated to making a social contribution by improving the quality of life of patients around the world. In doing so, we believe that we can also maximize corporate value. We sincerely ask for your continued support as we move forward.

September 2006

Takakazu Morita
Chairman and Chief Executive Officer

Akira Kurokawa
President and Chief Operating Officer

Toward a New Stage: The 2006–2010 Medium-term Management Plan

An interview with Chairman and CEO, Takakazu Morita on Santen's new medium-term management plan

"By leveraging our unique strengths, we aim to be a company that makes a significant and worthwhile contribution to patients worldwide."

Takakazu Morita Chairman and CEO

Q.1

Before we discuss the new medium-term management plan, could you first tell us where you see Santen now? What has the company achieved to date?

Santen has concentrated in the fields of ophthalmology and rheumatology. As a specialty company, we have deliberately focused our resources in areas where we can leverage our strengths. This approach has helped us carve out a distinctive identity.

In research and development, which is the source of our growth, we have channeled our resources by concentrating on research themes in the core therapeutic segments with unmet medical needs. These priority areas are glaucoma, corneal conditions such as dry eye, and retinal disorders. This focus has yielded a steady stream of new drug candidates, principally in these core therapeutic segments. We have also targeted acceleration of new drug development, and have succeeded in substantially reducing the time required for preclinical and clinical studies.

Next, in our Japanese business, we have secured the number-one position in the prescription ophthalmics market. These operations are now firmly established as the mainstay of our revenues. Our sales and marketing capabilities in our chosen fields are second to none in Japan. We have a full product portfolio, and extensive experience and expertise which allow us to meet the market needs in Japan.

Nara Research and Development Center

In overseas markets, we began developing operations at an early stage to support our goal of becoming a global company. We started clinical development of drugs in the United States in 1993 and in Europe the following year. In 1997, we acquired a Finnish ophthalmic pharmaceutical manufacturer. We have achieved notably high market positions in Northern Europe, Eastern Europe and Russia. Today, we are also the market leader in China.

On the production front, besides consistent cost-reduction efforts, we have also succeeded in raising manufacturing productivity through the introduction of the new *Dimple Bottle*. This has improved patient utility and drug identification. We can manufacture ophthalmic pharmaceuticals of world-class quality at a highly competitive cost.

Q.2

You have always emphasized Santen's global development as a long-term theme. Please elaborate.

Long-term Vision:

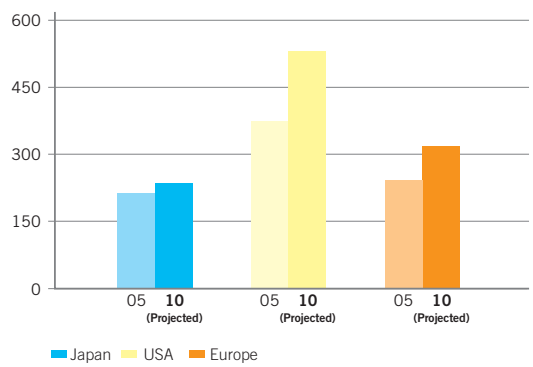
- World-class company
- Leader in the ophthalmic and anti-rheumatic fields
- R&D-oriented pharmaceutical company specializing in ophthalmology and other areas where we can leverage our strengths

There are two reasons why we have made Santen's global development a long-term theme. First, this thinking is based on our core value.

Our mission is to focus on specific areas of expertise, such as eye care, developing our unique capabilities and technologies, and contributing to the health and quality of life of patients and their loved ones, and society as a whole. Today, although our products are prescribed widely in Japan, that is certainly not the case in many other markets. There are still many countries where we can use our experience and expertise to improve the medical treatments available to doctors and patients.

The second reason for global development is its commercial importance. The global ophthalmic market is growing at very different rates in various regions. For instance, in the period from 2005 to 2010, annual growth in the ophthalmic market is projected to average 6% around the world. But looking at this in terms of countries and regions, the compound annual growth rate (CAGR) is expected to be a relatively low 2% in Japan. This compares with the United States and Europe, where CAGRs of 7% and 6%, respectively, are predicted and growth is expected to be at least 10% in China and Russia. In all of these important geographic regions the growth rates are consistently higher than in Japan. This shows that we cannot afford to limit our efforts to the Japanese market if we want to achieve higher growth for the corporation. Our continued ability to fulfill our mission of providing improved health and quality of life to patients depends on our ability to meet the challenge of achieving success in overseas markets.

Ophthalmic Pharmaceutical Market Size by Region (Actual and Projected)



Source: Santen analysis based on IMS data
IMS MIDAS (U.S., Major Western European Countries, Northern Europe, Eastern Europe), 2005, Copyright IMS 2006
IMS JPM (Japan), 2005, Copyright IMS 2006. All rights reserved.

Q.3 What is the plan for Santen's development as a global company?

We have set fiscal 2015—10 years from now—as the target date for realizing our plans for Santen's global development. We view our path as a two-stage process.

We have positioned the five-year period from fiscal 2006 to the end of fiscal 2010 as the first stage. During this time, our aims are to further Santen's global development by creating a strong pipeline of new drug candidates and by actively developing operations in regions where we can leverage our strengths. We have formulated four medium-term strategic policies to guide our efforts during this period. First, we aim to enhance the global strategic product pipeline through internal discovery and development, joint development projects and in-licensing efforts. Second, we will generate growth mainly in Japan, Northern/Eastern Europe, Russia and China while focusing our U.S. activities on clinical and business development. Third, we are strengthening our manufacturing bases. Fourth, we aim to strengthen human resources and organizational capabilities on a global basis. Based on this strategy, we aim to achieve solid growth in the first stage.

In the second five-year period from fiscal 2011 to the end of fiscal 2015, we hope to reap the fruits of our investments in R&D. During this stage, we aim to achieve higher rates of growth as we realize our global ambition, which includes continuing to expand our business in the U.S. market.

Q.4 What is Santen's fundamental R&D strategy?

The fundamental strategy that we have applied consistently over the years is to invest selectively and to concentrate resources on research themes in those areas where there are significant unmet medical needs which we can meet with our unique capabilities and where there is significant growth potential. This strategy is unchanged in the medium-term management plan.

In drug discovery, we focus on areas where there is high medical demand and where we can demonstrate our competitive edge. Our basic aim is to increase the number of new drug candidates that are highly competitive internationally, focusing primarily on next-generation drugs.

Turning to specifics, our core therapeutic segments are glaucoma, corneal conditions and retinal disorders. The network-based approach that we have developed for drug discovery aims to leverage the benefits of collaborative development activities. This means that we combine competitive internal resources with advanced technology from external sources to search for drug discovery targets and to acquire development compounds.

On the development side, we are devoting the majority of our efforts to ensuring that we properly develop those compounds that are likely to drive the growth of our prescription pharmaceuticals business.

Our immediate priority is to gain manufacturing and marketing approvals for the three products that we plan to launch within the period of the new medium-term management plan. These are DE-085, a treatment for glaucoma and ocular hypertension; DE-089, a treatment for corneal and conjunctival disorders; and MD-14, which is an intraocular lens.

Next in the development pipeline are a group of global strategic products that we are planning to launch from 2011 onward (DE-104 for glaucoma and ocular hypertension; DE-096 for retinal disorders that is also an anti-rheumatic; and DE-101 for corneal and conjunctival disorders) and a group of global products (DE-102 for retinal disorders; and DE-099 for corneal and conjunctival disorders).

We have also taken steps to strengthen our global portfolio by creating a strong development pipeline including back-up candidates. In this way we hope to maximize the chances of success for each product in our pipeline.

In addition, we have continued to work on improving our research and development processes. Between fiscal 2003 and the end of fiscal 2005, we specifically targeted an acceleration of clinical development. In the period from fiscal 2006 through fiscal 2010, in addition to maintaining our focus on accelerating our development process, we aim to integrate the drug development processes across our regional R&D centers in Japan, the U.S. and Europe, with additional links to major countries within the Asian market. This is vital in order to create an effective process for developing global strategic products.

Santen's definition of a "global strategic product":
A drug candidate with a novel mechanism of action that has the potential to generate higher sales than current products. Such a product would be marketed in Japan, the U.S. and Europe.
Santen's definition of a "global product":
A drug candidate with an improved mechanism of action compared with existing drugs and that has the potential to generate sales on a par with current products. Such a product would be marketed in Japan and some overseas markets.

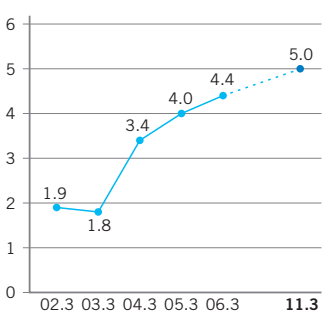
Q.5 Could you tell us about Santen's policies on dividends and other profit distributions to shareholders?

Santen treats the distribution of profit to shareholders as a key management focus. To date, our policy has been to set dividends at a level that is commensurate with performance while at the same time maintaining capital efficiency and keeping a sound and flexible financial position that will allow us to pursue product acquisition, licensing and alliance activities and to build up sufficient retained earnings to fund our long-term growth strategy. We have also made effective use of share buybacks and retirements in a flexible manner. Going forward, this approach will remain our profit distribution strategy.

In the 2006–2010 Medium-term Management Plan, with the aim of generating a future stream of profits to fund more consistent and stable dividends to shareholders, we have adopted the dividend-on-equity (DOE) ratio as a new performance indicator to measure dividends. DOE is calculated by multiplying the payout ratio by return on equity (ROE). We aim to raise DOE to 5.0% by fiscal 2010. This approach is a good way of boosting returns to shareholders in the form of dividends while also improving capital efficiency.

Furthermore, in addition to dividends, we plan to be more proactive in undertaking share buybacks. Our aim over the next five years is thus to have a consistent management focus on providing an appropriate return of profits to our shareholders.

DOE Ratio



An interview with President and COO, Akira Kurokawa on Santen's new medium-term management plan

"We aim to achieve growth by successful launch of new products by focusing resources on those regions where we can make the most of our strengths."

Akira Kurokawa President and COO

Q.1 What are the sales and profit targets in the new plan?

For the final year of the new plan, fiscal 2010, we have set minimum performance targets of ¥115 billion in net sales, operating income of ¥32 billion, net income of ¥22 billion and ROE of 13%. Compared to our results in fiscal 2005, these targets equate to prospective CAGRs of over 3% for net sales and 8% for operating income.

There are three factors that we see contributing to the higher growth rate for operating income relative to net sales. First, during the plan period, we expect to launch products that we have developed in-house for glaucoma, for corneal disorders, and in intraocular lenses. Second, our strategy is to generate growth increasingly from high-value-added products for which there is substantial untapped market demand. Third, we expect to generate ongoing cost savings from the continuing rationalization of our production lines. I believe that these various initiatives will more than absorb higher spending on R&D and promotion. I feel confident that we can hit the targets we have set.

Q.2 How do you aim to develop Santen's prescription pharmaceuticals operations in Japan, and what are the major business objectives?

We forecast a CAGR of approximately 2% for the Japanese prescription ophthalmics market in the period from 2006 through 2010. How we expand sales and raise profitability in this market will be a major determinant of Santen's overall financial performance during the next five years.

We have already established a strong promotional base in Japan in the specialized areas of ophthalmic medicine and rheumatology. Our basic strategy in these fields—in both of which I believe we can maximize our strengths—is to launch new products while at the same time working to expand sales of the existing product portfolio.

Turning first to the glaucoma market, we expect this market to achieve a CAGR in volume terms of 5% over the next five years. In the plan period we expect to launch DE-085, a prostaglandin treatment for glaucoma that we developed in-house. Our objective is to effectively market this drug so that we can derive

the maximum market value as quickly as possible. Using our overwhelming sales presence in this market—one of our greatest strengths—we plan to quickly raise awareness for the new drug and thus maximize prescription numbers.

Next, in the market for corneal conditions, a volume CAGR of approximately 8% is forecast. This reflects a number of factors driving growth in the dry eye market, such as increasing numbers of people wearing contact lenses or using personal computers or other equipment with display monitors for long periods, plus the ongoing aging of the population. In this segment, one goal is to expand sales of our existing product *Hyalein*. We also expect to launch DE-089 as a new treatment for corneal disorders in the latter half of the plan period. Once we have both drugs on the market, this will improve our ability to offer medical professionals a wide range of treatment options for varying medical conditions within this segment. We also plan to conduct campaigns to boost awareness of dry eye among patients. Through an effective combination of these approaches, we intend to realize increased sales and profits from this segment.

We expect the needs of medical professionals to become more diverse. We also anticipate fiercer competition due to the entry of rival companies. In such a competitive business environment, it is critical that we continue to raise the quality of our promotional activities so we can ensure a successful launch for all new products. To this end, we are increasing the number of specialist medical representatives in both ophthalmology and rheumatology as well as further enhancing training programs focused on scientific knowledge and professional skills in both fields.

Q.3 What is Santen's business development strategy in overseas markets?

In the five years to 2010, our overseas business strategy is, first, to concentrate on priority regions. We are tailoring the development of each of these regions to their specific characteristics.

In terms of actual regions, we plan to focus most of our development efforts on countries where growth is expected, where we have already built up a certain commercial presence and where we can make the most of our strengths. These regions are Northern Europe, Eastern Europe, Russia, Germany and China.

In Northern Europe, Eastern Europe and Russia, we are using in-licensing of local European products to supplement the sales of our existing lineup so that we can boost our overall market presence. Over the next five years, we aim to increase sales within this region to ¥9.0 billion, which is equivalent to a CAGR of approximately 8%. In particular, we plan to enhance our position within the growing Russian market for prescription ophthalmics through the launch of our anti-infective *Oftaquix*. This will add to the growth that we have achieved with our existing lineup of cataract treatments. In Northern Europe, Eastern Europe and Germany, we will boost promotional efforts to increase sales, particularly in the two key therapeutic segments of glaucoma and corneal disorders.

In China, we aim to achieve sales of ¥4.5 billion within five years, which is equivalent to a CAGR of about 25%. We have been targeting the huge potential of the Chinese market for many years now. We began exporting to China in 1988, and today we are the market leader in our target segments. We are also taking the steps necessary to build a robust base of in-house operations within the country. In 2005, we

established a local subsidiary Santen Pharmaceutical (China) Co., Ltd., to conduct manufacturing and direct sales and marketing in China. Using this new base, we have adopted sales and marketing techniques based on academic studies and other medical information. Our promotional goals are to make our mainstay products *Cravit* and *Hyalein* first-choice prescription drugs within the Chinese market.

In the United States, while continuing to develop the business by promoting our existing product lineup through the sales partnership with Johnson & Johnson Vision Care, Inc., we are also focusing on further development of our in-house capabilities for both clinical development and business development.

Q.4 What is Santen's strategy in HR and organizational management?

Whether you are trying to create and manufacture a product or whether you are trying to achieve your plan targets, my personal belief is that people and organization are vital.

It is important to tap the potential of employees and develop their abilities in order to create a strong organization. We value an open and fair atmosphere in which employees can work proactively.
We are strengthening development of Santen's human resources in Japan. This is critical if we are to stake claim to an even higher position in our home market, particularly with overseas firms providing much stiffer competition these days. I believe that we also have to put a lot of effort into overall HR development so that we can forge the internal talent pool needed to realize Santen's transformation into a global company.

In terms of upgrading our organizational management, we are focusing on three areas: R&D, production and strategic marketing.

Within R&D, we are developing integrated clinical development functions across Japan, Europe, the U.S. and Asia with the aim of sharing data between regions and making our clinical development more efficient. Our goal is to upgrade our R&D capabilities so that we have a high-quality, high-speed global clinical development capacity. We are also working to integrate regulatory functions within global drug development.

We are seeking to integrate capabilities worldwide on the production side, too. We plan to optimize production across our three regional manufacturing bases in Japan, Finland and China.

Finally, in strategic marketing, our goal is to establish a global marketing function to ensure our product development efforts support our commercialization goals and prepare for the launch of the global strategic products currently in development.

Through these strategic initiatives we aim to create a stronger and more talented organization. Besides helping us to achieve the medium-term plan objectives, these moves will also help us to further improve our corporate value.

Research and Development

Santen's R&D vision is to provide a continuous flow of products that satisfy unmet medical needs and contribute to improved patients' quality of life (QOL). To realize this vision, we focus our resources in ophthalmology and other specific fields where we can play a leading role, and work to expand the number of new drug candidates, to manage clinical development in an effective manner, and to bring products to market as quickly as possible. To the same end, we are both strengthening our R&D systems and utilizing external resources for product development, including joint research with other firms and technology partnerships.

Development Update and Outlook

In R&D, we have defined glaucoma, retinal conditions, and corneal and conjunctival disorders as our three priority therapeutic fields. We are striving to boost new drug development by improving the quality and efficiency of our ophthalmology research—an area where we have extensive experience.

In the glaucoma field, we filed for manufacturing and marketing approval for DE-085 (generic name: tafluprost), a treatment for glaucoma and ocular hypertension, in Japan in July 2006. We are preparing to file for approval in Europe during the year ended March 31, 2007 and we will decide whether to file in the U.S. on the basis of an analysis of future business potential. In addition, we have signed an agreement with Ube Industries, Ltd. on the joint development of DE-104, which has a novel mechanism of action compared with existing drugs. We are moving ahead with preparations for clinical studies. In other news, we have temporarily suspended clinical studies on DE-092 (olmesartan) and will decide whether to restart clinical development once we have repeated dose-finding studies based on an improved formulation.

In the field of retinal conditions, we have started Phase II clinical trials in Japan on DE-096 for diabetic macular edema. DE-096 is also undergoing Phase II trials as a treatment for rheumatoid arthritis. In March 2006, we signed an agreement with U.S. firm Oakwood Laboratories L.L.C. on the development and licensing of manufacturing technologies for DE-102, a steroid microsphere-based product (note 1) that is also being developed to treat diabetic macular edema. Under the agreement, Santen will work with Oakwood on the development of manufacturing technologies, utilizing Oakwood's technical and developmental expertise in the area of microsphere products.

In the field of corneal and conjunctival disorders, we have begun Phase III clinical trials in Japan on DE-089 (diquafosol tetrasodium), a treatment for corneal and conjunctival epithelial disorders including dry eye. We are also conducting Phase I trials in the U.S. on DE-101 (rivoglitazone) as a treatment for corneal and conjunctival epithelial disorders including dry eye. Santen has acquired exclusive development, manufacturing and marketing rights worldwide for this compound from Sankyo Co., Ltd.

In the field of inflammation and allergies, in January 2006, we launched the vernal keratoconjunctivitis treatment *PAPILOCK* Mini ophthalmic solution 0.1%, which had been developed as an orphan drug (note 2). In March 2006, we signed an agreement with Ono Pharmaceutical Co., Ltd. on the exclusive development, manufacturing and marketing rights in Japan to DE-103 for allergic conjunctivitis.

We are also actively engaged in discovery research on next-generation ophthalmic drugs. As part of this work, in March 2006, we signed a three-year joint research contract with CytoPathfinder, Inc. on the application of its cubic liquid crystal technology to ophthalmic drug development. This technology is expected to have a wide range of applications, including in drug delivery and the search for drug discovery targets for the treatment of ophthalmic disorders using genetics-related assessment techniques. We will be conducting research to identify drug targets and therapeutic nucleotide derivatives and small molecules.

Notes 1: Steroid microsphere-based product: A product comprising a steroid encapsulated within a microsphere.
2: Orphan drug: A drug for which there is a high degree of medical need but small patient numbers mean that the drug is unlikely to be profitable. Orphan drug R&D is eligible for government subsidies in Japan.

Pipeline of prescription pharmaceuticals (Clinical studies)

As of September 2006

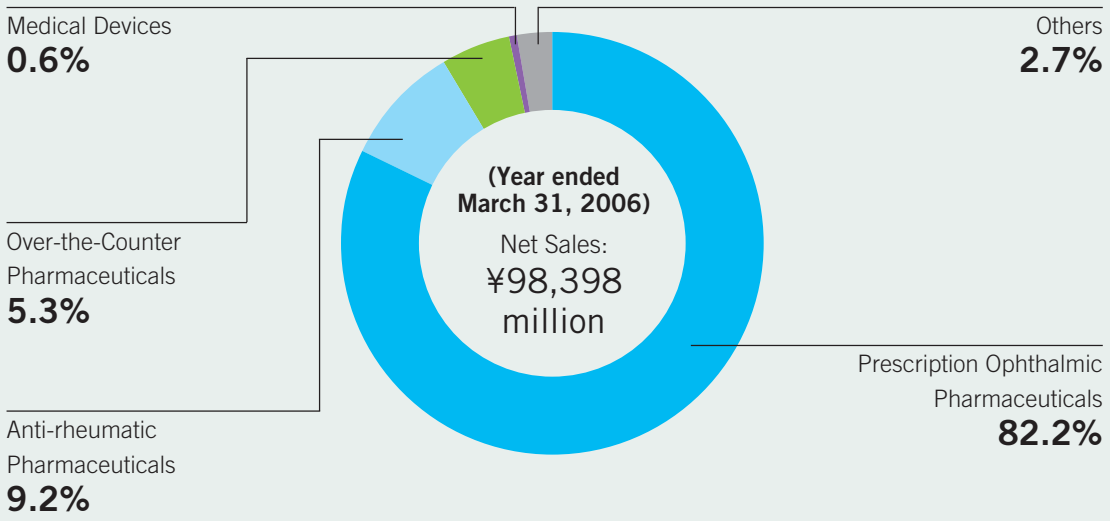
Generic name	Brand name/ Dev. Code	Indication	Region	Phase I	Phase II	Phase III	NDA Filed	Characteristics
Pemirolast potassium	Alamast	Allergic conjunctivitis	Europe				○	A mast cell stabilizer with superior efficacy on allergic conjunctivitis and vernal keratoconjunctivitis.
Tafluprost	DE-085	Glaucoma/ Ocular hypertension	Japan Europe USA			○	○ ○ (In preparation)	Prostaglandin glaucoma treatment for ocular hypertension. Has demonstrated a potent and stable inter ocular pressure-lowering effect by promoting uveoscleral outflow. It can be stored at room temperature.
Diquafosol tetrasodium	DE-089	Corneal and conjunctival epithelial disorder associated with dry eye, etc.	Japan			○		A treatment for corneal and conjunctival epithelial disorder associated with dry eye, etc. that stimulates the ocular surface to secrete tear fluid and moisture. Expected to be used in combination with existing dry eye treatments.
Levofloxacin + prednisolone A	DE-094	Infectious keratitis	USA		○			Fluoroquinolone antibacterial agent. A combination treatment with steroids.
Olmesartan	DE-092	Glaucoma/ Ocular hypertension	Japan USA/ Europe		○ (Suspended) ○ (Suspended)			The angiotensin II receptor antagonist. Currently, the clinical studies are suspended. We will decide whether we resume the clinical studies after conducting another pilot study with different doses and different formulation.
Lomerizine HCL	DE-090	Glaucoma	Japan		○			A new type of oral glaucoma treatment studied for inhibiting the progression of visual field defects. The only calcium antagonist in full-fledged development as a glaucoma treatment. Compared with NMDA receptor antagonists, fewer generalized side effects are expected, thus having excellent safety. Marketed by Nippon Organon as a migraine drug.
(Undetermined)	DE-096	Rheumatoid arthritis Diabetes Macular Edema	Japan Japan		○ ○			An oral TNF inhibitor. Anti-rheumatic effect comparable to injectable biological agents. In addition to RA, the effect on DME was also observed in basic research, and the phase II studies are being conducted with both diseases.
Gefarnate	DE-099	Corneal and conjunctival epithelial disorder associated with dry eye, etc.	Japan	○				Treats corneal and conjunctival epithelial disorder mostly associated with dry eye, by stimulating the secretion of mucin and promoting the corneal epithelial migration. Preservative-free eye ointment that can be used in combination with existing drugs.
Rivoglitazone	DE-101	Corneal and conjunctival epithelial disorder associated with dry eye, etc.	USA	○				It is expected to show a potent effect on corneal and conjunctival epithelial disorders by directly acting on the corneal and conjunctival epithelial cells. It has an action mechanism which differs from any other existing treatment or drug candidate in development.

When safety and efficacy of candidate compounds are determined in preclinical studies, they undergo the following clinical trials. After completing the Phase III clinical trials, a new drug application (NDA) is filed for marketing approval.

Phase I: Tests to check drug safety with a small number of healthy volunteers.
Phase II: Tests to determine dosage and administration method with a small number of patients.
Phase III: Tests to confirm safety and efficacy by comparing to existing drugs and placebo with a large number of patients.

Review of Operations

Sales by Business



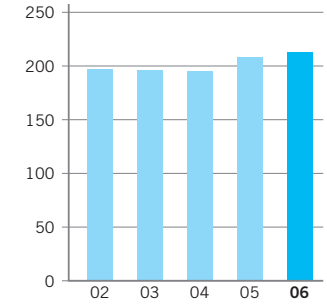
Business Area		Description of Business	Market Share; Market Position
Prescription Pharmaceuticals	Ophthalmic Pharmaceuticals	• Santen enjoys a position as the leader of the Japanese prescription ophthalmics market. We deploy 400 medical representatives (MRs), the largest number in the industry, and our product lineup covers a broad array of ophthalmic disorders. • Overseas, Santen markets levofloxacin ophthalmic solution (brand names: *Quixin*, *Oftaquix* and *Cravit*) and other products through a sales network in the United States, Europe and Asia.	40.9%; Number One[1]
	Anti-rheumatic Pharmaceuticals	• In Japan, we offer *Rimatil* and *Azulfidine EN*, physicians' disease modifying anti-rheumatic drugs (DMARDs) of choice for treating rheumatoid arthritis.	45.2%; Number One[1]
Over-the-Counter (OTC) Pharmaceuticals		• Our OTC pharmaceuticals business consists of market-leading eye drop brands in Japan such as *Sante FX Neo*, the *Sante 40* series and the *Sante de U* series.	Approx. 20%; Number Two[2]
Medical Devices		• In Japan, Santen handles medical devices used in cataract surgery, including intraocular lenses and phacoemulsification machines.	–

Notes:

1. Market share and market position in Japan for the year ended March 31, 2006. The share and position for anti-rheumatic pharmaceuticals represent those in the disease modifying anti-rheumatic drugs (DMARDs) segment.
   Source: Santen analysis based on IMS data. Copyright IMS Japan KK, 2006. All rights reserved.
2. Market share and market position in the Japanese OTC eye drop market for the year ended March 31, 2006. Source: Santen Pharmaceutical Co., Ltd.

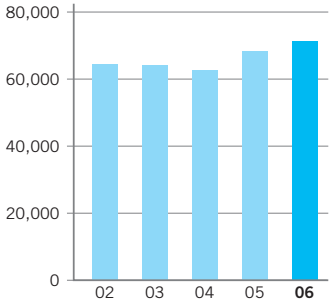
Prescription Ophthalmics Market in Japan

(Billions of yen)



Sales of Prescription Ophthalmic Pharmaceuticals in Japan

(Millions of yen)



Japanese Prescription Ophthalmics Market by Therapeutic Field

(Year ended March 31, 2006)

Glaucoma	37.1%	Infection	12.5%
Corneal disorder	12.0%	Allergy	11.5%
Surgical preparation	6.8%	Steroid	5.3%
Cataract	3.1%	Others	11.7%

Japan

The Japanese prescription ophthalmic pharmaceuticals market expanded in the year ended March 31, 2006. Market growth in year-on-year terms was highest in the segments for glaucoma and corneal disorders.

Since glaucoma is a condition associated with aging, the number of glaucoma patients in Japan is expected to continue rising as the country's population ages. The number of patients seeking treatment for corneal and conjunctival epithelial disorders associated with dry eye is also increasing, reflecting growth in the elderly population and the widespread use of information technology.

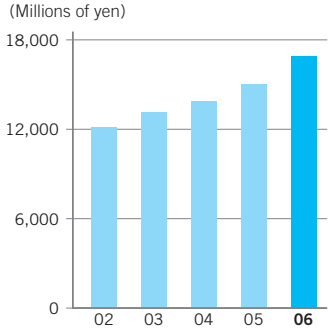
Under these market conditions, Santen continued to focus on maintaining and expanding its earnings base by concentrating resources in key growth segments (glaucoma, corneal and conjunctival disorders, and allergies). Sales and marketing activities focused on boosting the market share of select drugs by supplying information to healthcare professionals to cater to unmet and evolving market needs. *Rescula*, a glaucoma treatment of which Santen began sales of in October 2004, made a significant contribution to sales. Overall, sales of prescription ophthalmic pharmaceuticals in Japan totaled ¥71,215 million, an increase of 4.1% compared with the previous year.

The National Health Insurance (NHI) drug price cut that was implemented in April 2006 is expected to affect the Japanese market for prescription ophthalmic pharmaceuticals in the year ending March 31, 2007. Market competition is also expected to intensify with the launch of new rival products in several therapeutic categories. Santen plans to leverage its traditional strengths in sales and marketing in the domestic market for prescription ophthalmic drugs to combat rival products and expand earnings by focusing on retaining and building on its competitive edge in key growth areas. On the R&D front, Santen continues to work on strengthening the pipeline of new drug candidates through a combination of in-house drug discovery, joint development and in-licensing of innovative compounds from both domestic and international sources, while also seeking to establish sales platforms of new products.

Note: All graphs in this section are based on fiscal years ended March 31.

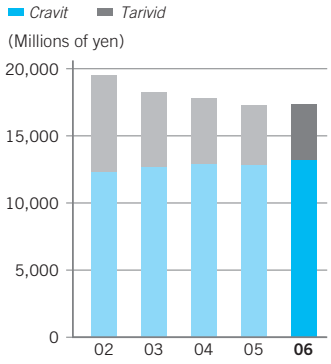
Hyalein

Sales of *Hyalein*



Cravit and *Tarivid*

Sales of *Cravit* and *Tarivid*



Treatments for Corneal/Conjunctival Disorders

The Japanese market for drugs used to treat corneal and conjunctival epithelial disorders associated with dry eye grew approximately 11% in year-on-year terms in the year ended March 31, 2006.

The number of people in Japan suffering from dry eye is estimated in excess of eight million, and this figure is expected to continue rising with the spread of personal computers, increasing use of contact lenses and the aging of the population. More physicians are recognizing that dry eye is a condition that requires treatment, since it is not just a matter of inadequate ocular hydration but may also inflict damage to the cornea.

Santen's mainstay drug in this field is *Hyalein*, a highly water-retentive ophthalmic solution that is effective in relieving corneal and conjunctival epithelial disorders associated with conditions such as dry eye. The drug works by enhancing tear film stability and its use is recognized as contributing to higher quality of life (QOL) for patients. Santen continues to raise public awareness of this condition and provides information to healthcare professionals on the diagnosis and treatment of dry eye. Sales of *Hyalein* rose steadily in the year ended March 31, 2006, increasing 11.1% to ¥15,815 million in Japan.

Santen aims to build on the competitive edge enjoyed by *Hyalein* by continuing to provide healthcare professionals with appropriate information and services.

Anti-Infective Ophthalmics

The Japanese market for anti-infective ophthalmics was roughly flat in the year ended March 31, 2006 after declining in the past few years due to a drop in the number of eye infection consultations because of medical cost-cutting policies. Santen continues to be the market leader in this segment with a market share of approximately 78% with a product portfolio that includes *Cravit* and *Tarivid*, both of which have outstanding clinical efficacy and safety profiles. These drugs are widely used to treat common ocular infections such as keratitis and conjunctivitis, and are also used in conjunction with surgical procedures to minimize the risk of surgical infection.

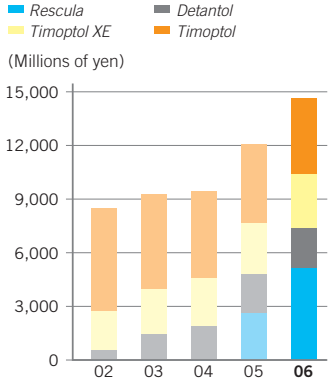
Thanks to a special anniversary campaign to mark the fifth year of its launch and other promotional efforts, sales of *Cravit* increased during the year ended March 31, 2006. However, aggregate domestic sales of the two drugs declined under testing market conditions, falling 1.5% to ¥16,103 million.

Santen will defend its dominant share of the anti-infective ophthalmics market by continuing to promote *Cravit's* clinical efficacy and safety, backed by scientific data, and by providing more information on ocular infections to further solidify *Cravit's* position as the drug of first choice to treat ocular infections.

Note: All graphs in this section are based on fiscal years ended March 31.

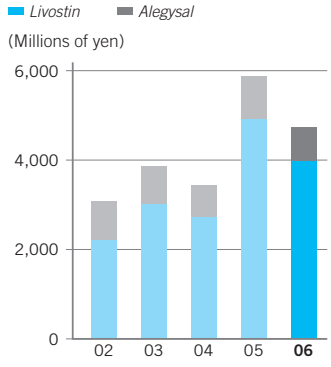
Rescula and *Detantol*

Sales of *Rescula*, *Detantol*, *Timoptol XE* and *Timoptol*



Livostin and *Alegysal*

Sales of *Livostin* and *Alegysal*



Treatments for Glaucoma

Glaucoma treatments are the largest segment of the Japanese prescription ophthalmic pharmaceuticals market, accounting for approximately 37% of total market value. Population aging has resulted in consistent growth in patient numbers in recent years, and the glaucoma market expanded approximately 5% in year-on-year terms in the year ended March 31, 2006.

Santen continued to provide the latest information on glaucoma and recommended treatments to establish a strong presence in the field ahead of the anticipated launch of new products such as DE-085 (generic name: tafluprost), which is currently being reviewed for manufacturing and marketing approval. In its first full year of sales after its introduction in October 2004, *Rescula* recorded approximately double the sales in the previous year. *Detantol* and *Timoptol XE* also posted higher sales than in the previous year. Including *Timoptol*, aggregate domestic sales of Santen's four treatments totaled ¥14,661 million, an increase of 21.6% compared with the previous year.

In the year ending March 31, 2007, Santen plans to continue promoting the effectiveness of *Rescula* and *Detantol* as optimal treatments for normal tension glaucoma, thereby meeting the treatment needs of healthcare professionals while helping to improve QOL for glaucoma patients.

Anti-Allergy Ophthalmics

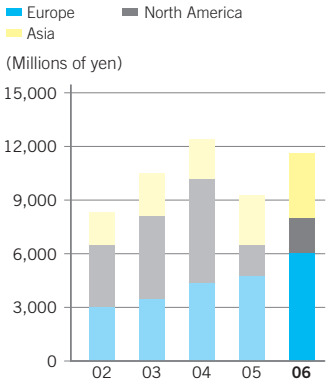
Sales of *Livostin* in the year ended March 31, 2006 fell 19.0% in year-on-year terms to ¥3,984 million, mainly due to significantly lower cedar and cypress pollen counts in Japan (airborne pollen is one of the main causes of allergic conjunctivitis). Sales of *Alegysal* were also substantially lower at ¥677 million, a 25.5% decline. Aggregate domestic sales of the two drugs declined 20.0% to ¥4,661 million. The drop in pollen counts resulted in a significant contraction of the entire market for anti-allergy ophthalmics, leading to lower sales. However, Santen steadily increased its market share to around 25% by promoting *Livostin* specifically for fast relief of itching and by targeting MR activities at specialists other than ophthalmologists, such as otorhinolaryngologists.

Santen will target gains in sales and market share by emphasizing the utility of *Livostin* in providing symptomatic relief of both year-round and seasonal allergies.

In January 2006, Santen launched *PAPILOCK* Mini ophthalmic solution 0.1% for the treatment of vernal keratoconjunctivitis in patients with symptoms that cannot be adequately treated with existing anti-allergy drugs. Santen's range of anti-allergy ophthalmics now meets the needs of a broad range of patients with ocular allergic conditions, including allergic conjunctivitis and vernal keratoconjunctivitis.

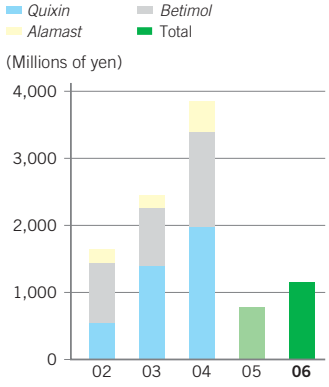
Note: All graphs in this section are based on fiscal years ended March 31.

Overseas Sales



* Overseas sales include prescription ophthalmics and other products.

Sales of *Quixin*, *Alamast* and *Betimol*



* Sales in and thereafter February 2004, when the marketing channels were changed, represent combined sales of three products to JJVCI.

Overseas Markets

Overseas sales grew substantially in the year ended March 31, 2006, led by Europe and Asia. After conversion into yen, total overseas sales increased 25.5% over the previous year to ¥11,613 million. Of this total, sales of prescription ophthalmic pharmaceuticals equaled ¥9,706 million, an increase of 34.0% in year-on-year terms.

United States

The U.S. market, the largest market for prescription ophthalmic pharmaceuticals in the world, continues to expand as the aging of the baby-boom generation drives growth in the number of patients suffering from age-related eye conditions such as glaucoma and age-related macular degeneration (AMD). Competition also continues to intensify in the anti-infective ophthalmics segment.

During the year ended March 31, 2006, the distribution and supply agreement with Johnson & Johnson Vision Care, Inc. (JJVCI) generated steady growth in sales of three drugs covered by the agreement—the anti-infective ophthalmic *Quixin* (sold as *Cravit* in Japan), the glaucoma treatment *Betimol*, and the anti-allergy ophthalmic *Alamast* (sold as *Alegysal* in Japan). Following an inventory supply adjustment in the previous year, sales in the U.S. rose 12.4% on a year-on-year basis to ¥1,916 million.

Under the 2003–2005 Medium-term Management Plan, Santen's main objective in the U.S. market was to make operations profitable as quickly as possible. The switch in February 2004 from direct sales to the sales partnership with JJVCI resulted in the swift restoration of profitability. Going forward, the core aims are to strengthen the pipeline of new drug candidates by leveraging U.S.-based R&D capabilities and to bolster business development activities.

Europe

In recent years, the market for prescription ophthalmic pharmaceuticals in Europe has maintained annual growth of 5–10%, due to increasing numbers of patients suffering from glaucoma and dry eye along with solid economic growth in Eastern Europe and Russia. At the same time, however, the promotion of generics and other measures to restrict growth in medical costs adopted by various governments across Europe have contributed to an increasingly challenging business environment. European markets also differ substantially in terms of health insurance and drug pricing systems by country, making it difficult to pursue a single pan-European strategy.

Note: All graphs in this section are based on fiscal years ended March 31.

Santen's booth at the World Ophthalmology Congress (WOC), February 2006

Subsidiaries such as Santen Oy (Finland), Santen GmbH (Germany) and Santen Pharma AB (Sweden) sell ophthalmic pharmaceuticals in Northern and Eastern Europe, Germany, Russia and other local markets. Santen Oy also undertakes clinical development and manufacturing for the European and U.S. markets. In Europe, the anti-infective ophthalmic *Oftaquix* (sold as *Cravit* in Japan) is currently sold in 12 countries, including Finland, Sweden and Germany. Santen is acknowledged as a reliable partner for ophthalmologists in niche markets, including anti-infective ophthalmics for applications such as the treatment of post-operative infections. During the year ended March 31, 2006, Santen achieved steady growth in sales in Northern and Eastern Europe, Russia and Germany, and also sought to raise profits through cost reductions and other efficiency enhancing initiatives. Sales of ophthalmic pharmaceuticals in Russia in particular posted robust growth, contributing to an overall increase in European sales of 27.0% compared with the previous year, to ¥6,089 million.

Asia

Santen is developing prescription pharmaceuticals business in 10 markets in Asia, notably China, South Korea and Taiwan. Santen's vision for the Asian market is to become the top drug manufacturer in ophthalmology by building trust-based relationships with patients and medical professionals and thereby contributing to the development of improved ophthalmic treatments in Asia. Santen primarily exports products to Asian markets for sale through local distributors.

Groundbreaking ceremony at Santen Pharmaceutical (China) Co., Ltd., July 2006

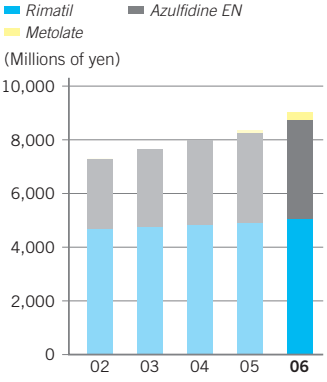
Santen's focus in the year ended March 31, 2006 was to boost the supply of scientific information to physicians in Asian markets and to bolster marketing activities. Sales rose steadily in the main target markets of China and South Korea. Overall, sales in Asia were 31.1% higher than in the previous year, reaching ¥3,608 million.

The Chinese market is expected to expand over the medium to long term, reflecting both population and economic growth. Since opening representative offices in Beijing and Guangzhou, Santen has focused on developing promotional activities in the major cities through the dissemination of scientific information. The leading products are the anti-infective ophthalmic *Tarivid* and the corneal and conjunctival disorder treatment *Hyalein*.

Santen established a new office in Shanghai in July 2005 to increase the communication of scientific product information and the collection of data on drug-related clinical needs in the local market. In September 2005, Santen also established a wholly owned subsidiary, Santen Pharmaceutical (China) Co., Ltd. This subsidiary is due to commence operations in China by 2009, with the completion of construction of a new manufacturing facility and the creation of an in-house sales and marketing network.

Prescription Pharmaceuticals *Anti-Rheumatic Pharmaceuticals*

Sales of *Rimatil*, *Azulfidine EN*, and *Metolate*



Rheumatoid arthritis is an inflammatory disorder that affects the whole body, causing pain and swelling associated with inflammation in joints throughout the body. A progressive disease, it can result in destruction of bone and cartilage leading to joint deformation. It may even cause organ damage. An estimated 700,000 people in Japan are afflicted with the condition.

The market for disease-modifying anti-rheumatic drugs (DMARDs*) for the year ended March 31, 2006 was ¥23.8 billion, an increase of 2% due to the increased number of patients associated with an aging population and the growth in sales of high-priced drugs. Santen is the leading supplier in the DMARD market with three products—*Rimatil*, *Azulfidine EN* and *Metolate* (all tablet formulations). Sales of the flagship product *Rimatil* rose 3.1%, while sales of *Azulfidine EN*, a drug with an early-onset effect, increased 10.1%. *Metolate*, which was launched in July 2004, also achieved steady gains in market penetration. Overall sales of the three DMARDs amounted to ¥9,041 million, an increase of 8.2% compared with the previous year. Santen's share of the Japanese DMARD market increased from 42.9% in the previous year to 45.2%.

The Guidelines for the Management of Rheumatoid Arthritis published by the Japan Rheumatism Foundation in April 2004 state that DMARDs can be effective in delaying the progression of bone and cartilage destruction if administered from the onset of the disease, thus improving patients' quality of life. These guidelines designate *Rimatil*, *Azulfidine EN* and *Metolate* as "Recommendation Grade A," meaning that the drugs are strongly recommended as treatment options. Santen intends to achieve further market share gains by capitalizing on the effectiveness of these three drugs based on the guideline recommendations.

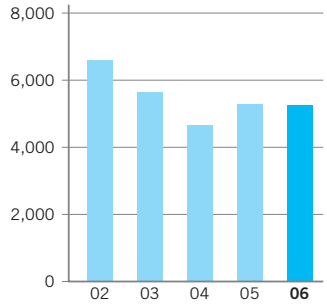
Since 2003, new categories of drugs such as tumor necrosis factor (TNF) inhibitors (injectable solution) have been launched in Japan for the treatment of rheumatoid arthritis. Santen is currently developing DE-096, a TNF inhibitor that is administered orally.

* Disease-modifying anti-rheumatic drugs (DMARDs) are a class of medicines whose anti-rheumatic effect involves calming of inflammation through the correction of immune abnormalities characteristic of rheumatoid arthritis.

Note: All graphs in this section are based on fiscal years ended March 31.

Over-the-Counter Pharmaceuticals

Sales of OTC Pharmaceuticals



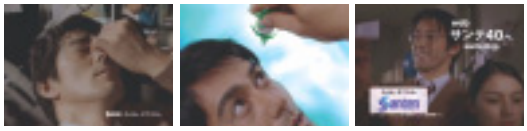
Sante 40V and *Sante FX Neo*

Santen has developed its over-the-counter (OTC) pharmaceutical business in Japan by concentrating on a broad range of eye drops. OTC brands include the top-selling *Sante FX Neo* and the *Sante 40* series, which is promoted for relieving blurred vision.

The Japanese OTC market for ophthalmic medicines was virtually flat in the year ended March 31, 2006, although sales of anti-allergy eye drops declined due to the steep fall in pollen counts compared with the previous year's season. Overall, sales of OTC pharmaceuticals declined 0.5% in year-on-year terms, to ¥5,248 million.

In September 2005, Santen established new units within the OTC Products Sales & Marketing Division to strengthen planning and marketing functions. At the same time, organizational reforms aimed at increasing the speed in which Santen can incorporate customer and consumer input into product development at the planning stage involved relocating the OTC headquarters to Tokyo, since this is the largest consumer market in Japan. Other reforms included the introduction of IT-based sales and promotional support systems. The revised sales organization and processes are expected to improve the development of high-value-added products through stronger connections and smoother communication between the sales organization and central corporate functions.

Going forward, Santen plans to focus promotional sales activities on both established and new products, particularly OTC medicines that relieve conditions such as eye fatigue or blurred vision, and that can provide cool refreshment for fatigued eyes.

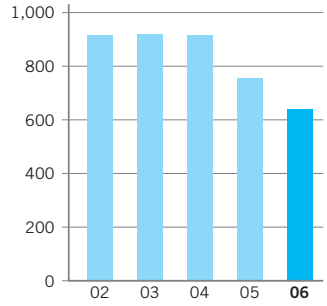


Shots from the TV commercial for *Sante 40*

Note: All graphs in this section are based on fiscal years ended March 31.

Medical Devices

Sales of Medical Devices



Santen's medical device business specializes in intraocular lenses (IOLs) and other products used in cataract surgery.

The number of cataract procedures performed in Japan increased slightly in the year ended March 31, 2006. Sales of *ClariFlex*, a foldable IOL that was the focus of promotional efforts, increased in volume and value terms. However, Santen's overall IOL sales were only on a par with the previous year due to increased competition. Total sales of medical devices fell 15.4% in year-on-year terms to ¥639 million. This reflected a number of factors, including the discontinuation of surgical instrument sales at the end of December 2004.

Demand in the IOL market has shifted in recent years toward new materials and foldable lenses that can be inserted through a small incision. Advanced Vision Science, Inc., a U.S.-based Santen subsidiary, is developing an original foldable IOL (development code: MD-14) made out of new high refractive index optical material. Santen has applied for regulatory approval to manufacture and market this lens in Japan, and a regulatory filing in the United States is pending.

Note: All graphs in this section are based on fiscal years ended March 31.

Society and the Environment

Santen aims to achieve sustained growth as a company. For this, the Company believes that it must conduct business activities targeting higher profits while at the same time fulfilling its corporate social responsibilities. Communication with all stakeholders is also vital in this context. Above anything else, as a company active in the medical field, which directly affects people's lives, Santen must earn the trust of all sections of society.

From this perspective, Santen is committed to upholding corporate ethics while conducting activities in a sound manner in a host of fields as it works to help advance society and protect the environment.

Santen Corporate Ethics Mission

Santen believes that it must deepen trust with society by conducting sound, socially aware business activities, and through this process, fulfill its obligations and responsibilities as a corporate citizen.

It was this thinking that led Santen in 1999 to create the Santen Corporate Ethics Mission, which is revised in line with changing social conditions.

The Santen Corporate Ethics Mission consists of a corporate action declaration and a corporate code of conduct. The former expresses Santen's basic stance on business activities with respect to society, customers, shareholders, suppliers and employees. The code of conduct, meanwhile, expresses decision-making guidelines for conducting business, thus serving as a touchstone for expected standards of behavior for Santen executives and employees.

Executives and employees of Santen are required to internalize these corporate ethics guidelines and to act and make decisions based on a shared awareness of them.

A Company That Has Society's Trust

As mentioned earlier, Santen conducts corporate activities to win the trust of all stakeholders.

In terms of its relationship with customers, Santen is committed to improving patients' quality of life (QOL). In this vein, Santen works to develop outstanding pharmaceutical products, as well as to improve drug administration and identification. In addition, Santen has established a world-class quality assurance system based on a proprietary basic quality policy. At the same time, it has earned high marks for post-market safety management. Moreover, Santen provides accurate information quickly to medical practitioners and other healthcare professionals through medical representatives (MRs), and provides an accurate response to customer and supplier consultations and feedback through a dedicated helpline.

In terms of its relationship with society, Santen makes donations and provides other relief to support victims of major natural disasters such as Hurricane Katrina in the U.S. and the large earthquake in Pakistan in 2005. Santen has also continuously made donations to charitable organizations, including Helen Keller International, a non-profit organization helping to prevent blindness worldwide. Santen has established a scholarship fund to nurture outstanding ophthalmologists in Asia. The fund also helps to train people who will invent tomorrow's cutting-edge technology. Santen has endowed university courses to this end.

The *Dimple Bottle* has enhanced usability and identification.

In terms of its relationship with employees, Santen has a non-discriminatory workplace environment and personnel system. Santen respects the human rights and individuality of all employees, a stance that is underscored by an online-based human rights education program and the launch of a project to help employees balance their work and child-rearing commitments. And by encouraging personal growth through friendly competition, Santen helps employees to become more independent and lead fuller lives. Furthermore, Santen is striving to create an ideal working environment by implementing occupational health and safety initiatives and supporting the health of employees.

Helping to Protect the Environment

Santen's mission is to help drive progress worldwide in medical science and pharmacology, while actively working with regional communities and in harmony with international society to conserve nature and protect the environment. To this end, environmental activities are positioned as an important initiative in all businesses and units. In 1998, Santen formulated a Basic Environmental Policy, followed by Environmental Guidelines in 2000. And through the disclosure of environmental information and voluntary activities by individual employees, Santen is contributing to environmental protection.

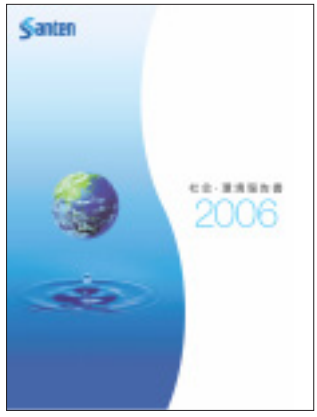
In addition to assessing the environmental impact of its business activities, Santen conserves energy, reduces waste, uses chemical substances in an appropriate manner, manages environmental impact and employs environmental accounting.

Initiatives to clean up communities

Santen also actively promotes the procurement of environmentally friendly products. Santen is currently formulating green procurement guidelines, which the company will use to raise environmental awareness not only within Santen but also at suppliers.

A Stronger Organizational Framework

To strengthen its various social and environmental activities, Santen has formed three cross-organizational bodies: the Compliance Committee, the Human Rights Education Committee and the Environmental Safety Committee. These bodies are spearheading corporate activities designed to increase Santen's value as a member of society and engender trust in the company.



Environmental Report

* Santen publishes an Environmental Report (in Japanese only) to foster a deeper understanding of its social and environmental initiatives. The same information is also available on the company's website.

Corporate Governance

Santen recognizes that it is vital to upgrade and strengthen corporate governance. Thus Santen is working to raise business performance while maintaining transparent and sound management practices through the development of effective corporate governance systems.

Governance Institutions

Board of Directors

In addition to various statutory functions, the Board of Directors formulates management policies and strategies and business plans for Santen, makes decisions relating to the acquisition or disposal of major financial assets and to important organizational or personnel-related moves, and also oversees the execution of business at Santen and its subsidiaries. The Board convenes in principle once a month. As of the end of July 2006, the Board comprised seven members, including three non-executive directors. The Board of Directors convened 11 times during the year ended March 31, 2006.

Board of Corporate Auditors

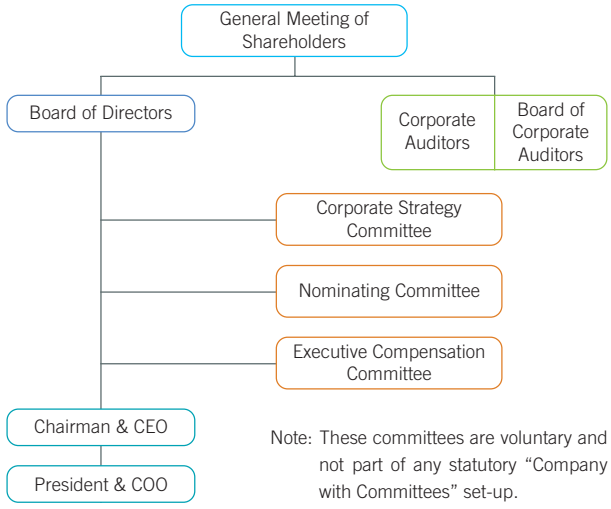
Santen has adopted a governance system using corporate auditors. This system relies on cooperation between the corporate auditors and the internal audit function to maintain high standards of auditing accuracy and efficiency.

Santen has a four-member Board of Corporate Auditors, including outside auditors. Besides formulating auditing policies and plans and attending important business meetings, notably those of the Board of Directors, the corporate auditors oversee the execution of duties by directors through audits of the operational and financial status of Santen's head office, major operating sites and subsidiaries. The Board of Corporate Auditors convened seven times during the year ended March 31, 2006.

Voluntary Committees

Santen has established three committees composed of executive and non-executive directors as deliberative bodies to strengthen corporate governance and to improve management transparency and objectivity. The Corporate Strategy Committee deliberates on key strategic issues such as business strategy. The Nominating Committee sets the criteria for the selection and appointment of directors, clarifies the decision-making process, and submits nominations to the Board of Directors based on its deliberations. The Executive Compensation Committee makes proposals for establishing and revising remuneration policies and related compensation systems for senior executives and deliberates on the setting of actual compensation. Note that these voluntary committees are of a different nature to the committees that a Japanese company would establish on adoption of the alternative "Company with Committees" system as laid down in the former Commercial Code of Japan.

Santen Internal Governance System (as of June 27, 2006)



Note: These committees are voluntary and not part of any statutory "Company with Committees" set-up.

Corporate Officer System

Santen has introduced a corporate officer system to strengthen management while improving the quality and speed of strategic decision-making processes. There were eight corporate officers at the end of July 2006, including some serving concurrently as directors.

Internal Governance System

As a company active in the pharmaceutical industry, Santen aims to maintain high ethical standards in all corporate activities undertaken by directors and employees.

Compliance

The Santen Corporate Ethics Mission, a statement of the corporate behavioral standards to which the company adheres, defines strict ethical standards governing corporate activities. The Compliance Group is in charge of coordinating internal compliance programs in cooperation with the Compliance Committee, which operates as a company-wide cross-functional group. Santen uses online programs and other types of training courses to educate its workforce on compliance-related issues on an ongoing basis.

Santen maintains an internal help line for employees to inquire about compliance-related issues. An external independent direct help line to an attorney is also available to all employees to report any suspected compliance violations or to receive advice.

Risk Management

Santen has compiled an internal risk management manual that defines basic policies in crisis management situations, based on the company's business philosophy. The manual also lists internal action standards for crisis management in emergency situations. Specific internal units are responsible for managing the major risks associated with operating activities, by gathering daily information for risk management purposes, and coordinating ongoing efforts to prevent key risk-related occurrences.

The Risk Evaluation Committee meets regularly to assess risks and to analyze any risk-related phenomena identified through internal or external information sources. This committee is also responsible for studying and overseeing the implementation of related preventative measures.

In line with internal guidelines, the occurrence of an emergency situation triggers the creation of a Crisis Response Committee headed by a representative director. Based on Santen's crisis management policies and related action standards, this Committee coordinates efforts to minimize any losses or damage and institutes measures to prevent recurrence.

Operating and Financial Controls

To maintain proper operating controls within the consolidated Santen Group, which is made up of the parent company and subsidiaries, Santen has created a system specifying in what situations subsidiaries must seek the final approval of Santen for important business transactions, based on internal approval criteria. Monthly operating and financial reporting controls are also in place.

Major overseas subsidiaries exchange information with the parent company through regular function-specific meetings as well as certain cross-functional forums. The appointment of presidents of these subsidiaries as corporate officers of Santen has built stronger links with the parent. Furthermore, formal operating and financial reports for all major overseas subsidiaries are submitted to the Board of Directors on a quarterly basis.

In November 2005, Santen established a new internal audit function as part of the Compliance Group to implement measures to verify that internal control systems work properly and efficiently. Santen is taking all necessary precautions to ensure that this function can operate on a strictly independent basis.

Santen continues to promote activities aimed at developing internal controls to boost the reliability of financial reporting. It is also engaged in actions to respond to the new system under the Securities and Exchange Law in Japan.

Cooperation Between Auditing Groups

The corporate auditors hold a meeting with the independent auditors at the start of each fiscal year to receive presentations on the financial auditing plans for the year and any key audit-related issues, and to exchange opinions. The independent auditors present audit findings to the corporate auditors at meetings twice a year, held after the interim and final results for exchanging opinions. In addition, the corporate auditors attend a meeting convened by the independent auditors after the conclusion of the year-end audit to share comments on the audit results. During the year, the corporate auditors undertake various audits of the auditing methods used by the independent auditors, such as internal audits and the witnessing of inventory checks.

The corporate auditors inform the internal audit function in the Compliance Group of any specific audit-related issues or future risk-related items that may be identified in the course of auditing Santen's head office or operating sites. The internal audit function also reports to the corporate auditors any important information gained from internal audits and related measures. As deemed necessary, the corporate auditors may provide support to the internal audit function in implementing countermeasures after receiving explanations.

Compensation for Directors and Corporate Auditors

Total remuneration for directors and corporate auditors for the year ended March 31, 2006 equaled ¥195 million.

1. Compensation paid to directors	¥145 million
2. Compensation paid to corporate auditors	¥ 49 million
3. Employee salary (including bonuses) paid to directors for the work undertaken in employee capacities	¥ 36 million
4. Executive bonuses paid out of the previous fiscal year's retained earnings	¥ 24 million

Executives have been granted subscription rights equivalent to 120,000 shares under a stock option scheme governed by the terms of Article 280-19 of the former Commercial Code and a total of 2,793 stock acquisition rights under a stock option scheme governed by the terms of Articles 280-20 and 280-21 of the former Commercial Code that was revised in 2001. Of these total figures, the portions that had already been exercised as of March 31, 2006 corresponded to 21,000 shares and 419 acquisition rights, respectively.

Board of Directors, Corporate Auditors and Corporate Officers

As of July 2006

BACK ROW FROM LEFT: Katsuhiro Waga, Kosei Furukawa, Isao Muramatsu, Noboru Kotani, Masahiro Mita
FRONT ROW FROM LEFT: Akira Kurokawa, Takakazu Morita

Board of Directors

Takakazu Morita
Chairman and Chief Executive Officer

Akira Kurokawa
President and Chief Operating Officer

Masahiro Mita, M.D., Ph.D.
Managing Director
Corporate and Regulatory Affairs

Katsuhiro Waga
Member of the Board
Community & Environment Relations

Kosei Furukawa*
Member of the Board

Isao Muramatsu*
Member of the Board

Noboru Kotani*
Member of the Board

Corporate Auditors

Shushi Sakamoto
Standing Corporate Auditor

Yukinori Mizumoto
Standing Corporate Auditor

Tadao Kagono**
Corporate Auditor

Yasuo Sato**
Corporate Auditor

* Outside Director
** External Corporate Auditor

Adrienne Graves

Jyrki Liljeroos

BACK ROW FROM LEFT: Yoshihiro Noutsuka, Kenji Morishima, Sadatoshi Furukado, Masamichi Sato
FRONT ROW FROM LEFT: Kenji Iwamoto, Toshiaki Nishihata

Corporate Officers

Toshiaki Nishihata, Ph.D.
Senior Corporate Officer
Head of Research and Development Division

Kenji Iwamoto
Corporate Officer
Head of Asia Division

Masamichi Sato
Corporate Officer
Strategic HR/OTC Business

Adrienne Graves, Ph.D.
Corporate Officer
President of Santen Inc.

Jyrki Liljeroos
Corporate Officer
President of Santen Oy

Sadatoshi Furukado
Corporate Officer
Sales & Marketing Division, Prescription Pharmaceuticals

Kenji Morishima
Corporate Officer
Head of Product Supply Division

Yoshihiro Noutsuka
Corporate Officer
Head of Planning & Control Division

Financial Review

Contents

Note: Figures have been rounded to the nearest unit.

Financial Review

Operating Results

Net Sales

Santen Group's consolidated sales for the year ended March 31, 2006 increased by ¥5,702 million, or 6.2%, from the previous year to ¥98,398 million. Sales of mainstay prescription pharmaceuticals increased by ¥5,953 million, or 7.1%, from the previous year to ¥90,251 million. Prescription pharmaceuticals accounted for 91.7% of total sales, a rise of 0.8 percentage points from the previous year's figure of 90.9%.

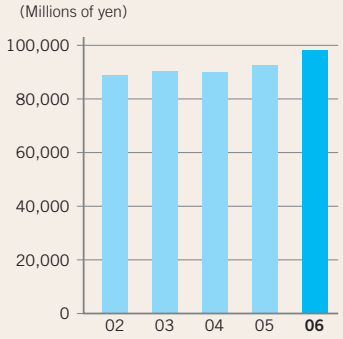
Prescription pharmaceutical sales can be broken down into ophthalmics, anti-rheumatics, and other pharmaceuticals. Domestic sales of prescription ophthalmic pharmaceuticals increased by ¥2,832 million, or 4.1%, from the previous year to ¥71,215 million. This was the result of further market penetration by Santen products amid market expansion, mainly for glaucoma and corneal disorder treatments. Overseas sales of prescription ophthalmics rose by ¥2,465 million, or 34.0%, to ¥9,706 million, due to steady sales growth in Northern and Eastern Europe, Russia and Asia and the absence of trade inventory adjustments in the U.S. the previous year. Sales of anti-rheumatic pharmaceuticals for the year increased by ¥688 million, or 8.2%, from the previous year to ¥9,041 million, reflecting growth in sales of *Rimatil*, *Azulfidine*, and *Metolate*. Sales of other pharmaceuticals fell by ¥32 million, or 10.0%, from the previous year to ¥288 million.

Sales of over-the-counter (OTC) pharmaceuticals declined by ¥29 million, or 0.5%, to ¥5,248 million, despite a continued focus on sales promotion of ophthalmics for tired eyes and blurred vision.

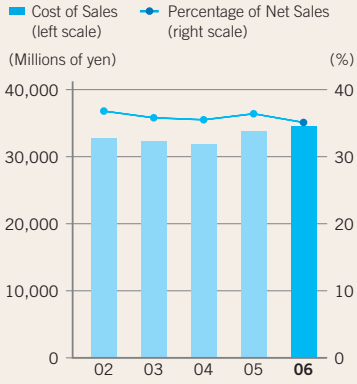
Sales of medical devices decreased by ¥116 million, or 15.4%, from the previous year to ¥639 million. The number of cataract procedures rose slightly in Japan, but sales of intraocular lenses trended flat due to increased competition. Sales were also affected by the discontinuation of sales of surgical instruments as of December 31, 2004.

Sales in the other business segment fell by ¥106 million, or 4.5%, to ¥2,260 million, attributable to the decline in contract manufacturing sales in the United States and Europe.

Net Sales



Cost of Sales and Percentage of Net Sales



Net Sales by Business Segment

(Millions of yen)

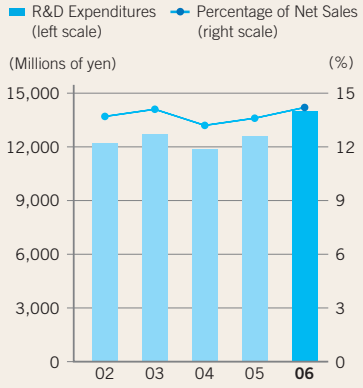
Years ended March 31	2006	2005	Change (%)
Prescription Pharmaceuticals	¥90,251	¥84,298	7.1%
Ophthalmics	80,922	75,625	7.0
Anti-rheumatics	9,041	8,353	8.2
Others	288	320	(10.0)
OTC Pharmaceuticals	5,248	5,277	(0.5)
Medical Devices	639	755	(15.4)
Other Business	2,260	2,366	(4.5)
Total Sales	98,398	92,696	6.2

Note: Figures in parentheses indicate a decrease.

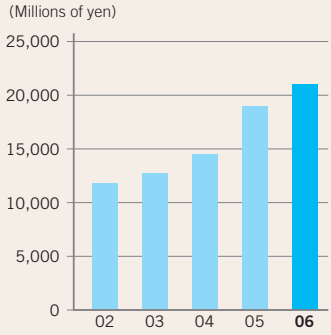
Cost of Sales

Cost of sales for the year grew by ¥825 million, or 2.4%, from the previous year to ¥34,535 million. The ratio of cost of sales to net sales fell by 1.3 percentage points to 35.1% from 36.4%, due to changes in the product mix—such as increased sales of *Hyalein*—as well as a higher operating ratio due to increased production volumes, and cost reductions.

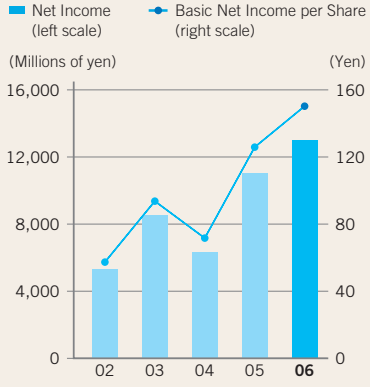
R&D Expenditures and Percentage of Net Sales



Operating Income



Net Income and Basic Net Income per Share



Selling, General and Administrative Expenses

Selling, general and administrative (SG&A) expenses for the year increased by ¥2,864 million, or 7.2%, from the previous year to ¥42,868 million. Selling expenses rose by some ¥800 million in Japan, ¥200 million in Europe, and ¥300 million in Asia, due to active efforts to disseminate medical information and defensive strategies against the competition. Moreover, R&D expenditures amounted to ¥13,971 million due to increased investment in the fields of glaucoma, corneal disorders, and retinal disorders.

Operating Income

Operating income for the year advanced by ¥2,013 million, or 10.6%, from the previous year to ¥20,995 million. The increase in SG&A expenses was offset by growing sales of prescription pharmaceuticals and a lower ratio of cost of sales to net sales. As a result, the ratio of operating income to net sales improved by 0.8 percentage points to 21.3% from 20.5% in the previous year.

Other Income and Expenses

Net other expenses for the year totaled ¥653 million.

Other income totaled ¥1,077 million, decreasing due to the absence of the gains recorded the previous year from the transition to the new retirement benefit program and the establishment of a retirement benefit trust, as well as almost no gains on the sale of fixed assets in the year under review.

Other expenses amounted to ¥1,730 million, decreasing due to the absence of costs from structural improvements at the U.S. business. On the other hand, Santen recorded impairment losses on land and property used in logistics operations accompanying the outsourcing of our logistics operations, and a special retirement premium for staff at Santen Distribution Co., Ltd.

Income Taxes

Income taxes for the year decreased slightly to ¥7,319 million compared with the previous year. The effective tax rate declined to 36.0%, from 40.2% in the previous year, as a result of improved profit at our overseas subsidiaries and the effect of a preferential tax system for domestic research spending.

Net Income

Net income expanded by ¥2,000 million, or 18.1%, from the previous year to ¥13,023 million. The ratio of net income to net sales improved by 1.3 percentage points to 13.2% from 11.9% in the previous year, primarily due to increased income reflecting growth in net sales and a reduction in the cost percentage. Basic net income per share rose by ¥24.41 to ¥150.26 from ¥125.85 in the previous year, and diluted net income per share rose by ¥24.3 to ¥150.01 from ¥125.71.

Net Income per Share, Dividend and ROE

(Yen)

Years ended March 31	2006	2005	2004
Net Income per Share — basic	¥150.26	¥125.85	¥71.65
Net Income per Share — diluted	150.01	125.71	71.64
Dividend	60.00	50.00	40.00
ROE (%)	11.5	10.4	6.3

Financial Condition

Assets

As of March 31, 2006, total assets were ¥150,458 million, up ¥10,478 million, or 7.5%, from the previous year-end. Current assets increased by ¥11,158 million, or 13.5%, to ¥93,893 million, reflecting an increase in cash and cash equivalents due to an increase in income before income taxes. The ratio of current assets to total assets rose by 3.3 percentage points to 62.4%, from 59.1% in the previous year. Net property, plant and equipment at year-end decreased by ¥2,281 million, or 7.0%, to ¥30,395 million, due to decreases in property, plant and equipment caused by depreciation and impairment losses on real estate used for logistics operations. In investments and other assets, there was an increase in investment securities due to a rise in the value of marketable securities. Return on assets (ROA) for the year improved by 1.4 percentage points to 9.0%, from 7.6% in the previous year.

Liabilities

Total liabilities amounted to ¥31,821 million, an increase of ¥81 million, or 0.3%, from the previous year-end. Current liabilities rose by ¥1,889 million, or 8.5%, to ¥24,111 million. This was primarily due to an increase of ¥1,532 million, or 44.9%, in income taxes payable compared to the previous fiscal year-end.

Noncurrent liabilities decreased by ¥1,808 million, or 19.0%, from the previous year-end to ¥7,710 million. The main factor was a decrease of ¥1,168 million in long-term debt. Interest-bearing debt declined by ¥1,268 million, or 18.4%, from the previous year to ¥5,614 million, reflecting the early repayment of long-term debt and other factors.

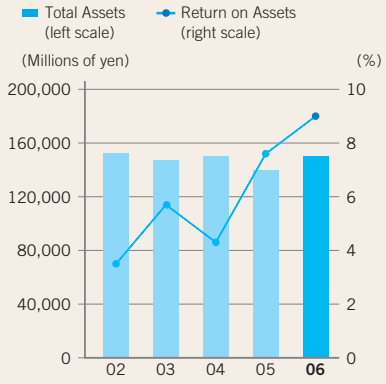
Shareholders' Equity

Shareholders' equity increased by ¥10,397 million, or 9.6%, from the previous year-end to ¥118,637 million. This was due to an increase in retained earnings reflecting growth in net income, as well as an increase in the value of other marketable securities. The shareholders' equity ratio improved by 1.6 percentage points to 78.9% from 77.3%, due to total liabilities trending flat. Return on equity (ROE) rose by 1.1 percentage points to 11.5% from 10.4%, mainly due to an increase in net income. Shareholders' equity per share at year-end increased by ¥118.95, or 9.5%, from the previous year-end to ¥1,368.27.

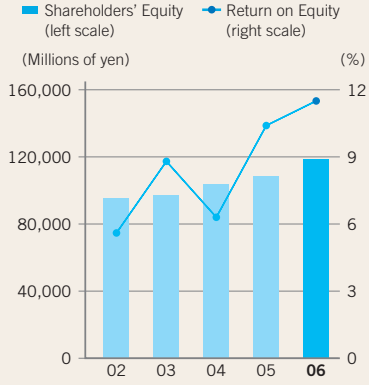
Capital and Liquidity

Santen Pharmaceutical is striving to maintain a healthy balance sheet and ensure the Company has appropriate liquidity and the necessary funds for its business activities. Net working capital—defined as the difference between current assets and current liabilities—increased by ¥9,269 million, or 15.3%, from the previous year-end to ¥69,782 million, while the current ratio improved by 17 percentage points to 389% from 372% at the previous year-end. Cash and cash equivalents at year-end increased by ¥13,724 million, or 42.4%, from the previous year-end to ¥46,105 million. Cash generated by operating activities totaled ¥20,879 million, of which ¥1,330 million was used for investing activities and ¥5,900 million for financing activities.

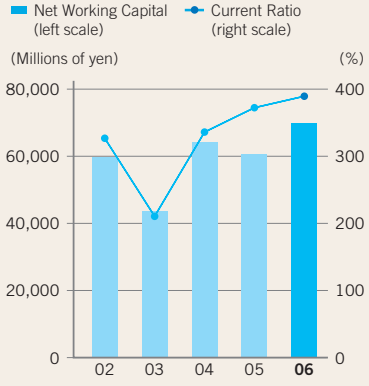
Total Assets and Return on Assets



Shareholders' Equity and Return on Equity



Net Working Capital and Current Ratio



Note: Net working capital is the difference between current assets and current liabilities, and reflects a company's ability to make payments in the short term.

Cash Flows

Cash Flows Summary

(Millions of yen)

Years ended March 31	2006	2005	Change
Cash Flows From Operating Activities	¥20,879	¥ 6,619	¥14,260
Cash Flows From Investing Activities	(1,330)	(2,907)	1,577
Cash Flows From Financing Activities	(5,900)	(12,712)	6,812
Cash and Cash Equivalents at End of Year	46,105	32,381	13,724

Note: Figures in parentheses indicate a decrease.

Cash Flows From Operating Activities

Net cash provided by operating activities increased by ¥14,260 million, or 315%, from the previous year to ¥20,879 million. This was due to a ¥1,906 million increase in income before income taxes, a ¥1,407 million decrease in trade receivable, and a significant decrease of ¥6,507 million in corporate tax payments.

Cash Flows From Investing Activities

Net cash used in investing activities decreased by ¥1,577 million to ¥1,330 million, compared with ¥2,907 million the previous year. This was due to reduced payments on the acquisition of property, plant and equipment and on the acquisition of investment securities.

Cash Flows From Financing Activities

Net cash used in financing activities decreased by ¥6,812 million, or 53.6%, to ¥5,900 million. Despite the increase in the dividend payment, expenditure decreased because of the absence of the early partial repayment of syndicated loans in the previous year and the reduced expenditure on the repurchase of treasury stock.

Risks Related to Our Business

Forward-looking Information and Factors That May Affect Future Results

Oral and written statements that we make in our annual report and through other public vehicles, other than historical facts, contain forward-looking information based on our business plans and assumptions at the time of disclosure. Such forward-looking information includes, but is not limited to, our expected growth strategies, projected operating results, market forecasts and anticipated timing for developing, obtaining approval and bringing products to market. These forward-looking statements represent our best estimates based on our awareness of market conditions and may differ substantially from actual results. Our business, as well as each product we develop and market, is subject to various risks and uncertainties beyond our control.

Risks and uncertainties that could affect the Company's future results and financial conditions include, but are not limited to, the factors described below.

External Factors

Regulatory Controls

We conduct business under government regulatory controls for healthcare programs and drug prices in Japan and other countries, and therefore future results could be affected by changes in any of these regulations. Our financial performance, in particular, relies heavily on Japan's prescription pharmaceuticals market, which represents 80% of our consolidated net sales. Biennial National Health Insurance (NHI) drug price revisions or other healthcare reforms that may take place beyond the scope of our anticipated projections may also affect our operating and/or financial results. In April 2006, NHI drug price revisions went into effect resulting in an average 6.7% reduction for the prescription ophthalmic pharmaceuticals industry, which translated into an average 5.3% reduction for our total prescription pharmaceuticals sales.

We continue to face a variety of regulatory controls and government pressures for drug price reduction in other countries and markets where we manufacture and sell our products.

Social and Economic Conditions and Changes in the Law

Santen's future results may be affected by political and economic changes in worldwide markets where we operate. Our anticipated performance and financial conditions may also be affected by changes in applicable accounting principles, and laws and regulations concerning taxes, product liability, antitrust, environmental controls and other factors.

Foreign Exchange

Overseas sales and expenses, as well as assets of overseas subsidiaries, affect our sales, profits and financial conditions depending on foreign exchange fluctuations. Overseas sales for the year ended March 31, 2006 accounted for 11.8% of our consolidated net sales.

Competition

Effects of Generic Pharmaceuticals

Sales of generic pharmaceuticals in Japan and abroad may affect Santen's overall business results.

While our mainstay products—including *Cravit*, *Rescula* and *Livostin*—are protected by patents, generic pharmaceuticals for products such as *Hyalein* and *Tarivid* have already been introduced into the Japanese market by other companies. Market analysis leads us to expect that generic competition will increase.

Competition From Other Branded Products

We have noted the launch of new branded products in the anti-infective market in Japan and overseas, and expect this trend to continue in the near future. These new products directly compete with our *Cravit* and *Quixin* products and may affect future performance.

Dependency on Specific Products and Business Partners

Dependency on Mainstay Products

Hyalein and *Cravit* each generate annual sales of over ¥10 billion, together representing 30% of Santen's consolidated net sales for the year ended March 31, 2006. Sales of these products are critical to our ongoing success, and any unanticipated negative influences, such as patent expiration and complications, potential product defects or newly discovered side effects, could affect our financial performance significantly.

Dependency on In-licensed Products

Many of the products we sell are in-licensed from other companies. We hold exclusive rights to manufacture and sell ophthalmic formulations of *Cravit* and *Detantol*. We also have sales rights in Japan for *Timoptol*, *Timoptol XE* and *Livostin* and exclusive sales rights for *Azulfidine EN* and *Rescula*. Should changes be made in the terms and conditions of these agreements or should the agreements not be renewed, our financial results may be affected.

Dependency on Specific Business Partners

As of February 16, 2004, we entered into an exclusive distribution agreement with Johnson & Johnson Vision Care, Inc. (JJVCI) in the U.S. In the event that JJVCI cannot achieve sufficient sales per our agreement, our financial results may be affected.

Some raw and processed materials, such as bulk pharmaceuticals for *Cravit* and containers for over-the-counter (OTC) pharmaceuticals, are dependent on specific business partners. If supply of these materials is interrupted or discontinued for any reason, our pharmaceutical production and financial performance may be adversely affected.

The percentage of our business executed with the top 10 wholesalers in Japan reached 70% of our consolidated net sales. If our wholesale partners experience bankruptcy leading to lending loss, we may be adversely affected.

Research and Development Activities

Uncertainty in New Product Development

Years are required to bring new drugs from initial research and development to final approval and marketing. Factors exist at every stage along the way that can sidetrack a new product and either delay or prevent it from reaching the marketplace. It is difficult for us to accurately predict when new products, indications, or formulations under development will reach the approval stage and be ready for launching.

Forecasting a precise timeline for project development and completion depends on a number of variable factors, including, but not limited to, delayed government reviews, conflicting or unusable clinical data, safety and efficacy concerns, unexpected side effects, discontinued development, and delayed product launches, negatively affecting projected sales of new drugs.

Potentially Insufficient Returns on R&D Investment

The creation and development of new pharmaceuticals, as well as the development of new indications and formulations, are critical for the future growth of Santen. Every year, we invest significantly in research and development, and there is a possibility future investments will not result in sufficient sales of new products.

Issues of Alliances

Forecasts for new pharmaceuticals include various assumptions of alliances in development and/or sales. Actual determination of these alliances may affect our overall results and financial conditions.

Other Factors

Production Interruptions or Delays

The interruption or delay of production activities due to natural disasters or other catastrophes such as fire, may affect our financial performance and conditions. Certain products are only manufactured at one location. If a specific plant is forced to stop production, supply of some products may be negatively affected.

Cancellation of Sales and Product Withdrawals

If sales of products are cancelled, or if we withdraw products due to a batch defect, unexpected side effects, tampering or other causes, our overall financial results may be negatively affected.

Litigation

Our main business involves production and sales of prescription pharmaceuticals. The nature of our business makes us vulnerable to litigation related to patents, product liability, violation of antitrust law, consumer-related issues, and environmental concerns. If such legal actions take place, the proceedings may affect our overall performance and financial conditions. Currently, we are involved in no litigation that substantially impacts the management or performance of our company.

Ten-year Summary of Selected Financial Data

Years ended March 31

	2006	2005	2004	2003
For the year:				
Net sales	¥ 98,398	¥ 92,696	¥ 89,858	¥ 90,253
Cost of sales	34,535	33,710	31,859	32,272
Selling, general and administrative expenses	42,868	40,004	43,475	45,284
Operating income	20,995	18,982	14,524	12,697
Interest expense	94	182	366	480
Income before income taxes	20,342	18,436	13,775	9,947
Income taxes	7,319	7,413	7,454	1,444
Net income	13,023	11,023	6,321	8,503
Capital expenditures	2,106	4,907	3,226	7,046
Depreciation and amortization	4,824	4,750	4,521	4,311
R&D expenditures	13,971	12,620	11,853	12,719
Per share data (yen and U.S. dollars)**:**				
Net income — basic	¥ 150.26	¥ 125.85	¥ 71.65	¥ 93.67
Net income — diluted	150.01	125.71	71.64	85.97
Shareholders' equity (BPS)	1,368.27	1,249.32	1,176.83	1,104.21
Cash dividends, applicable to period	60.00	50.00	40.00	20.00
Cash Flows:				
Net cash provided by operating activities	¥ 20,879	¥ 6,619	¥ 23,196	¥ 15,808
Net cash (used in) provided by investing activities	(1,330)	(2,907)	5,246	(9,951)
Net cash (used in) provided by financing activities	(5,900)	(12,712)	(12,122)	(6,507)
Interest coverage ratio (times)	218.7	36.1	70.6	34.5
Debt amortization period (years)	0.2	1.0	0.5	1.5
At year-end:				
Current assets	¥ 93,893	¥ 82,735	¥ 91,231	¥ 83,431
Net property, plant and equipment	30,395	32,676	37,237	40,850
Total assets	150,458	139,980	150,238	147,148
Long-term debt	5,614	6,882	12,686	23,047
Total shareholders' equity	118,637	108,240	103,500	97,126
Return on equity (ROE) (%)	11.5	10.4	6.3	8.8
Return on total assets (ROA) (%)	9.0	7.6	4.3	5.7
Shareholders' equity ratio (%)	78.9	77.3	68.9	66.0
Shareholders' equity ratio on stock price basis (%)	163.0	142.3	101.8	68.7
Price earnings ratio (PER) (times)	18.8	18.3	24.3	12.3
Issued shares (thousands)	86,751	86,659	87,963	90,704
Number of employees	2,312	2,308	2,335	2,500

Notes: 1. U.S. dollar amounts have been translated from yen, solely for the convenience of the reader, at the rate of ¥117.47 to U.S.$1 prevailing on March 31, 2006.
2. See Notes 2. 14) and 11 of Notes to Consolidated Financial Statements in respect of per share data.
3. Net sales in the six years ended March 31, 2006 to 2001 include royalty income which was presented as "Other, net" in "Other income (expenses)" through the fiscal year ended March 31, 2000.

Millions of yen						Thousands of U.S. dollars
2002	2001	2000	1999	1998	1997	**2006**
¥ 88,966	¥ 88,449	¥ 83,577	¥ 79,639	¥ 77,957	¥ 75,216	**$ 837,643**
32,701	33,385	32,195	32,746	31,278	27,552	**293,986**
44,475	38,546	33,894	30,294	30,535	27,984	**364,932**
11,790	16,518	17,488	16,599	16,144	19,680	**178,725**
465	430	462	588	654	624	**796**
12,679	15,521	14,422	15,969	14,917	18,913	**173,164**
7,373	7,807	6,481	7,864	7,594	9,915	**62,309**
5,306	7,714	7,941	8,105	7,323	8,998	**110,855**
6,586	4,943	2,510	3,443	5,898	16,725	**17,931**
5,334	5,683	5,725	6,314	6,674	4,202	**41,073**
12,187	10,511	9,221	7,335	7,731	6,213	**118,935**
¥ 57.34	¥ 81.32	¥ 83.54	¥ 85.27	¥ 77.06	¥ 105.32	**$ 1.28**
53.07	75.01	77.04	78.63	71.01	99.87	**1.28**
1,048.51	1,022.99	1,006.48	935.71	862.88	877.12	**11.65**
20.00	20.00	12.00	12.00	12.00	12.00	**0.51**
¥ 6,941	¥ 6,832	¥ 9,372	¥ 16,339	¥ 11,535	¥ 16,181	**$ 177,737**
(6,374)	(3,172)	837	(8,305)	(9,537)	(28,259)	**(11,322)**
(5,684)	(7,193)	(3,817)	(3,857)	(1,677)	18,610	**(50,227)**
14.9	16.8	20.3	27.8	21.6	32.8	**—**
3.5	3.7	2.7	1.7	2.7	2.0	**—**
¥ 86,064	¥ 88,025	¥ 82,218	¥ 78,018	¥ 70,892	¥ 69,065	**$ 799,290**
42,159	36,684	37,416	39,638	43,425	47,278	**258,755**
152,103	153,243	149,968	144,913	138,822	140,226	**1,280,824**
24,467	25,482	26,491	27,496	31,168	31,807	**47,791**
95,101	94,834	95,669	88,950	81,998	75,759	**1,009,938**
5.6	8.1	8.6	9.5	9.3	11.9	
3.5	5.1	5.4	5.7	5.2	6.4	
62.5	61.9	63.8	61.4	59.1	54.0	
86.6	134.3	139.4	145.0	106.1	131.8	
25.3	27.3	26.3	25.9	20.1	21.6	
90,704	92,721	95,075	95,075	95,075	86,410	
2,463	2,167	2,093	2,037	2,010	1,910	

Consolidated Balance Sheets

Santen Pharmaceutical Co., Ltd. and Subsidiaries
As of March 31, 2006 and 2005

	Millions of yen		Thousands of U.S. dollars (Note 3)
ASSETS	**2006**	2005	**2006**
Current assets:			
Cash and cash equivalents (Note 4)	**¥ 46,105**	¥ 32,381	**$ 392,481**
Short-term investments (Note 4)	**180**	914	**1,533**
Trade receivables:			
Notes	**309**	398	**2,632**
Accounts	**34,115**	35,227	**290,407**
Less allowance for doubtful receivables	**(1)**	(18)	**(6)**
Net trade receivables	**34,423**	35,607	**293,033**
Inventories (Note 6)	**9,838**	9,827	**83,747**
Deferred tax assets (Note 14)	**1,651**	1,625	**14,060**
Other current assets	**1,696**	2,381	**14,436**
Total current assets	**93,893**	82,735	**799,290**
Property, plant and equipment (Notes 7 and 8)**:**			
Land	**9,064**	9,487	**77,159**
Buildings and structures	**40,289**	40,257	**342,976**
Machinery and equipment	**10,982**	11,036	**93,491**
Tools, furniture and vehicles	**10,452**	10,609	**88,977**
Construction in progress	**275**	182	**2,338**
Total	**71,062**	71,571	**604,941**
Less accumulated depreciation	**(40,667)**	(38,895)	**(346,186)**
Net property, plant and equipment	**30,395**	32,676	**258,755**
Investments and other assets:			
Investment securities (Note 4)	**17,716**	14,314	**150,811**
Goodwill	**709**	1,015	**6,039**
Other intangibles	**2,242**	2,303	**19,083**
Deferred tax assets (Note 14)	**380**	1,052	**3,231**
Other assets	**5,123**	5,885	**43,615**
Total investments and other assets	**26,170**	24,569	**222,779**
Total assets	**¥150,458**	¥139,980	**$1,280,824**

See accompanying notes to consolidated financial statements.

LIABILITIES AND SHAREHOLDERS' EQUITY	Millions of yen 2006	Millions of yen 2005	Thousands of U.S. dollars (Note 3) 2006
Current liabilities:			
Current portion of long-term debt (Note 9)	¥ 168	¥ 268	$ 1,430
Trade accounts payable	5,631	6,123	47,934
Other payables	9,308	8,578	79,239
Accrued expenses	3,417	3,214	29,087
Income taxes payable (Note 14)	4,946	3,414	42,107
Other current liabilities	641	625	5,454
Total current liabilities	24,111	22,222	205,251
Noncurrent liabilities:			
Long-term debt (Note 9)	5,446	6,614	46,361
Retirement and severance benefits (Note 10)	1,707	1,858	14,529
Deferred tax liabilities (Note 14)	20	23	172
Other liabilities	537	1,023	4,573
Total noncurrent liabilities	7,710	9,518	65,635
Shareholders' equity:			
Common stock (Notes 11 and 12):			
Authorized — 151,493,354 shares (151,493,354 shares in 2005)			
Issued — 86,751,203 shares (86,658,703 shares in 2005)	6,319	6,248	53,795
Additional paid-in capital (Notes 11 and 12)	7,014	6,943	59,710
Retained earnings (Note 11)	104,134	95,902	886,472
Unrealized holding gains on securities (Notes 4 and 11)	3,996	2,049	34,016
Foreign currency translation adjustments	(2,736)	(2,827)	(23,288)
	118,727	108,315	1,010,705
Treasury stock at cost (Note 11):			
45,090 shares in 2006 and 39,660 shares in 2005	(90)	(75)	(767)
Total shareholders' equity	118,637	108,240	1,009,938
Contingent liabilities (Note 15)			
Total liabilities and shareholders' equity	¥150,458	¥139,980	$1,280,824

Consolidated Statements of Income

Santen Pharmaceutical Co., Ltd. and Subsidiaries
For the years ended March 31, 2006, 2005 and 2004

	Millions of yen			Thousands of U.S. dollars (Note 3)
	2006	2005	2004	**2006**
Net sales	**¥98,398**	¥92,696	¥89,858	**$837,643**
Cost of sales	**34,535**	33,710	31,859	**293,986**
Gross profit	**63,863**	58,986	57,999	**543,657**
Selling, general and administrative expenses	**42,868**	40,004	43,475	**364,932**
Operating income	**20,995**	18,982	14,524	**178,725**
Other income (expenses):				
Interest and dividend income	**262**	249	240	**2,228**
Gain on insurance received	**74**	114	1,712	**634**
Dividends received from investment limited partnership	**136**	—	—	**1,156**
Interest expense	**(94)**	(182)	(366)	**(796)**
Gain on sale of investment securities	**0**	1	675	**0**
Gain on sale of fixed assets	**3**	341	5	**27**
Net gain on the change of the retirement benefits program (Note 10)	**—**	316	—	**—**
Gain on marketable securities contributed to employees' retirement benefit trust (Note 10)	**—**	211	—	**—**
Loss on impairment of fixed assets (Note 8)	**(909)**	(823)	(377)	**(7,745)**
Loss on valuation of investment securities	**—**	(51)	(201)	**—**
Retirement benefit under the carrier development support program	**—**	—	(719)	**—**
Restructuring charge for the logistics operations	**(149)**	—	—	**(1,267)**
Loss on discontinued operations of affiliates	**—**	—	(855)	**—**
Restructuring charge for the U.S. business	**—**	(441)	(386)	**—**
Other, net	**24**	(281)	(477)	**202**
Income before income taxes	**20,342**	18,436	13,775	**173,164**
Income taxes (Note 14):				
Current	**7,999**	6,447	8,751	**68,095**
Deferred	**(680)**	966	(1,297)	**(5,786)**
	7,319	7,413	7,454	**62,309**
Net income	**¥13,023**	¥11,023	¥ 6,321	**$110,855**

	Yen			U.S. dollars (Note 3)
	2006	2005	2004	**2006**
Per share data:				
Net income — basic	**¥150.26**	¥125.85	¥ 71.65	**$ 1.28**
Net income — diluted	**150.01**	125.71	71.64	**1.28**
Cash dividends, applicable to the period	**60.00**	50.00	40.00	**0.51**

See accompanying notes to consolidated financial statements.

Consolidated Statements of Shareholders' Equity

Santen Pharmaceutical Co., Ltd. and Subsidiaries
For the years ended March 31, 2006, 2005 and 2004

	Millions of yen			Thousands of U.S. dollars (Note 3)
	2006	2005	2004	2006
Common stock (Notes 11 and 12):				
Balance at beginning of year	¥ 6,248	¥ 6,214	¥ 6,214	$ 53,187
Exercise of stock options	71	34	—	608
Balance at end of year	¥ 6,319	¥ 6,248	¥ 6,214	$ 53,795
Additional paid-in capital (Notes 11 and 12):				
Balance at beginning of year	¥ 6,943	¥ 6,909	¥ 6,909	$ 59,101
Exercise of stock options	71	34	—	609
Balance at end of year	¥ 7,014	¥ 6,943	¥ 6,909	$ 59,710
Retained earnings (Note 11):				
Balance at beginning of year	¥ 95,902	¥91,845	¥90,552	$816,393
Net income	13,023	11,023	6,321	110,855
Cash dividends paid	(4,766)	(4,397)	(1,758)	(40,563)
Bonuses to directors and corporate auditors	(25)	(21)	(30)	(213)
Retirement of treasury stock	—	(2,548)	(3,240)	—
Balance at end of year	¥104,134	¥95,902	¥91,845	$886,472
Unrealized holding gains on securities (Notes 4 and 11):				
Balance at beginning of year	¥ 2,049	¥ 1,426	¥ 294	$ 17,442
Net change	1,947	623	1,132	16,574
Balance at end of year	¥ 3,996	¥ 2,049	¥ 1,426	$ 34,016
Foreign currency translation adjustments:				
Balance at beginning of year	¥ (2,827)	¥ (2,854)	¥ (3,566)	$ (24,062)
Net change	91	27	712	774
Balance at end of year	¥ (2,736)	¥ (2,827)	¥ (2,854)	$ (23,288)
Treasury stock at cost:				
Balance at beginning of year	¥ (75)	¥ (40)	¥ (3,277)	$ (635)
Repurchase of treasury stock, net	(15)	(2,583)	(3)	(132)
Retirement of treasury stock	—	2,548	3,240	—
Balance at end of year	¥ (90)	¥ (75)	¥ (40)	$ (767)

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

Santen Pharmaceutical Co., Ltd. and Subsidiaries
For the years ended March 31, 2006, 2005 and 2004

	Millions of yen			Thousands of U.S. dollars (Note 3)
	2006	2005	2004	2006
Cash flows from operating activities:				
Income before income taxes	¥20,342	¥18,436	¥13,775	$173,164
Depreciation and amortization	4,824	4,750	4,521	41,073
Loss on impairment of fixed assets (Note 8)	909	823	377	7,745
(Decrease) increase in retirement and severance benefits	(212)	(2,551)	43	(1,807)
Interest and dividend income	(262)	(249)	(240)	(2,228)
Gain on insurance received	(74)	(114)	(1,712)	(634)
Interest expense	94	182	366	796
Decrease (increase) in trade receivables	1,407	(3,082)	(315)	11,979
(Increase) decrease in inventories	(18)	595	1,342	(154)
(Decrease) increase in trade accounts payable	(495)	1,066	(441)	(4,217)
Other, net	571	(2,263)	1,046	4,860
Subtotal	27,086	17,593	18,762	230,577
Interest and dividend income received	266	247	233	2,264
Interest expense paid	(95)	(183)	(329)	(813)
Insurance received	129	198	3,003	1,102
Income taxes paid	(6,507)	(11,236)	(453)	(55,393)
Income taxes refunded	—	—	1,980	—
Net cash provided by operating activities	20,879	6,619	23,196	177,737
Cash flows from investing activities:				
Capital expenditures	(2,106)	(4,907)	(3,226)	(17,931)
Purchase of investment securities	(58)	(3,230)	(511)	(490)
Proceeds from sale of investment securities	20	1,059	1,074	172
Proceeds from sale of property, plant and equipment	29	2,488	3,770	249
Purchase of short-term investments	(804)	(6,048)	(7,022)	(6,844)
Proceeds from sale of short-term investments	1,547	7,722	11,520	13,169
Other, net	42	9	(359)	353
Net cash (used in) provided by investing activities	(1,330)	(2,907)	5,246	(11,322)
Cash flows from financing activities:				
Proceeds from long-term debt	—	—	10,000	—
Repayment of long-term debt	(1,268)	(5,804)	(416)	(10,794)
Redemption of convertible bonds	—	—	(19,945)	—
Repurchase of treasury stock, net (Note 11)	(15)	(2,583)	(3)	(131)
Dividends paid	(4,760)	(4,393)	(1,758)	(40,518)
Other, net	143	68	—	1,216
Net cash used in financing activities	(5,900)	(12,712)	(12,122)	(50,227)
Effect of exchange rate changes on cash and cash equivalents	75	(42)	49	642
Net increase (decrease) in cash and cash equivalents	13,724	(9,042)	16,369	116,830
Cash and cash equivalents at beginning of year	32,381	41,423	25,054	275,651
Cash and cash equivalents at end of year	¥46,105	¥32,381	¥41,423	$392,481

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Santen Pharmaceutical Co., Ltd. and Subsidiaries

1 Basis of Presentation of Consolidated Financial Statements

The accompanying consolidated financial statements have been prepared in accordance with the provisions set forth in the Japanese Securities and Exchange Law and its related accounting regulations, and in conformity with accounting principles generally accepted in Japan ("Japanese GAAP"), which are different in certain respects as to application and disclosure requirements of International Financial Reporting Standards.

The accounts of overseas subsidiaries are based on their accounting records maintained in conformity with generally accepted accounting principles prevailing in the respective countries of domicile. The accompanying consolidated financial statements have been restructured and translated into English (with some expanded descriptions and the inclusion of consolidated statements of shareholders' equity) from the consolidated financial statements of Santen Pharmaceutical Co., Ltd. (the "Company") prepared in accordance with Japanese GAAP and filed with the appropriate Local Finance Bureau of the Ministry of Finance as required by the Securities and Exchange Law. Some supplementary information included in the statutory Japanese language consolidated financial statements, but not required for fair presentation, is not presented in the accompanying consolidated financial statements.

2 Summary of Significant Accounting Policies

1) Principles of consolidation

The accompanying consolidated financial statements include the accounts of the Company and its subsidiaries (the "Companies"). All significant intercompany balances and transactions are eliminated on consolidation.

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

2) 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. Actual results could differ from those estimates.

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

The Company and all domestic subsidiaries have adopted "Accounting Standard for Financial Instruments" which was issued by the Business Accounting Council in Japan. In accordance with this 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.

Those classified as other securities with an available market value are reported at fair value with unrealized holding gains, net of related taxes reported in equity. Realized gains and losses on sales of such securities are determined by the moving average cost method. Other securities with no available market value are carried at cost, which is determined by the moving average cost method.

In addition, this standard also requires the recognition of an impairment loss on golf membership rights, included in other assets, on the consolidated balance sheets, when the market value shows a substantial decline and does not appear to be recoverable.

4) Derivative instruments (see Note 5)

Derivative instruments are stated at fair value, and accounted for using deferred hedge accounting. Deferred hedge accounting requires unrealized gains or losses to be deferred as assets or liabilities. 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 the exposure risk arising from fluctuations in foreign currency exchange rates, interest rates, and prices of securities. The Company evaluates hedge effectiveness by comparing the cumulative changes in cash flows from hedged items and corresponding changes in hedging derivative instruments.

5) Allowance for doubtful receivables
Allowance for doubtful receivables is provided principally at an amount computed based on the actual ratio of bad debts in the past and the estimated uncollectible amounts based on the individual analysis of certain receivables.

6) Inventories (see Note 6)
Inventories are stated at cost, determined principally by the average method.

7) Property, plant and equipment
Property, plant and equipment is stated at cost. Depreciation of buildings, acquired prior to April 1, 1998, and other property, plant and equipment is computed over the estimated useful lives of the assets by the declining-balance method for the Company and all domestic subsidiaries. Buildings (other than leasehold improvements), which were acquired on or after April 1, 1998, are depreciated using the straight-line method for the Company and all domestic subsidiaries. Depreciation is computed over the estimated useful lives of the assets by the straight-line method for all overseas subsidiaries.

The principal estimated useful lives are as follows:

Buildings and structures	31 to 50 years
Machinery and equipment	7 years
Tools, furniture and vehicles	4 to 10 years

8) 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.

9) 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.

10) Impairment of fixed assets (see Note 8)
In accordance with "Accounting Standard for Impairment of Fixed Assets" which was issued by the Business Accounting Council in Japan, fixed assets, such as property, plant and equipment and intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset, or group of assets, to estimated undiscounted future cash flows expected to be generated. If the carrying amount of an asset, or group of assets, exceeds its estimated future cash flows, an impairment charge is recognized for the amount by which the carrying amount of the asset exceeds the greater of its net realizable value or value in use.

11) Retirement and severance benefits (see Note 10)
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.

The Company and all domestic subsidiaries have adopted "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. 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. Prior service cost is expensed as incurred.

In January 2005, due to the enforcement of the Defined Contribution Pension Plan Act in Japan, the Company has abolished its qualified pension plan and introduced a new retirement benefit scheme, which is a combination of lump-sum severance plan, cash balance and defined contribution pension plan and has adopted the Financial Accounting Standards Implementation Guidance No. 1 "Accounting for Transfers between Retirement Benefit Plans" which was issued by the Accounting Standards Board of Japan. The Company also established the retirement benefits trust in March 2005.

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. The accrued provision for severance indemnities for members of the board and corporate auditors is not funded.

Certain overseas subsidiaries have defined contribution plans covering substantially all of their employees. The amounts contributed under the plans are charged to income.

12) Foreign currency translation
All monetary assets and liabilities 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.

The Company and all domestic subsidiaries have adopted "Accounting Standard for Foreign Currency Transactions" which was issued by the Business Accounting Council in Japan.

Financial statements of overseas 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 are reflected under the caption, "Foreign currency translation adjustments," in shareholders' equity.

13) Research and development and computer software (see Note 13)

Research and development expenditures are charged to income when incurred.

Expenditures relating to computer software developed for internal use are charged to income when incurred except if they contribute to the generation of income or to future cost savings. Such expenditures are capitalized as an asset and are amortized using the straight-line method over their estimated useful life, five years.

14) Net income and dividends per share (see Note 11)

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 86,662 thousand, 87,390 thousand and 87,931 thousand for the years ended March 31, 2006, 2005 and 2004, respectively.

The diluted net income per share assumes the dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock. The average number of shares used in the computation is 86,808 thousand, 87,485 thousand and 87,942 thousand for the years ended March 31, 2006, 2005 and 2004, respectively.

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

15) Income taxes (see Note 14)

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, operating loss carryforwards 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.

16) Cash and cash equivalents

Cash and cash equivalents mainly include cash on hand, readily available deposits 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.

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 ¥117.47=US$1, the approximate exchange rate prevailing on March 31, 2006. 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

The following is a summary of held-to-maturity debt securities and other securities with a market value at March 31, 2006 and 2005:

	Millions of yen							
	2006				2005			
	Held-to-maturity debt securities				Held-to-maturity debt securities			
	Book value (Carrying amount)	Gross unrealized gains	Gross unrealized losses	Estimated fair value	Book value (Carrying amount)	Gross unrealized gains	Gross unrealized losses	Estimated fair value
Bonds and debentures	¥ 1,000	¥ 9	¥ —	¥ 1,009	¥ 1,000	¥ 12	¥ —	¥ 1,012

	Millions of yen							
	2006				2005			
	Other securities				Other securities			
	Cost	Gross unrealized gains	Gross unrealized losses	Book value (Estimated fair value)	Cost	Gross unrealized gains	Gross unrealized losses	Book value (Estimated fair value)
Equity securities	¥ 8,796	¥ 6,647	¥ —	¥15,443	¥ 8,789	¥ 3,576	¥ (114)	¥12,251

	Thousands of U.S. dollars			
	2006			
	Held-to-maturity debt securities			
	Book value (Carrying amount)	Gross unrealized gains	Gross unrealized losses	Estimated fair value
Bonds and debentures	$ 8,513	$ 78	$ —	$ 8,591

	Other securities			
	Cost	Gross unrealized gains	Gross unrealized losses	Book value (Estimated fair value)
Equity securities	$74,876	$56,585	$ —	$131,461

Maturities of investments at March 31, 2006 and 2005 are as follows:

	Millions of yen				Thousands of U.S. dollars	
	2006		2005		2006	
	Bonds and debentures	Other securities	Bonds and debentures	Other securities	Bonds and debentures	Other securities
Cash equivalents	¥ 9,300	¥ —	¥ 7,500	¥ —	$79,169	$ —
Due within one year	—	—	5	—	—	—
Due after one year through five years	1,000	—	1,000	—	8,513	—
	¥10,300	¥ —	¥ 8,505	¥ —	$87,682	$ —

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, but the Company believes that such risk is mitigated by the high credit ratings of the counterparties.

There is no outstanding derivative transaction for which hedge accounting was not applied at March 31, 2006 and 2005.

6 Inventories

Inventories at March 31, 2006 and 2005 consist of the following:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Merchandise	¥2,680	¥2,295	$22,811
Finished goods	5,151	5,159	43,852
Work in process and semi-finished goods	749	854	6,377
Raw materials and supplies	1,258	1,519	10,707
	¥9,838	¥9,827	$83,747

7 Leases

Finance leases, except for those in which ownership is deemed to be transferred to the lessee, are accounted for as operating leases.

Finance leases:

Equivalent purchase amount, accumulated depreciation and future minimum lease payments on an "as if capitalized" basis at March 31, 2006 and 2005 are as follows:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Machinery and equipment:			
Equivalent purchase amount	¥14,236	¥14,318	$121,192
Equivalent accumulated depreciation amount	11,498	10,751	97,882
Equivalent balance at year-end	2,738	3,567	23,310
Tools:			
Equivalent purchase amount	514	623	4,380
Equivalent accumulated depreciation amount	287	298	2,445
Equivalent balance at year-end	227	325	1,935
Total:			
Equivalent purchase amount	14,750	14,941	125,572
Equivalent accumulated depreciation amount	11,785	11,049	100,327
Equivalent balance at year-end	¥ 2,965	¥ 3,892	$ 25,245
Future minimum lease payments:			
Due within one year	¥ 948	¥ 963	$ 8,069
Due after one year	2,123	3,045	18,071
	¥ 3,071	¥ 4,008	$ 26,140

Lease payments, equivalent depreciation and equivalent interest expense for the three years ended March 31, 2006 are as follows:

	Millions of yen			Thousands of U.S. dollars
	2006	2005	2004	2006
Lease payments	¥1,035	¥977	¥736	$8,813
Equivalent depreciation	969	911	692	8,251
Equivalent interest expense	61	68	55	518

Operating leases:

Future minimum rents under non-cancellable operating leases at March 31, 2006 and 2005 consist of the following:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Due within one year	¥107	¥ 97	$ 916
Due after one year	98	147	832
	¥205	¥244	$1,748

8 Impairment of Fixed Assets

The Company and all domestic subsidiaries account for impairment of fixed assets in accordance with the Financial Accounting Standard on Accounting for Impairment of Assets. The Company and all domestic subsidiaries review the recorded value of their property, plant and equipment and intangible assets to determine if the future cash flows to be derived from these properties will be sufficient to recover the remaining recorded asset values.

The impairment losses recognized for the three years ended March 31, 2006, 2005 and 2004 are as follows:

	Millions of yen			Thousands of U.S. dollars
	2006	2005	2004	2006
Land	¥433	¥700	¥323	$3,686
Building and structures	372	73	54	3,167
Others	104	50	—	892
	¥909	¥823	¥377	$7,745

The Company and certain subsidiaries recorded impairment losses related to the write-down of land and buildings in connection with the logistics operations in the western area of Japan as a result of an outsourcing plan during fiscal 2006. The fair value of the land and buildings was determined by specific appraisal.

The Company decided to sell the rental land and buildings during fiscal 2005. As a result, the Company recognized an impairment loss. The fair value of the land and buildings was determined by using a purchase price offered by a third party.

The Company recognized impairment losses on land and buildings during fiscal 2004. One of the impairment losses was related to the write-down of some unused land and the fair value was determined by estimating the market value. The other impairment loss was related to the write-down of a rental building to be sold and the fair value was determined by using a purchase price offered by a third party.

9 Long-term Debt

Long-term debt at March 31, 2006 and 2005 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Unsecured yen syndicated loans from domestic banks, due in 2008, interest 0.50%	¥5,000	¥5,000	$42,564
Unsecured yen loans from domestic banks, due in installments through 2009, interest 4.75%	614	1,882	5,227
Total	5,614	6,882	47,791
Less: Current portion shown in current liabilities	(168)	(268)	(1,430)
	¥5,446	¥6,614	$46,361

In 2006, the Company entered into a commitment line contract with seven domestic banks. The maximum aggregate credit available to the Company is ¥16,000 million. The credit has not been used as of March 31, 2006.

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 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 maturities of long-term debt at March 31, 2006 are as follows:

Years ending March 31	Millions of yen	Thousands of U.S. dollars
2007	¥ 168	$ 1,430
2008	168	1,430
2009	5,168	43,995
2010	110	936
Total	¥5,614	$47,791

10 Retirement and Severance Benefits

As discussed in Note 2, 11), the Company has abolished its qualified pension plan and introduced a new retirement benefit scheme, which is a combination of lump-sum severance, cash balance and defined contribution pension plans, since January 2005. In addition, the Company has set up an employees' retirement benefit trust in March 2005.

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

The following table sets forth the details of benefit obligation, plan assets and funded status of the Companies at March 31, 2006 and 2005:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
For employees:			
Benefit obligation at end of year	¥(10,838)	¥(10,053)	$(92,259)
Fair value of plan assets at end of year	8,939	7,694	76,094
Funded status (benefit obligation in excess of plan assets)	(1,899)	(2,359)	(16,165)
Unrecognized actuarial loss	655	904	5,576
For directors and corporate auditors:			
Accrued retirement benefit	(463)	(403)	(3,940)
Retirement and severance benefits recognized in the consolidated balance sheets	¥ (1,707)	¥ (1,858)	$(14,529)

Retirement and severance costs of the Companies included the following components for the three years ended March 31, 2006:

	Millions of yen			Thousands of U.S. dollars
	2006	2005	2004	**2006**
For employees:				
Service cost	**¥ 673**	¥ 869	¥1,086	**$ 5,727**
Interest cost	**208**	217	265	**1,767**
Expected return on plan assets	**(154)**	(103)	(92)	**(1,310)**
Recognized actuarial loss	**76**	111	122	**651**
Amortization of unrecognized prior service cost	**—**	572	—	**—**
Net gains on the change of the retirement benefits program	**—**	(316)	—	**—**
Contribution to defined contribution pension plan	**770**	491	—	**6,551**
Net periodic benefit cost	**¥1,573**	¥1,841	¥1,381	**$13,386**
For directors and corporate auditors:				
Accrual for retirement benefit	**¥ 60**	¥ 6	¥ 28	**$ 513**

Assumptions used in the accounting for retirement and severance benefits for the three years ended March 31, 2006 are as follows:

	2006	2005	2004
Method of attributing benefit to period of service	**Straight-line basis**	Straight-line basis	Straight-line basis
Discount rate	**2.00%**	2.00%	2.00%
Expected return on plan assets	**2.00%**	2.00%	2.00%
Amortization period for actuarial losses*	**14 years**	14 years	14 years

* Amortized on a straight-line basis over the average remaining service period for employees in service starting from the year in which the losses occur.

11 Shareholders' Equity

Under the former Japanese Commercial Code ("the Code"), at least 50% of the issue price of new shares 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 the aggregated amount of additional paid-in capital and the legal reserve equals 25% of the stated capital. Additional paid-in capital and the legal reserve may be used to reduce a deficit by resolution of the shareholders' meeting or may be capitalized by resolution of the Board of Directors. The portion in excess of 25% of the stated capital may be used for dividend distribution. The legal reserve, which is included in retained earnings, amounted to ¥1,551 million ($13,207 thousand) and ¥1,551 million as of March 31, 2006 and 2005, respectively.

Cash dividends charged to retained earnings during the three years ended March 31, 2006 represent dividends paid out during the periods. The accompanying consolidated financial statements do not include any provision for the year-end dividend of ¥35 ($0.30) per share, aggregating ¥3,035 million ($25,834 thousand) which was approved at the Company's shareholders' meeting on June 27, 2006 in respect of the year ended March 31, 2006.

Under the Code, the amount available for dividends is based on retained earnings, net of treasury stock, as recorded on the Company's books. At March 31, 2006, retained earnings, net of treasury stock, recorded on the Company's books were ¥104,615 million ($890,569 thousand). Such retained earnings included ¥89,109 million ($758,568 thousand) which is designated as general reserves, but is available for distribution as future dividends subject to approval of the shareholders' meeting and legal reserve requirements. Unrealized holding gains on securities, net of related taxes are not available for distribution as dividends or bonuses to directors and corporate auditors.

12 Stock Options

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

Information concerning option activities and balances for the three years ended March 31, 2006 is as follows:

		Weighted average exercise price	
	Number of shares	Yen	U.S. dollars
Balance at March 31, 2003	335,000	¥ 2,000	
Granted	137,600	1,176	
Balance at March 31, 2004	472,600	1,760	
Granted	78,200	1,743	
Exercised	(46,500)	(1,450)	
Balance at March 31, 2005	504,300	1,786	$ 15.20
Granted	**129,200**	**2,480**	**21.11**
Exercised	**(92,500)**	**(1,544)**	**(13.14)**
Balance at March 31, 2006	**541,000**	**¥ 1,993**	**$ 16.97**

On June 27, 2006, the Company's shareholders' meeting approved that the Company's stock acquisition rights would be allotted to directors and corporate officers of the Company as stock options. These stock option rights are exercisable from June 28, 2008 to June 24, 2016. The total number of stock acquisition rights is limited in aggregate to 102,800 common shares.

13 Research and Development Expenditures

Research and development expenditures charged to income for the three years ended March 31, 2006, 2005 and 2004 amounted to ¥13,971 million ($118,935 thousand), ¥12,620 million and ¥11,853 million, respectively.

14 Income Taxes

The Company and its domestic subsidiaries are subject to a number of taxes based on earnings which, in the aggregate, resulted in average normal tax rates of approximately 40.4%, 40.4% and 42.0% for the years ended March 31, 2006, 2005 and 2004, respectively. Overseas subsidiaries are subject to income taxes of the countries in which they operate.

The effective rates for the three years ended March 31, 2006, 2005 and 2004 differ from the normal tax rates for the following reasons:

	2006	2005	2004
Normal tax rate	**40.4%**	40.4%	42.0%
Expenses not deductible for tax purposes	**1.7**	1.6	2.0
Change in valuation allowance allocated to income tax expenses	**0.6**	2.7	12.6
Per capita inhabitants' tax	**0.4**	0.4	0.6
Lower tax rates of subsidiaries	**(0.7)**	0.6	2.8
Tax credit for research and development expenses	**(6.4)**	(5.7)	(8.3)
Adjustments of deferred tax assets and liabilities for enacted changes in tax rates	**—**	—	0.6
Others	**0.0**	0.2	1.8
Effective tax rate	**36.0%**	40.2%	54.1%

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, 2006 and 2005 are presented below:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Deferred tax assets:			
Tax loss carryforwards	¥ 5,943	¥ 5,657	$ 50,593
Retirement and severance benefits	1,961	1,798	16,692
Accrued expenses	1,039	1,044	8,843
Loss on impairment of fixed assets	514	148	4,375
Accrued enterprise taxes	428	298	3,646
Deferred assets for tax purposes	271	118	2,307
Loss on impairment of golf membership rights	222	230	1,893
Depreciation and amortization	191	666	1,624
Unrealized profit of other intangibles	67	92	571
Loss on valuation of securities	44	231	371
Loss on valuation of inventories	60	74	511
Other	1,368	839	11,643
Total gross deferred tax assets	12,108	11,195	103,069
Less valuation allowance	(7,152)	(6,921)	(60,880)
Net deferred tax assets	4,956	4,274	42,189
Deferred tax liabilities:			
Net unrealized holding gains on securities	(2,698)	(1,391)	(22,966)
Reserve for special depreciation	(227)	(206)	(1,932)
Other	(20)	(23)	(172)
Total gross deferred tax liabilities	(2,945)	(1,620)	(25,070)
Net deferred tax assets	¥ 2,011	¥ 2,654	$ 17,119

Net deferred tax assets at March 31, 2006 and 2005 are reflected in the accompanying consolidated balance sheets under the following captions:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Current assets — deferred tax assets	¥1,651	¥1,625	$14,060
Investments and other assets — deferred tax assets	380	1,052	3,231
Non current liabilities — deferred tax liabilities	(20)	(23)	(172)
Net deferred tax assets	¥2,011	¥2,654	$17,119

15 Contingent Liabilities

At March 31, 2006, the Company has provided guarantees to financial institutions covering employee loans totaling ¥510 million ($4,342 thousand).

16 Segment Information

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

Intercompany sales between geographic areas are recorded at cost plus a markup 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
	2006	2005	2004	2006
Geographic areas:				
Net sales:				
Japan:				
External customers	¥ 89,882	¥ 85,837	¥ 79,338	$ 765,147
Intersegment	986	549	1,018	8,392
Total	90,868	86,386	80,356	773,539
Europe:				
External customers	8,156	6,375	8,849	69,428
Intersegment	1,988	1,624	1,156	16,924
Total	10,144	7,999	10,005	86,352
Other:				
External customers	360	484	1,671	3,068
Intersegment	2,859	2,570	6,036	24,340
Total	3,219	3,054	7,707	27,408
Corporate and eliminations	(5,833)	(4,743)	(8,210)	(49,656)
Consolidated	¥ 98,398	¥ 92,696	¥ 89,858	$ 837,643
Operating income (loss):				
Japan	¥ 22,623	¥ 22,169	¥ 20,351	$ 192,587
Europe	951	(150)	(2,599)	8,098
Other	(708)	(743)	(550)	(6,028)
Corporate and eliminations	(1,871)	(2,294)	(2,678)	(15,932)
Consolidated	¥ 20,995	¥ 18,982	¥ 14,524	$ 178,725
Assets:				
Japan	¥127,647	¥123,067	¥132,791	$1,086,637
Europe	8,744	8,604	11,669	74,437
Other	5,217	5,155	6,016	44,411
Corporate and eliminations	8,850	3,154	(238)	75,339
Consolidated	¥150,458	¥139,980	¥150,238	$1,280,824

The main countries included in Europe and Other are as follows:
Europe: Finland, Germany and Sweden
Other: United States of America, China, Korea and Taiwan

Overseas sales:				
Europe	¥ 6,089	¥ 4,794	¥ 4,370	$ 51,838
North America	1,916	1,704	5,814	16,310
Other	3,608	2,752	2,197	30,716
Total	¥ 11,613	¥ 9,250	¥ 12,381	$ 98,864
Consolidated net sales	98,398	92,696	89,858	837,643
Percentage of overseas sales to consolidated net sales	11.8%	10.0%	13.8%	11.8%

The main countries included in Europe, North America and Other are as follows:
Europe: Finland, Russia, Sweden, Germany and Norway
North America: United States of America and Canada
Other: Korea, China and Taiwan

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 are eliminated upon consolidation).

Independent Auditors' Report

To the Board of Directors of
Santen Pharmaceutical Co., Ltd.:

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

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

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

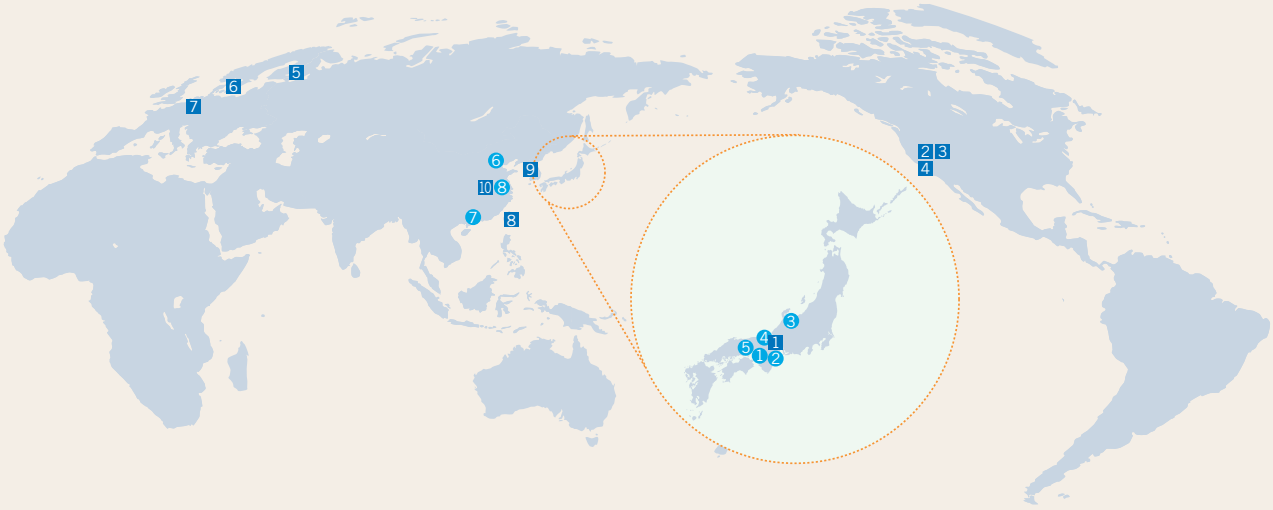
The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended March 31, 2006 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 3 to the consolidated financial statements.

KPMG AZSA & Co.

Osaka, Japan
June 27, 2006

Major Subsidiaries and Facilities

As of July 2006



Subsidiaries

1 Claire Co., Ltd.
348-3, Aza-suwa, Oaza-shide, Taga-cho, Inukami-gun, Shiga 522-0314, Japan
TEL: +81-749-48-2234 FAX: +81-749-48-2239
Business: Cleaning of antidust and sterilized clothing
Equity Ownership: 100%

2 Santen Holdings U.S. Inc.
555 Gateway Drive, Napa, California 94558, U.S.A.
Business: Holding company for North American businesses
Equity Ownership: 100%

3 Santen Inc.
555 Gateway Drive, Napa, California 94558, U.S.A.
TEL: +1-707-254-1750 FAX: +1-707-254-1755
Business: Clinical development and contract manufacturing of pharmaceuticals
Equity Ownership: 100%*

4 Advanced Vision Science, Inc.
5743 Thornwood Drive, Goleta, California 93117, U.S.A.
TEL: +1-805-683-3851 FAX: +1-805-964-3065
Business: Research and development of medical devices
Equity Ownership: 100%*

5 Santen Oy
Niittyhaankatu 20, P.O. Box 33, FIN-33721 Tampere, Finland
TEL: +358-3-284-8111
FAX: +358-3-318-1900
Business: Development, production and marketing of pharmaceuticals
Equity Ownership: 100%

6 SantenPharma AB
Solna torg 3, SE-17145 Solna, Sweden
TEL: +46-8-83-4140 FAX: +46-8-83-4145
Business: Marketing support of pharmaceuticals
Equity Ownership: 100%

7 Santen GmbH
Industriestrasse 1, Germering D-82110, Germany
TEL: +49-89-848078-0
FAX: +49-89-848078-60
Business: Marketing support of pharmaceuticals, regulatory affairs, scientific marketing and business development
Equity Ownership: 100%

* Indirect investment through Santen Holdings U.S. Inc.

8 Taiwan Santen Pharmaceutical Co., Ltd.
16F, No. 57, Sec. 2, Tun-Hwa South Rd., Taipei, Taiwan, R.O.C.
TEL: +886-2-2700-1553
FAX: +886-2-2700-1730
Business: Import and marketing of pharmaceuticals
Equity Ownership: 100%

9 Santen Pharmaceutical Korea, Co., Ltd.
Room 805, Center Building, 91-1, Sogongdong, Chung-ku, Seoul, Republic of Korea
TEL: +82-2-754-1434 FAX: +82-2-754-2929
Business: Import and marketing of pharmaceuticals
Equity Ownership: 100%

10 Santen Pharmaceutical (China) Co., Ltd.
Temporary office:
303 Room, Ganjiang Branch, Agricultural Bank of China, No. 8 Ganjiang East Road, Suzhou, Jiangsu Province, 215021, China
TEL: +86-512-6750-2747
FAX: +86-512-6750-2743

Offices, Laboratory and Plants

1 Corporate Headquarters
9-19, Shimoshinjo 3-chome, Higashiyodogawa-ku, Osaka 533-0021, Japan
TEL: +81-6-6321-7000 FAX: +81-6-6328-5082

2 Nara Research and Development Center
8916-16, Takayama-cho, Ikoma-shi, Nara 630-0101, Japan
TEL: +81-743-79-4501 FAX: +81-743-79-4521

3 Noto Plant
2-14, Shikinami, Houdatsushimizucho, Hakui-gun, Ishikawa 929-1494, Japan
TEL: +81-767-29-2666 FAX: +81-767-29-4233

4 Shiga Plant
348-3, Aza-suwa, Oaza-shide, Taga-cho, Inukami-gun, Shiga 522-0314, Japan
TEL: +81-749-48-2900 FAX: +81-749-48-2901

5 Osaka Plant
9-19, Shimoshinjo 3-chome, Higashiyodogawa-ku, Osaka 533-0021, Japan
TEL: +81-6-6321-7070 FAX: +81-6-6321-3026

6 Beijing Representative Office
Room 2010, Beijing Fortune Bldg., No. 5, Dongsanhuan Beilu, Chaoyang District Beijing 100004, China
TEL: +86-10-6590-8535
FAX: +86-10-6590-8537

7 Guangzhou Representative Office
2605 Peace World Plaza, 362-366, Huan-shi East Road, Guangzhou 510060, China
TEL: +86-20-8375-2212
FAX: +86-20-8387-8799

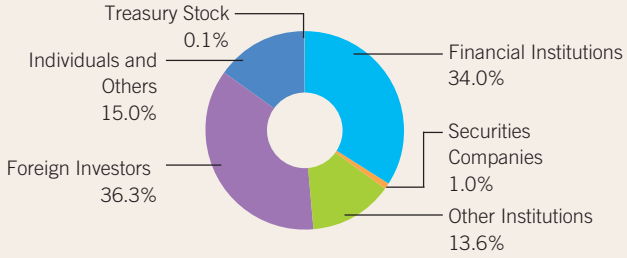
8 Shanghai Representative Office
1804, Shanghai Ciro's Plaza No. 388, West Nanjin Road, Shanghai 200003, China
TEL: +86-21-6334-5813
FAX: +86-21-6334-5819

Corporate Information/Stock Information

As of March 31, 2006

Corporate Headquarters	Santen Pharmaceutical Co., Ltd. 9-19, Shimoshinjo 3-chome, Higashiyodogawa-ku, Osaka 533-0021, Japan URL: http://www.santen.co.jp Investor relations contact: TEL: +81-6-6321-7007 FAX: +81-6-6321-8400 E-mail: ir@santen.co.jp
Established	1890
Paid-in Capital	¥6,319 million
Number of Shareholders	13,557
Stock Exchange Listings	Tokyo and Osaka
Ticker Code	4536
Transfer Agent	Mitsubishi UFJ Trust and Banking Corporation 6-3, Fushimicho 3-chome, Chuo-ku, Osaka 541-8502, Japan
Major Offices	Sendai, Tokyo, Saitama, Nagoya, Osaka, Hiroshima and Fukuoka
Manufacturing Plants	Noto, Shiga and Osaka
Research Laboratory	Nara Research and Development Center
Number of Employees	2,312 (non-consolidated: 1,695)
Number of Shares Issued	86,751,203

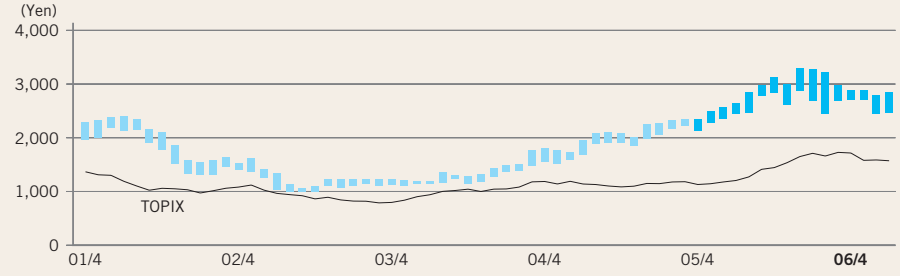
Distribution of Shareholders by Number of Shares Held



Major Shareholders (Leading 10 by number of shares held)

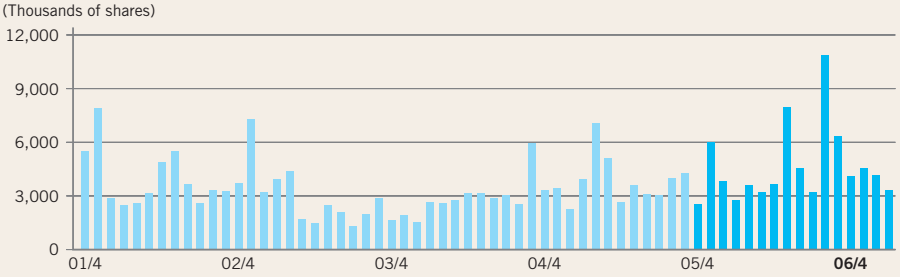
Shareholders	Thousands of Shares	Percentage of Total Voting Rights
Northern Trust Company AVFC Sub-account American Clients	8,030	9.3%
Japan Trustee Services Bank, Ltd.	4,912	5.7
Mita Sangyo Co., Ltd.	4,756	5.5
The Bank of Tokyo-Mitsubishi UFJ, Ltd.	4,296	5.0
The Master Trust Bank of Japan, Ltd.	3,922	4.5
Trust & Custody Services Bank, Ltd.	2,750	3.2
Tokio Marine & Nichido Fire Insurance Co., Ltd.	2,668	3.1
Nippon Life Insurance Company	2,661	3.1
Mitsubishi UFJ Trust and Banking Corporation	1,930	2.2
Investors Bank & Trust Company	1,718	2.0

Stock Price Range Osaka Securities Exchange (monthly basis)



*TOPIX: Tokyo stock price index

Trading Volume Osaka Securities Exchange (monthly basis)



Yearly High and Low Prices

	2002	2003	2004	2005	2006
High (yen)	1,635	1,435	2,240	3,290	3,280
Low (yen)	990	1,099	1,362	2,050	2,440

Note: Calendar years. Stock prices for 2005 are for the period to the end of July.

History

Company History

1900

1890 Founder Kenkichi Taguchi opens Taguchi Santendo in Kitahama, Osaka

1925 Operations incorporated as Santendo Co., Ltd.

1935 Yodogawa Plant established in Higashiyodogawa-ku, Osaka

1945 Head Office transferred to Yodogawa Plant (current site)
Company name changed to Santendo Pharmaceutical Co., Ltd.

1950

1958 Company name changed to current form of Santen Pharmaceutical Co., Ltd.
Santen enters prescription pharmaceuticals business

1977 Stock listed on First Section of Tokyo Stock Exchange and Osaka Securities Exchange
Production system introduced to allow filling of solution into molded containers to make bottle-packed eye drops

1982 Central Research Laboratories established
1985 Noto Plant established

1990 Long-term business vision formulated to mark centenary

1993 Subsidiary Santen Inc. established in United States
1994 Subsidiary Santen GmbH established in Germany
1995 Representative office established in Beijing, China
1996 Nara Research and Development Center and Shiga Plant established
1997 Finnish ophthalmics pharmaceutical company acquired and Santen Oy established
Subsidiary Taiwan Santen Pharmaceutical Co., Ltd. established
1998 Medium-term Plan "Hitomi 21" formulated

2000

2000 Subsidiary Santen Pharmaceutical Korea, Co., Ltd. established
Representative office established in Guangzhou, China
2001 U.S.-based Advanced Vision Science, Inc. acquired

2002 Introduced *Dimple Bottle*, an innovative patient-oriented container for ophthalmic solutions
2003 2003–2005 Medium-term Management Plan formulated
ISO 14001 certification acquired by Noto Plant
Santen Activity Improved Navigator (SAIN) medical information support system developed
2004 U.S. sales partnership with Johnson & Johnson Vision Care, Inc. started

2005 Representative office established in Shanghai, China
Subsidiary Santen Pharmaceutical (China) Co., Ltd. established
2006 2006–2010 Medium-term Management Plan formulated

Product History

1890s Main product is *Heburin-gan*, a cold medicine

1900

1899 Launch of *Daigaku Eye Drops*

1950

1952 Launch of *Daigaku Penicillin Eye Drops*
1953 Launch of *Daigaku Mycillin Eye Drops*
1954 Launch of *Daigaku Super Eye Drops*
1956 Launch of *Sante de U*

1962 Launch of *Mydrin-P*, a mydriatic drug (for pupil dilation)
Launch of *Super Sante* marks first use of plastic eye drop containers in Japan
1963 Launch of *Thiola*, an original liver detoxification agent

1970 Launch of antibiotic ophthalmic *Ecolicin*
1975 Launch of anti-inflammatory ophthalmic *Flumetholon*

1978 Santen commences sales of medical devices

1981 Launch of *Timoptol*, a treatment for glaucoma

1985 Launch of *Sante 40 NE*
1986 Santen commences sales of intraocular lenses
1987 Launch of anti-infective ophthalmic *Tarivid*
Launch of anti-rheumatic *Rimatil*

1991 Launch of *Sante FX*
1992 Launch of *Kary Uni*, a treatment for early-stage senile cataracts
Launch of *BSS PLUS*, an ophthalmic perfusion and bathing solution

1995 Launch of *Hyalein*, a drug for treating corneal and conjunctival epithelial disorders
Launch of anti-allergy ophthalmic *Alegysal*
Launch of anti-rheumatic *Azulfidine EN*
Launch of *OPEGAN Hi*, an adjuvant for ophthalmic operations

1999 Launch of *Timoptol XE*, a treatment for glaucoma
Launch of *Sante FX Neo*

2000

2000 Launch of anti-infective ophthalmic *Cravit*

2001 Launch of *Detantol*, a treatment for glaucoma
Launch of anti-allergy ophthalmic *Livostin*
2002 Launch of *Sante de U Plus E Alpha*
Launch of *Sante 40*
2003 Launch of *ClariFlex* foldable intraocular lenses

2004 Launch of *Rescula*, a treatment for glaucoma
Launch of anti-rheumatic *Metolate*

2006 Launch of *PAPILOCK* Mini ophthalmic solution 0.1%, a treatment for vernal keratoconjunctivitis

*Based on the years when sales were launched by Santen Pharmaceutical.

SANTEN PHARMACEUTICAL CO., LTD.

http://www.santen.co.jp

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