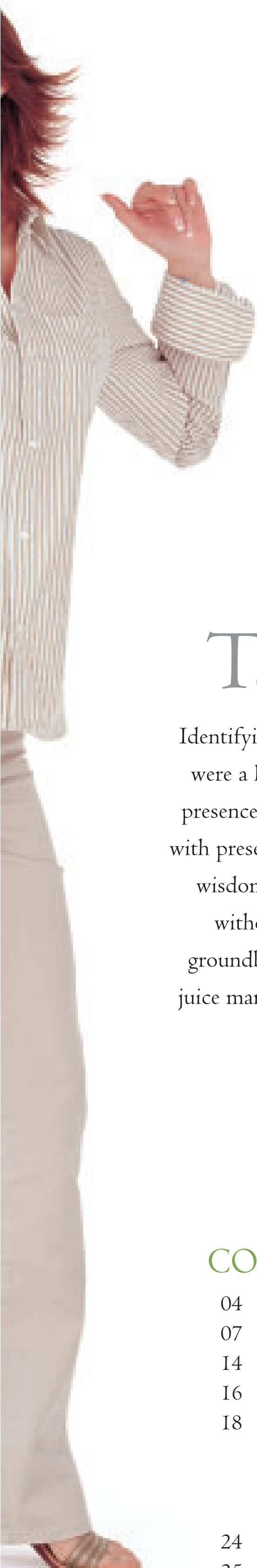
Changing

FANCL CORPORATION

Annual Report 2003

Year Ended March 31, 2003



KENTARO KITAJIMA
“FANCL supplements are the perfect way for me to get the nutrition my body needs when I'm busy and on the move.”

Taking on New Challenges

Identifying and addressing negative consumer issues—that's our hallmark at FANCL. Although we were a late entrant to the highly competitive Japanese cosmetics market, we have built a powerful presence in the industry on a lineup of innovative products. Initially, we made a name for ourselves with preservative-free cosmetic products for women with sensitive skin. Then we turned conventional wisdom on its head in nutritional supplements by proving supplement products can be effective without being expensive. FANCL continues to take on challenges in new fields and develop groundbreaking products and services. Our recent moves into the germinated brown rice and kale juice markets are good examples. In existing and new fields, our goal is simple: To help people look more beautiful and live healthier lives.

ERI TAKAHASHI
“I used to think cosmetic products were all basically the same, but my visit to FANCL Square opened my eyes. FANCL really does offer something different.”

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A Stronger FANCL Brand

Customer-centric approaches and products, paired with an unwavering commitment to quality since our founding, have made the FANCL brand synonymous with trust, safety and sensitivity. We are building on this brand image with FANCL Square, which opened in April 2003 in the heart of Ginza, Tokyo's premier shopping district. This new building is giving more people the chance to get to know our products, services and corporate philosophy—to experience the value in our brand.

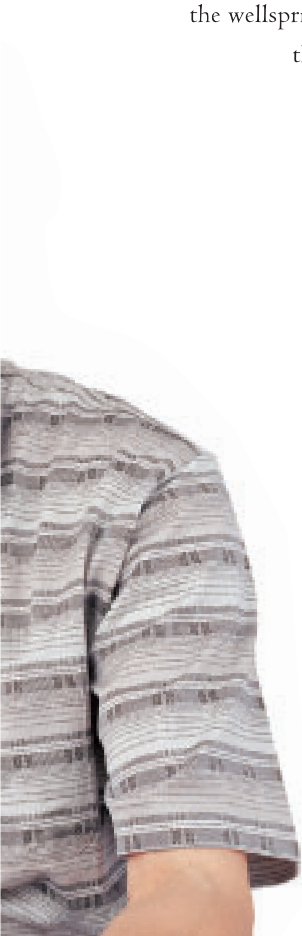
EIICHI MITSUHASHI
"Everyone's more health conscious these days, me included. I changed by daily rice dish to germinated brown rice to keep me going through the working day."

NAOKO MITSUHASHI
"I was a bit apprehensive about the smell and taste of kale juice before I tried FANCL's product. But it surprised me, there was no strange odor or taste."

MICHIKO NAKAO
"During my visit to FANCL SQUARE, it was wonderful to see cosmetics, nutritional supplements, esthetic salon treatments and a whole range of other beauty products all in one place."

Renewed Focus on R&D

Our Central Research Center boasts a 91-member research team that includes 10 researchers with PhDs. All are committed to one goal: developing safe products that win the trust of consumers. Nothing demonstrates this more clearly than the introduction of our own set of strict standards for product safety. These criteria must be cleared before a new product sees the light of day. Our devotion to safety is matched by our desire to innovate—we had filed over 290 patent applications as of May 31, 2003. We believe basic R&D is the wellspring of sustained growth, which is why we will channel resources into this area to develop products worthy of the FANCL name.



SHOKO MARUYAMA

"You don't have to overdo your diet with Perfect Slim, because you can still lose weight without having to cut back your meals."

KIWAKO SHIMIZU
"I'm not too good with cosmetics, but the advice from the in-store FANCL staff really gave me confidence."

OSAMU MINOSHIMA
"I'm a guy but I still want to look good and take care of my skin. I'm not embarrassed to say I've been using FANCL preservative-free skincare products for a while now."

Greater Customer Satisfaction

FANCL gives priority to raising customer satisfaction over and above any short-term goal to increase sales. Our constant customer-centric approach has led to the creation of relationships with consumers that are founded on trust. We have introduced a raft of unique services ahead of rivals that seek to rapidly eliminate any inconvenience for the customer. These include customer-designated delivery points and open-ended guarantee periods for exchanged and returned mail-order goods. In our retail sales channel, we are motivated by a desire to sell products that customers really need rather than just the latest trends.

SAYAKA AND YAYOI TERAMOTO
"My baby's skin is so sensitive that I can't be careful enough. That's why I chose FANCL preservative-free baby care products for safety and peace of mind."

A MESSAGE FROM MANAGEMENT

FANCL Has Changed the Face of Health and Beauty in Japan, Now it's Changing Itself.....

Chairman and Representative Director:
KENJI IKEMORI, 66
Began selling preservative-free cosmetics by himself in 1980, founding FANCL the following year. Success quickly followed, prompting him to try his hand in new product areas such as nutritional supplements, germinated brown rice and kale juice. His years of effort from humble beginnings culminate in FANCL's listing on the First Section of the Tokyo Stock Exchange in 1999.

President and Representative Director:
KENJI FUJIWARA, 56
Joined The Daiei, Inc., a leading Japanese supermarket chain and retailer, in 1969. Becomes general manager of the Food Products Division in 1989, rising to the position of director in 1993. Appointed president of Lawson, Inc., one of Japan's biggest convenience store operators, in 1994. Joined FANCL as an advisor in March 2003, and appointed president and representative director the following June.

HIGHER SALES AND EARNINGS

In fiscal 2003, the year ended March 31, 2003, consolidated net sales rose 6.3% to ¥90,026 million, operating income increased 3.7% to ¥11,526 million and net income was up 7.2% to ¥6,429 million. Net sales were about the same as our target for the year, but operating income exceeded out target, reaching an all-time high. However, higher earnings were due primarily to a decline in advertising expenses. Despite the record results, fiscal 2003 spotlighted a number of issues that will need to be addressed in fiscal 2004. Most significant was slowing sales growth in our core cosmetics and nutritional supplements businesses and our inability to achieve profitability as planned in the germinated brown rice and kale juice businesses.

A NEW SENIOR MANAGEMENT TEAM

At the June 15, 2003 Annual Meeting of Shareholders, Kenji Ikemori, founder of FANCL, having reached the mandatory retirement age of 65, was named chairman and representative director. Replacing him as president and representative director is Kenji Fujiwara, who is 56. Other changes to senior management and directors were made to give younger executives greater authority. For example, our board now includes a director who is 40 years old. This is aimed at injecting a new energy and responsiveness into management in reply to the dramatic changes in our operating environment.

Mr. Fujiwara has many years of experience in the retailing industry. At The Daiei, Inc., he was a director and served as general manager of the grocery division, the largest grocery retailing operation in Japan. There, he succeeded in further raising sales. He was subsequently named president of convenience store operator Lawson, Inc., overseeing this company's stock listing during a difficult period in this company's development. Backed by Mr. Ikemori, the new management team led by Mr. Fujiwara will take the actions required to enable FANCL to post consistent growth in sales and earnings as in the past.

A MORE GROWTH-ORIENTED STRUCTURE

Under the powerful leadership of the founder, FANCL has grown rapidly. During the past few years, however, net sales and operating income have stalled in the region of ¥100 billion and ¥10 billion respectively. We are determined to take FANCL to the next stage of growth, one that will propel us above and beyond these two marks. Doing so will mean strengthening FANCL's management structure by dealing with our past over-reliance on the leadership and knowledge of the founder. Now is the time to ensure that Mr. Ikemori's knowledge and spirit are passed on to the following generations of employees and managers, while he is still involved in management. This will allow FANCL to remain a company with a distinct identity and realize a highly profitable operating structure.

To create a stronger organization, we established a framework in April 2003 made up of five operating divisions and one research center. The general managers of each of these six units have been given greater authority to run day-to-day operations. Additionally, we will be working harder at nurturing employees who are true professionals in a specific fields, a task that we regard as essential to extending the scope of our business activities. Changing how our employees approach their jobs will be vital in achieving this. One step we have taken in this direction is the adoption of a merit-based personnel system to replace the traditional system that was based on seniority. Underpinned by our new personnel system, we believe we have created an environment where our people can be more self-reliant and realize their full potential.

TAKING ON THE IMPOSSIBLE

As one of the most important building blocks of society, companies have an obligation to fulfill their responsibilities to all stakeholders. That means management must constantly work toward generating higher enterprise value while maintaining the proper balance between the different interests of all stakeholders.

FINANCIAL HIGHLIGHTS

FANCL CORPORATION and Consolidated Subsidiaries

	Millions of yen		% Change	Thousands of U.S. dollars
	2003	2002	2003/2002	2003
FOR THE YEAR:				
Net sales	¥90,026	¥84,657	6.3%	$748,969
Operating income	11,526	11,118	3.7	95,890
Income before income taxes	11,078	10,545	5.1	92,163
Net income	6,429	5,995	7.2	53,486
	Yen		% Change	U.S. dollars
PER SHARE DATA:				
Net income	¥279.58	¥307.55	–	$2.32
Cash dividends	35.00	25.00	–	0.29
	Millions of yen		% Change	U.S. dollars
AT YEAR-END:				
Shareholders' equity	¥66,350	¥64,719	–	$551,997
Total assets	79,804	79,026	–	663,927

Note: U.S. dollar amounts have been translated from yen, for convenience only, at the rate of ¥120.20=U.S.$1, the approximate Tokyo foreign exchange market rate as of March 31, 2003.

FANCL has always been a company that seeks to take on and resolve negative consumer issues that rivals in the industry have seen as impossible or even not worth the effort. Our actions are creative and inspired, never restricted by what others are thinking. And we take pride in our ability to surmount one apparently impossible barrier after another. We believe this is the best way to increase our value, generating profits for shareholders over the long term.

FANCL, like many companies, strives to offer its customers beauty and good health. But what distinguishes us from our peers is our wealth of technological skills. Beauty and long life are perhaps two of the most fervent wishes of people everywhere. As a company whose very mission is to assist people achieve these timeless goals, our future is bright.

FANCL today stands on the verge of a new and exciting stage in its development. With the support of shareholders and other stakeholders, we are confident that we can reach the consistently higher goals we know we are capable of.

Kenji Ikemori

KENJI IKEMORI

Chairman

Kenji Fujiwara

KENJI FUJIWARA

President

July 2003

A DISCUSSION WITH THE CHAIRMAN AND PRESIDENT

Q. Would you explain why FANCL's growth rate is slowing?

A. IKEMORI:

I believe we are seeing a weakening in the distinctive FANCL identity that has supported our growth since our foundation. This identity has two core strengths. One is the FANCL brand, which has come to stand for products that consumers can use with complete trust, thanks to the use of highly sophisticated technology. The other is our excellent customer service. At the moment, I think that customers don't have sufficient trust in our brand. Frankly, we've not been working hard enough to get our message across, and we've also become lax in our approach to customer service. When a problem occurs, we need to take the customers' viewpoint to get to the heart of the matter to prevent the issue reoccurring. Right now, there is a tendency to pass responsibilities on to other individuals and sections. We must return to the basics and ask ourselves why FANCL developed into such a respected brand over the years. All of us need to reaffirm the qualities that brought us this far. This is our most crucial task in the current fiscal year.

Q. Mr. Fujiwara, how has your impression of FANCL changed between the time you viewed the company as an outsider and now, since becoming president?

A. FUJIWARA:

There has been no notable change in how I view FANCL since I became president. Our brand represents social awareness and corporate honesty. FANCL also has a reputation as a profitable company. Having spent some time as president, I can say that these images are accurate. But we need to think about whether or not they will take us to the future we envision for ourselves. Here, I must say that FANCL has reached a turning point in its development. I'm extremely impressed with the skills of every single employee, but I also get the impression that their energy is not always being channeled into achieving fundamental, company-wide objectives. Are our people truly working with our customers in mind? At the moment, I don't think so. And I believe this lack of customer focus is perhaps our single greatest weakness right now. All of us need to take a close look at how we do our jobs so that we can become entirely committed to customer needs.


Left: Kenji Ikemori *Chairman*
Right: Kenji Fujiwara *President*

Q. In what ways is FANCL improving services for customers?

A. IKEMORI:

We are making our people more aware of the importance of customer satisfaction. A Customer Committee has been formed to take the lead in building deeper bonds of partnership with our customers. This 182-member committee is made up of customers between the ages of 20 and 70 and many former FANCL employees, including retirees. These individuals perform regular checks to gauge the quality of call centers, store personnel and other places where FANCL serves its customers. Resulting improvements in our services are just one of many benefits. While information gathered by the committee is also invaluable in developing and refining products. In another step, we are currently reviewing our entire customer information management system. This process will facilitate the centralized management of customer data regardless of sales channel—store, mail-order, wholesaler or other means.

Q. Would you describe specific strategies for FANCL's product line?

A. IKEMORI:

We have identified one problem with our product line—the number of products we offer has doubled while total sales have been generally flat. FANCL's answer to multiplying customer likes and dislikes has been the development of items that cater to more narrow market segments. This is particularly true of cosmetics and nutritional supplements. So what happened as a result? Customers were confronted with a bewildering selection of look-alike products. No one was certain which one to buy. So instead of making our customers happy, we created confusion and maybe even dissatisfaction.

At our Central Research Center, our researchers were overwhelmed with new product development projects. That left them little time to spend on basic research. We were no longer able to conceive products that were truly different, the kinds of merchandise that our rivals can't match.

We are now turning our attention back to basic research. We want to create "master products," even if it's just one each year. This is the kind of approach I want to develop. At the same time, we'll stand in the customer's shoes when we review our product line, paring back some items and integrating others into single products.

Q. Making your advertising stand out is obviously just as important as creating distinctive products. What are your plans here?

A. IKEMORI:

We need to learn from our mistakes. Until now, we have placed too much emphasis on promoting individual products. This has prevented us from establishing a unified corporate image. I also believe that we could have used our advertising budget more effectively. We also need to raise our profile in areas outside Japan's major cities.

From now on, we will concentrate on campaigns using an ideal media mix that cover all product lines and sales channels. This will both clarify our corporate image and bring down advertising expenses. Outside major cities, we will use regional advertising media to make the FANCL name a more familiar sight to consumers.

FUJIWARA:

Today, consumers take more time and care when comparing products before a purchase. Quality alone is no guarantee of success. Our customers are, of course, interested in quality. But they are also looking for another reason to part with their hard-earned money. I am confident we can give them that reason by more effectively conveying our strengths built up over the years—the ability to offer products that embody advanced technology along with outstanding quality backed by that technology.

IKEMORI:

FANCL has a reputation for excellence in R&D among scientists and other professionals specializing in our core fields. After all, we have already registered about 290 patents. Despite these accomplishments, awareness of our R&D skills is relatively low among consumers. We have simply not done enough to tell consumers about our technological expertise. It's vital then that our advertisements stress the fact that FANCL is conducting leading-edge research in cosmetics, nutrition and other fields.

Q. What is your strategy for FANCL's cosmetics business?

A. IKEMORI:

We will focus on turning around sales of makeup and bodycare products, both categories where sales declined last year. We have two lines of makeup products: Belmeil, which contains no preservatives; and Clevance, which contains only trace amounts of preservatives. In September 2003, we will introduce a new line of Belmeil products that do away with limitations on colors and usability, problems often associated with preservative-free cosmetics. Following this dramatic improvement in our Belmeil line, we plan to phase out the Clevance brand. In bodycare products, we are revamping our entire lineup in order to emphasize items that offer specific functions, including slimming.

To back up our cosmetics strategy, we unveiled a redesigned version of our Espoir magazine in October 2002. This publication covers a range of inner & outer beauty care subjects. In addition, customers will now find qualified advisers for inner & outer beauty in all our stores. These steps are aimed at stepping up efforts to educate consumers about the importance of beauty that comes from your appearance and from within. This process will take time. There is a close link between good health and attractive skin, and our position is that you can't look your very best just by applying cosmetics and creams. This underpins our drive to promote our theme of inner & outer beauty.

Q. How do you explain the popularity of ATTENIR cosmetics?

A. IKEMORI:

After posting record sales in the March 1999 fiscal year, ATTENIR cosmetics have generally declined since. In the past fiscal year, though, under our new senior management team, ATTENIR posted a V-shaped recovery as sales rose 9.1% to ¥7,078 million. One reason was the success of advertising and sales promotion activities that were more in tune with the customers. We saw a big increase in first-time buyers of ATTENIR cosmetics. R&D was another factor. The February 2002 launch of a new makeup lineup and the September 2002 introduction of a new skincare product lineup both contributed to ATTENIR's popularity. We are now building on this momentum. Key actions will include an improved line of beauty lotion and other specialty products, and the continuation of carefully targeted marketing campaigns.

Q. What are your plans for the nutritional supplements business?

A. IKEMORI:

We are seeing growth in the nutritional supplements market as a whole. At the same time, competition is heating up as sales channels proliferate and more companies enter the market. This situation has led to drastic reductions in retail prices over the past few years. Although we initially entered the market as a cost-cutter in an attempt to set more realistic prices for what had become extortionately priced products, price-cutting is now rampant. FANCL is no longer a leader in terms of pricing, but we do, however, supply products at a cost that is consistent with global prices. Having reached this point, we do not plan to lower our prices further.

But lets think about this from the customer standpoint. Are they really looking for nothing more than the lowest prices? I believe not. I think consumers want nutritional supplement products that meet specific requirements, in other words, that have a high degree of added value. They also want products that remove all doubts about quality and safety. Our products meet all these demands while also offering reasonable prices. If we can make consumers aware of these strengths, I think we will see our sales recover.

Consumers have become much more knowledgeable about nutritional supplements during the past few years. But I feel that they are still unable to select the right products on their own. People must also be aware of the dangers of combining nutritional supplements and pharmaceuticals. FANCL must therefore sell carefully selected products based on information concerning customer health, the medication they are taking and other related factors. We plan to provide this type of service by incorporating data on customers' medication and other items in our nutritional supplement sales system.

Q. Germinated brown rice recorded a strong sales increase last year. How do you plan to take advantage of this growth?

A. IKEMORI:

We are witnessing rapid expansion in demand for germinated brown rice. The public is becoming aware of the numerous benefits of this product in areas ranging from nutrition to dieting. Mail-order operations were responsible for much of last year's sales growth. Demand rose from many sectors, including the foodservice and commercial sectors. Green tea beverage makers are using this rice as an ingredient, schools are including it in their menus, and many food companies are beginning to incorporate this rice in their products. Although this business was in the red last year, mainly due to advertising expenses, we finally expect to report a profit in the year ending in March 2004.

At this point, our priority is enlarging the overall market for germinated brown rice. For example, we plan to hold nationwide food fairs with the support of public-sector agencies, to communicate to the public the nutritional advantages of germinated brown rice. I believe that sales will continue to climb as more people become aware of the benefits of this product.

Q. How do you plan to increase sales of kale juice?

A. IKEMORI:

In the past fiscal year, we recorded a huge increase in the number of customers who use our mail-order channel to receive regular deliveries of kale juice. Sales through convenience stores are stable. Another favorable trend is the increasing use of kale juice in processed foods such as soy milk and yogurt drinks. Our research into the benefits of kale, the key ingredient of kale juice, is sparking further interest in this beverage. Last March, for example, a FANCL research team presented a report at The Pharmaceutical Society of Japan on the ability of kale to alleviate the symptoms of hayfever.

In the current fiscal year, we plan to attract more mail-order customers and increase sales through the wholesale channel to convenience store operators, supermarkets and other retailers. At the same time, we will cut distribution and other costs to make this business profitable.

Left: Kenji Ikemori *Chairman*
Right: Kenji Fujiwara *President*

Left: Kenji Ikemori *Chairman*
Right: Kenji Fujiwara *President*

Q. In what ways will FANCL bolster its various sales channels?

A. IKEMORI:

We got our start as a mail-order company, subsequently adding retailing and wholesaling channels. Increasing mail-order sales will remain a priority, but we must also raise sales at our stores.

FUJIWARA:

There are now approximately 130 FANCL stores. Although this is a large number, it is far below the scale we need to serve all of our customers directly. Meanwhile, the mail-order approach has always been the nucleus of our sales activities. All of our marketing plans are structured around the mail-order channel. If we started focusing on stores more, we would need to make a fundamental shift in the way we approach our entire business, from how we make products to the way we use our computer systems. Now, all store operations are highly reliant on our mail-order infrastructure. This is wasteful in many respects. That's why I believe we could achieve a substantial growth in sales if we repositioned our store operations.

Opening more stores would immediately give a larger number of people the opportunity to see FANCL products for themselves. I think many of them would then make mail-order purchases. So a larger store network would produce both higher store and mail-order sales, helping to generate sales synergies.

I'm sure that my appointment as president was interpreted by many people as signaling the start of a fundamental shift in our sales channel strategy. We are examining our current strategy, but will take actions only after thoroughly considering all our options. FANCL needs to preserve some elements and discard others, but a mistake in selecting what to keep and what to abandon could have a grave impact on our future. Consequently, we will give a great deal of thought to selecting sales channels, both existing and new, that will best serve FANCL and our customers.

Q. Exactly how does FANCL Square fit in with your growth strategy?

A. IKEMORI:

FANCL Square is based on the concept of providing "a place for new discoveries and experiences involving beauty and good health." Personally, I view FANCL Square as a place where we can polish and refine our brand image. The building will allow consumers to understand us better by seeing our products and coming into direct contact with our people. Tokyo's Ginza district, known worldwide as a center of fashion, is an ideal location for FANCL Square. As an integral element of our advertising strategy, we will be using FANCL Square to raise the awareness and value of our brand.

FUJIWARA:

FANCL Square will play a crucial role communicating the total reliability and the quality of our products. True customer satisfaction is impossible unless we can reach customers through all five senses. FANCL Square has been conceived precisely with this in mind. With this facility located at a high-profile Ginza site, we now have a powerful means of disseminating information about our company. I feel very fortunate that the grand opening of the building happened not long after I became president.

Q. In closing, would you describe your plans for expansion outside Japan?

A. IKEMORI:

We are currently active in Asia and the United States. Hong Kong is our largest operation in Asia, and we also have operations in Taiwan, Singapore and Indonesia. We foresee continued growth in the cosmetics market in all parts of Asia. To capitalize on this opportunity, we converted FANCL ASIA (PTE) LTD in Singapore into our overseas headquarters in May 2002. Responsibility for all operations outside Japan has been transferred to this company. We plan to use Asia as a springboard for establishing the FANCL brand on a global scale.

In the United States, we have been conducting mail-order and Internet sales of FANCL products since July 1997. Thus far, results have been disappointing, mainly due to different approaches to cosmetics in Japan and the United States. To solve this problem, we began test marketing products bearing the "boscia" brand in October 2002. This brand has been specifically created for U.S. consumers. Naturally, the new brand fully embodies the core FANCL attributes of trust, high quality and the absence of preservatives. At the same time, "boscia" products are tailored to the needs and skin characteristics of U.S. consumers, as well as to how they use cosmetics. Results of this test marketing campaign will be used to determine our next step in the U.S. cosmetics market.

FANCL SQUARE

RAISING BRAND RECOGNITION AND VALUE

FANCL has won a reputation for trust among the public, thanks to its preservative-free cosmetics, nutritional supplements and other products that are safe, engender confidence, and are developed entirely with the customer in mind. And with a strong focus on research, based on the concept of inner & outer beauty, FANCL has set itself apart from other players in the market. FANCL Square, which was opened in April 2003 in the heart of Ginza, Tokyo's premier shopping district, is our flagship building. We are using it to communicate our corporate philosophy and showcase our products and services by encouraging as many people as possible to visit. In this way, FANCL Square is the focal point of our efforts to raise FANCL brand recognition and value.

FANCL Square offers a wide range of new services that leverage our lineup of existing products—one-on-one advice about cosmetics and nutritional supplements from professional counselors; dependable esthetic services provided by a partner medical institution; and cafeterias that serve food made with germinated brown rice and kale juice. A large CyberVision screen has been installed on the facade of the building to showcase FANCL products, increase brand recognition and provide up-to-the-minute information.

▶BUILDING DETAILS

Address:	8-16, Ginza 5-chome, Chuo-ku, Tokyo
Site area:	289.91 m^2
Total floor space:	2,609.19 m^2
Floors:	Two basement floors and 10 above-ground floors
Structure:	Steel-frame reinforced concrete

▶AMOUNT OF INVESTMENT

Buildings	¥1,204 million
Land	¥4,470 million
Other	¥1,235 million
Total	¥6,910 million

* Land for the building was acquired in October 1999

▶FUTURE OUTLOOK

Projected results for FANCL Square are as follows:

	Year ending March 2004	Year ending March 2005	Year ending March 2006
Net sales	¥867 million	¥902 million	¥933 million
Gross profit	¥640 million	¥666 million	¥687 million
Selling, and administrative expenses	¥1,142 million	¥879 million	¥849 million
[Equivalent amount of advertising expenses]	[¥228 million]	[¥228 million]	[¥228 million]
Operating profit (loss)	¥(274) million	¥14 million	¥65 million

* Since the CyberVision screen, roof-top neon advertisements, and the 10th floor Guest Room will be used to promote the activities of the entire FANCL Group, these costs included in total advertising expenses have been excluded in calculating operating income.

In the year ending March 31, 2004, FANCL Square is expected to report an operating loss of ¥274 million, due to expenses totaling ¥198 million in the first year of operations, including tax on the acquisition of real estate and opening costs.

FLOOR OVERVIEW

8.9F

Restaurant "DOROBUSHI" (Managed by partner)

The first Tokyo branch of one of Kumamoto's most famous restaurants. "*Dorobushi*" serves meals that use only the safest and freshest ingredients and seasonings to bring out the full flavor of the food.

7F

Esthetic Salon (Directly managed)

Offering total facial and esthetic services based on one-on-one counseling, for the ideal beauty treatment experience.

6F

Medical esthetic salon (Managed by partner)

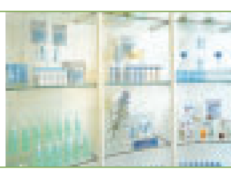
The latest esthetic services such as chemical peeling, laser treatments, skin discoloration and hair removal, and collagen injections offered by a medical institution.

5F

Esthetic Salon (Directly managed)

Quick and competitively priced esthetic services such as foot, nail and hand care treatments, and facials, all using preservative-free beauty products that are kind to the skin.

4F



Shopping Area (Directly managed)

Retailing of preservative-free cosmetics, nutritional supplements, germinated brown rice, kale juice and a variety of other products bearing the FANCL name. Customers can also sample a wide range of tester products on display.

3F

Counseling Area (Directly managed)

Specialist advice offered by professional counselors such as pharmacists and nutritionists. Also a gallery showcasing FANCL's technological capabilities and commitment to safety.

2F

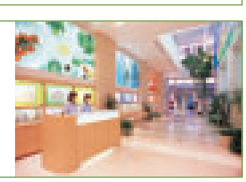
Café (Managed under contract)

Serving healthy drinks and deserts such as seasonal tarts made with germinated brown rice and parfaits using kale juice. Customers are encouraged to relax and enjoy the murals in the café.

1F

Entrance

An oasis from the busy streets, visitors are greeted by a mural painted by Noriko Tamura and a ten-meter high water feature, titled "Encounter with a Waterfall."



B1F

Cafeteria (Managed under contract)

A fast-food cafeteria designed around the concepts of health and beauty. Customers can drop in and enjoy rice balls made from germinated brown rice, kale juice drinks and other healthy pre-pared snacks, while relaxing under a shower of minus ions descending from the water feature.

AT A GLANCE

	Products and Services	Mail-Order Sales	Retail Store Sales	Others *
COSMETICS BUSINESS 	▶ FANCL cosmetics (Preservative-free cosmetics that contain no ingredients known to cause skin allergies) ▶ ATTENIR cosmetics (Attractive, quality cosmetics at reasonable prices)	25.5% ¥22,961 million	12.9% ¥11,554 million	2.9% ¥2,640 million
NUTRITIONAL SUPPLEMENTS BUSINESS 	▶ Health supplements (High-quality nutritional supplements at competitive prices) ▶ Beauty supplements (Nutritional supplements for inner beauty)	19.0% ¥17,123 million	6.1% ¥5,525 million	7.3% ¥6,563 million
OTHER BUSINESSES 	▶ Germinated brown rice ▶ Kale juice ▶ Comfort undergarments ▶ Health equipment and lifestyle goods ▶ Publications targeted at middle-aged and senior readers	21.4% ¥19,250 million	0.7% ¥665 million	4.2% ¥3,745 million
TOTAL CHANNEL SALES		65.9% ¥59,334 million	19.7% ¥17,744 million	14.4% ¥12,948 million

Major Developments During the Year	Segment Total
▶ Based on a philosophy of helping women achieve both inner & outer beauty, we bolstered our FANCL preservative-fee cosmetics line with the launch of Evanté in April 2002 and CLEARTUNE the following June. ▶ Sales of FANCL preservative-fee cosmetics dipped slightly year on year due to lower sales of makeup, hair care and body care products ▶ At FANCL House stores, we arrested a downward trend in sales with revitalization measures that produced sales on a par with the previous year. ▶ ATTENIR cosmetics performed well thanks to the renewal of makeup products in the previous period and a revamp of skincare products in September 2002.	Net Sales 41.3% ¥37,155 million Operating Income Margin 21.8% Operating Income ¥8,099 million
▶ During the year, FANCL launched the world's first plant-based hard-capsule nutritional supplements. ▶ The product lineup was expanded with the launch of 14 new herbal supplements between June and November 2002. ▶ Sales at Genki Station stores were favorable on the back of higher customer footfall. ▶ Sales grew in other channels thanks to an increase to 15 in the number of nutritional supplement products available at Lawson convenience stores, where we rolled out an inner & outer beauty promotion.	Net Sales 32.4% ¥29,211 million Operating Income Margin 23.5% Operating Income ¥6,879 million
▶ The launch of a trial pack helped to generate customer interest, leading to significantly higher mail-order sales of germinated brown rice. Sales for OEM supply were also strong. Overall, germinated brown rice sales doubled. ▶ Annual subscribers to our regular mail-order delivery service for kale juice increased, resulting in substantial growth in this channel. The introduction of a 3-serving pack for convenience stores also boosted sales. Here, too, sales doubled overall. ▶ At mail-order business NGC Co., Ltd., there was an increase in sales of fitness equipment and other products, but this was offset by declining sales of gardening and cooling/heating products, which had been brisk in fiscal 2002	Net Sales 26.3% ¥23,660 million Operating Income Margin -7.0% Operating Income ¥(1,646) million

* "Others" denotes wholesale and overseas sales

REVIEW OF OPERATIONS

Cosmetics Business

Our Cosmetics Business is built on two main brands—FANCL preservative-free cosmetics, based on the philosophy of offering women both inner & outer beauty, and the high-quality ATTENIR cosmetics line, priced competitively to offer consumers value for money.

Building on the launch of the FENATTY series of skincare cosmetics in fiscal 2002, we bolstered our FANCL preservative-free cosmetics line with the introduction of Evanté in April 2002 and CLEARTUNE skincare products in June 2002. In the ATTENIR cosmetics range, we followed up the renewal of makeup products in the previous fiscal year with a revamp of skincare products in September 2002.

Mail-order sales totaled ¥22,961 million, a decrease of 0.5% compared with the previous year. With FANCL cosmetics, we failed to sufficiently signpost the introduction of new brands such as FENATTY, thereby causing some confusion among customers immediately following their launch. Despite this, sales of skincare products were higher than the previous year. This was on the back of a steady shift towards new product lines and success in winning new customers. Total mail-order sales of cosmetics fell 3.4% year on year to ¥16,235 million however, due to a decrease in sales of makeup, hair care and body care products. ATTENIR cosmetics posted a rise in sales of 7.5% to ¥6,725 million, thanks to effective advertising campaigns and sales promotions that broadened our customer base, and product relaunches that were well-received by consumers.

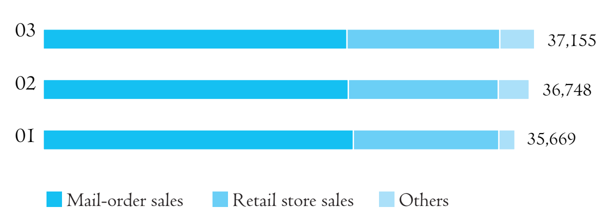
Retail store sales grew 1.9% to ¥11,554 million. Sales at existing stores, which had been on a downward trend, held up well, maintaining the level achieved in fiscal 2002. This was mainly due to the success of measures to revitalize sales. In an effort to develop new retail formats, FANCL opened one FANCL Style store, combining characteristics of FANCL House and Genki Station, and one FANCL Garden shop, which incorporates a relaxing café area. As of March 31, 2003, the number of FANCL House stores totaled 119, including 2 franchise stores, while there were 5 ATTENIR Shops. During the last year, we opened 8 new FANCL House stores and closed 3. There were no new openings or closures of ATTENIR stores.

Looking at **other channels**, sales grew 12.5% to ¥2,640 million. This rise was primarily due to an increase from 5 to 16 in the number of products sold at Lawson convenience stores in June 2002, and the start of an inner & outer beauty campaign across the Lawson network.

Fueled by these initiatives, sales in the Cosmetics Business increased 1.1% year on year to ¥37,155 million. FANCL cosmetics contributed ¥29,683 million of the total, 0.9% down on fiscal 2002, and ATTENIR cosmetics provided ¥7,078 million, an increase of 9.1%. Although advertising expenses declined, there were increases in costs associated with opening of new stores and expenses related to the start of the inner & outer beauty campaign at Lawson convenience stores. Consequently, operating income decreased 3.7%, to ¥8,099 million and the operating margin fell 1.1 percentage points to 21.8%.

Looking ahead, we plan to carry out a renewal of the Belmeil line of preservative-free makeup for people with sensitive skin, and a revamp of special care products such as beauty lotion in ATTENIR cosmetics. The latter step is aimed at creating synergies with last year's renewal of ATTENIR skincare products. Based on these initiatives, we are forecasting increased revenues in the Cosmetics Business on the back of aggressive sales strategies and product relaunches.

NET SALES
(¥ Million)



FANCL Cosmetics

Skincare series FENATTY

Skincare series Evanté

Skincare series CLEARTUNE

FDR cosmetics and bodycare products for ultra dry and sensitive skin

Shape Design slimming lotion and supplements

JINNOUS skincare products for men

ATTENIR Cosmetics

Skincare cosmetics

Foundation products

Lipstick and eyecolor products

	Millions of yen						% change
	2003		2002		2001		2003/2002
		% of net sales		% of net sales		% of net sales	
Net sales	¥37,155	100.0%	¥36,748	100.0%	¥35,669	100.0%	1.1%
Gross profit	28,407	76.5	28,038	76.3	27,792	77.9	
Selling, general and administrative expenses	20,308	54.7	19,632	53.4	19,472	54.6	3.4
Operating income	8,099	21.8	8,406	22.9	8,320	23.3	(3.7)

Nutritional Supplements Business

The nutritional supplement market continues to grow in Japan, as consumer health consciousness increases and the benefits of supplement products become more widely known. Although the market is expanding, competition intensified significantly in fiscal 2003 due to sales channel diversification and the entry of major players into the market.

In the past year, we worked to set FANCL products apart in the market. This was achieved in a number of ways, including the introduction of innovative hard-capsule nutritional supplement products using pullulan plant extract, and the launch of no less than 14 new herbal supplements between June and November 2002.

Mail-order sales declined 4.8% to ¥17,123 million. Attracting new customers proved difficult, mainly due to heightened competition, while unit prices fell as customers tended to purchase lower-end products. By product segment, sales of herbal supplements were strong due to an upgraded product line. Unfortunately this was not sufficient enough to compensate for the decline in sales of both diet supplements, which had posted growth during the previous year, and the functional Support Series.

Retail store sales increased 0.2% to ¥5,525 million. Although sales of diet supplements at FANCL House stores were down year on year, sales at Genki Station stores were healthy due to an increase in the number of customers. As of March 31, 2003, the number of Genki Station stores stood at 8, while Genki Net stores totaled 10. During the year, we opened 1 new Genki Station store and closed 1. In addition, 9 new stores were added in the Genki Net format.

In **other sales channels**, sales grew 19.4% to ¥6,563 million. As with the Cosmetics Business, this rise was primarily the result of an increase to 15 in the number of products available through Lawson convenience stores from June 2002.

Consequently, sales in the Nutritional Supplements Business increased 0.7% year on year to ¥29,211 million. Although the cost of sales ratio increased, mainly due to the introduction of plant-based hard-capsule nutritional supplement products, advertising and sales promotion expenses declined. As a result, operating income increased 15.4% to ¥6,879 million, and the operating income margin rose 2.9 percentage points to 23.5%.

Looking ahead, although conditions will be challenging in the coming fiscal year due to the entry of new competitors into the market, we expect sales to grow slightly. We believe that as we provide more information to customers about the benefits of nutritional supplements, and strive to build a distinctive market niche for each product by narrowing the range of our current product lineup, we can grow sales.

NET SALES

(¥ Million)


Multi-vitamins, multi-amino acids and multi-minerals


Fruit, seaweed and vegetable supplements


Herbal supplements


Herbal supplements


The Support Series


Royal jelly products


Diet supplements, drinks and chewing-gum


Beauty supplements


Good choice vitamin, mineral and supplement packs

	Millions of yen						% change
	2003		2002		2001		2003/2002
		% of net sales		% of net sales		% of net sales	
Net sales	¥29,211	100.0%	¥28,995	100.0%	¥25,408	100.0%	0.7%
Gross profit	19,161	65.6	19,747	68.1	17,532	69.0	
Selling, general and administrative expenses	12,282	42.1	13,787	47.5	12,839	50.5	(10.9)
Operating income	6,879	23.5	5,960	20.6	4,694	18.5	15.4

Other Businesses

In the **Germinated Brown Rice Business** (*Hatsuga Genmai* Business), the launch of a trial pack helped to generate customer interest and higher sales. Sales of economy-size 4-kg and 8-kg bags were solid, while mail-order sales posted a significant increase. Our germinated brown rice product was featured on a popular health information television program, helping to raise its visibility in the market. OEM supply to the Japan Rice Millers and Distributors Cooperative as well as the Hokuren Federation of Agricultural Cooperatives rose steadily. There was also a gradual increase in demand for germinated brown rice from the commercial sector, with convenience store operators using it in ready-made meals, and food companies using it as an ingredient in beverages and bread.

Looking ahead, we plan to enlist the help of public agencies in a nationwide food roadshow. The initiative will showcase the health benefits of germinated brown rice and help to raise the profile of the product throughout Japan. We are also aiming to introduce a system of regular mail-order deliveries of germinated brown rice, modeled on the successful system already in place for our kale juice line.

In the **Kale Juice Business**, effective television advertising contributed to an increase in the number of annual subscribers to our regular mail-order delivery service, resulting in substantial growth in mail-order sales. Wholesale demand was also favorable, due to an increase in the number of stores carrying the product following the introduction of a 3-serving pack for convenience stores in June 2002. Going forward, we hope to make our Kale Juice Business profitable in a short time frame by leveraging the mail-order delivery sales channel and actively developing processed food products that use kale juice as an ingredient.

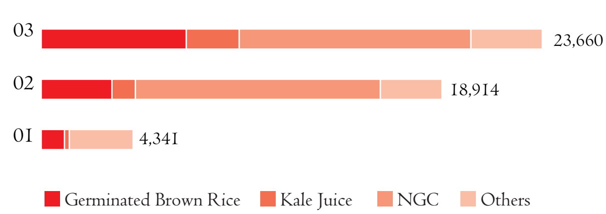
At **NGC Co., Ltd.**, a mail-order business, there was an increase in sales of fitness equipment and other products. However, this was offset by a decline in sales of gardening products and cooling/heating products, which had posted strong sales in fiscal 2002. Consequently, sales declined year on year. Looking ahead, we plan to carry out a restructuring of NGC that will involve a substantial review of sales, services and product selection.

In **Related Businesses**, sales of household sundries and comfort undergarments were strong, but subscriptions to *Mainichi Ga Hakken* (Everyday a New Discovery), a lifestyle magazine for middle-aged and senior readers, continued to decline. We made the decision to cease publication of this magazine after the July 2003 issue, based on our assessment that it is unlikely to achieve profitable operations.

As a result of the above, sales in Other Businesses rose 25.1% to ¥23,660 million. Despite success in significantly reducing losses in the Germinated Brown Rice Business, we recorded an operating loss of ¥1,646 million, essentially unchanged from the previous year. This was mainly due to widening losses in the Kale Juice Business and losses recorded by Related Businesses.

NET SALES

(¥ Million)



Germinated brown rice products

Pop Rice products made with germinated brown rice

Processed rice products using germinated brown rice

FANCL Kale Juice

Powdered kale juice base

Processed soy milk and yoghurt drinks with kale juice

NGC mail-order catalogs

Comfort lifestyle goods

Comfort undergarments

	Millions of yen						% change
	2003		2002		2001		2003/2002
		% of net sales		% of net sales		% of net sales	
Net sales	¥23,660	100.0%	¥18,914	100.0%	¥4,341	100.0%	25.1%
Gross profit	11,413	48.2	8,895	47.0	1,708	39.3	
Selling, general and administrative expenses	13,059	55.2	10,575	55.9	4,240	97.6	23.5
Operating income (loss)	(1,646)	-7.0	(1,681)	-8.9	(2,532)	-58.3	–

STRENGTHENING THE FANCL MANUFACTURING FRAMEWORK

DUAL BASE COSMETICS MANUFACTURING

In January 2003, FANCL made the decision to acquire a factory in Shiga prefecture from Nippon Boehringer Ingelheim Co., Ltd. This represented an important step in the realization of a dual base preservative-free cosmetics manufacturing framework, covering both eastern and western Japan.

Currently, the production of FANCL preservative-free cosmetic products is carried out solely by our factory in Chiba prefecture in eastern Japan. At the Chiba Factory, we have put in place a production process specifically designed for preservative-free cosmetics. That means every product is stamped with the date of manufacture and inventories are kept to an absolute minimum to ensure products are shipped to customers in the freshest possible condition. However, we realized this approach also had certain drawbacks—in the event of an earthquake or other natural disaster centered on eastern Japan, the supply of FANCL preservative-free cosmetics to domestic and international markets could be severely disrupted. This could then have a major impact on FANCL's operations. To eliminate this risk, we took the decision to establish a second factory in western Japan's Shiga prefecture, a region less prone to earthquakes.

Total investment in this new facility has totaled ¥3,688 million, mainly for the purchase of land and buildings, refurbishment and equipment installation. The Shiga Factory was originally designed and built to manufacture pharmaceutical products, and is therefore ideally suited to the exacting standards of FANCL cosmetics production. The Shiga Factory also has cleanroom facilities, essential for the production of high-quality preservative-free cosmetics. Compared to the construction of a totally new facility, our purchase of the Shiga Factory offers significant savings in capital outlays for FANCL.

INTEGRATED MANUFACTURING MANAGEMENT

In October 2002, FANCL Biken Co., Ltd. was established to manage all the manufacturing operations of the FANCL Group. This new company will aim to pare back costs at our three main factories in Shiga, Chiba and Yokohama by substantially reducing the incidence and disposal of defective products and shortening lead times. Our dual base cosmetics manufacturing framework is due to become operational when the Shiga Factory comes on stream in September 2003. The diagram below shows our new manufacturing framework.

Current Framework

Chiba Factory
FANCL preservative-free cosmetics
Nutritional supplements

Yokohama Factory
ATTENIR cosmetics
Nutritional supplements

New Framework After September 2003

Chiba Factory
FANCL preservative-free cosmetics

Yokohama Factory
Nutritional supplements

Shiga Factory
FANCL preservative-free cosmetics
ATTENIR cosmetics

FANCL'S COMMITMENTS TO THE ENVIRONMENT AND SOCIETY

THE ENVIRONMENT

On November 15, 2003, the FANCL Group attained ISO 14001 certification, the international standard for environmental management. Based on its environmental management system, FANCL strives to make a meaningful contribution to protecting the global environment by designing products and services that give due consideration to the environment and safety, and by providing training on environmental issues to its employees.

CONTRIBUTING TO SOCIETY

Since FANCL was founded, we have consistently sought to play a meaningful role in society and local communities. Supporting a variety of regional cultural and artistic activities has been one way we have tried to do this. At FANCL though, we have had a particularly close and rewarding relationship with one group—a social welfare organization called *Tomo*, which means friendship in Japanese.

Tomo was founded in 1986 as Japan's first welfare facility providing people with severe or multiple disabilities the chance to lead a normal life. Until that point, people with severe or multiple disabilities were confined to their beds for much of their lives in specialist facilities for the disabled. With the opening of *Tomo* however, they were finally given the opportunity to live together with their families in the community.

FANCL's relationship with *Tomo* began 15 years ago, when FANCL's founder and chairman, Kenji Ikemori, visited *Tomo* and met with the then manager of the facility, Michie Hiura. During that first visit, Kenji Ikemori quickly built up a rapport with *Tomo* members, helping them to bake bread. These and other kinds of activities are aimed at supporting all *Tomo* members actively work to become independent members of society. This first individual contact has now grown into a relationship that spans many areas of the FANCL organization, including help in running bazaars and the donation of specialist bathing facilities and minibuses. Many FANCL employees are also active volunteers at *Tomo* events: providing makeup services for coming-of-age ceremonies and Christmas parties, giving concerts and putting on lunch parties for *Tomo* members and employees. FANCL's relationship with *Tomo* also directly led to the creation of subsidiary FANCL SMILE Co., Ltd., which provides employment opportunities for disabled persons and gives them the chance to play a fuller role in society.

In this way FANCL is constantly working to play a meaningful role in communities as it strives to give something back to society, no matter how little.

FANCL employees helping to run a *Tomo* bazaar

FANCL employees putting on lunch parties for *Tomo* members and employees

Financial Section

CONTENTS

SIX-YEAR SUMMARY

FANCL CORPORATION and Consolidated Subsidiaries
For the years ended March 31

	Millions of yen					
	2003	2002	2001	2000	1999	1998
FOR THE YEAR:						
Net sales	¥ 90,026	¥ 84,657	¥ 65,418	¥ 62,980	¥ 54,475	¥ 45,429
Cosmetics	37,155	36,748	35,669	38,039	35,891	31,095
Nutritional supplements	29,211	28,995	25,408	21,898	17,180	13,056
Others	23,660	18,914	4,341	3,043	1,404	1,279
Net sales by sales channels:						
Mail-order sales	59,334	56,821	43,360	45,942	43,573	39,491
Retail store sales	17,744	17,073	15,632	14,143	10,425	5,278
Others	12,948	10,763	6,426	2,893	474	660
Gross profit	58,982	56,682	47,034	44,969	40,384	32,822
Gross profit margin (%)	65.5	67.0	71.9	71.4	74.1	72.2
Selling, general and administrative expenses	47,456	45,564	38,402	33,426	29,685	25,012
Selling, general and administrative expense ratio (%)	52.7	53.9	58.7	53.1	54.5	55.0
Operating income	11,526	11,118	8,632	11,543	10,699	7,810
Cosmetics	8,099	8,406	8,320	10,712	10,206	8,138
Nutritional supplements	6,879	5,960	4,694	3,587	3,461	2,546
Others	(1,646)	(1,681)	(2,532)	(641)	(631)	(321)
Operating income margin (%)	12.8	13.1	13.2	18.3	19.6	17.2
Net income	6,429	5,995	4,867	6,723	4,730	3,635
Net income to net sales (%)	7.1	7.1	7.4	10.7	8.7	8.0
ROE (%)	9.8	9.7	8.5	15.3	16.8	17.2
Research and development expenses	1,683	1,524	1,294	1,302	764	562
Capital expenditures	5,397	3,589	2,727	7,138	9,872	6,232
Depreciation	2,268	2,245	2,379	2,424	1,406	1,334
Net cash provided by operating activities	9,828	7,426	6,083	5,681	–	–
Net cash used in investing activities	(5,582)	(5,416)	(4,838)	(7,736)	–	–
Net cash (used in) provided by financing activities	(5,432)	(2,456)	(1,410)	13,006	–	–
Net (decrease) increase in cash and cash equivalents	(1,213)	(437)	(162)	10,949	–	–
	Yen					
PER SHARE:						
Net income	¥ 279.58	¥ 307.55	¥ 249.77	¥ 459.50	¥ 457.74	¥ 396.94
Shareholders' equity	2,976.31	3,320.23	3,051.42	3,678.94	2,944.00	2,357.04
Cash dividends	35.00	25.00	25.00	30.00	25.00	20.00
	Millions of yen					
AT YEAR-END:						
Total assets	¥ 79,804	¥ 79,026	¥ 75,481	¥ 67,657	¥ 49,399	¥ 36,833
Shareholders' equity	66,350	64,719	59,482	55,146	32,761	23,335
Equity ratio (%)	83.1	81.9	78.8	81.5	66.3	63.4
Interest-bearing debt	350	1,092	3,086	2,780	5,052	3,828
Working capital	29,805	31,082	28,456	29,219	12,934	9,178
Number of stores:						
FANCL HOUSE	119	114	121	82	62	46
Genki Station	8	8	7	2	1	1
ATTENIR Shop	5	5	5	1	1	1
Others	12	6	5	1	1	1
Number of consolidated subsidiaries	6	4	3	2	2	2

MANAGEMENT'S DISCUSSION AND ANALYSIS

CHANGES TO THE SCOPE OF CONSOLIDATION

In the fiscal year ended March 31, 2003, FANCL ASIA (PTE) LTD and FANCL Biken Co., Ltd. were included in the scope of consolidation. These new consolidations had a negligible impact on results.

NET SALES

Net sales increased 6.3% year on year to ¥90,026 million. Although sales in the core Cosmetics Business and Nutritional Supplements Business were sluggish, the growth in net sales was driven by a strong performance from Other Businesses, particularly the Germinated Brown Rice Business and the Kale Juice Business.

Sales in the Cosmetics Business rose 1.1% to ¥37,155 million. Sales of FANCL cosmetics, which account for 80% of sales in this segment, fell 0.9% to ¥29,683 million. Sales of ATTENIR cosmetics, which account for the remaining 20% of segment sales, increased 9.1% to ¥7,078 million.

Despite strong demand for basic skincare products in the FANCL cosmetics line on the back of new product launches such as the FENATTY series, and higher sales through the convenience store channel related to the start of the inner & outer beauty campaign in the Lawson chain, falling demand for makeup, hair care and body care products dragged down overall sales of FANCL cosmetics. On a positive note, sales at existing FANCL House stores are improving, reversing the recent downward trend. In ATTENIR cosmetics, the strong year-on-year increase in sales was attributable to successful advertising campaigns and sales promotion activities that led to a steady increase in customers, and relaunches of basic skincare products and makeup, which were well-received by consumers.

In the Nutritional Supplements Business, sales edged up 0.7% to ¥29,211 million. The launch of 14 new herbal supplements and the inner & outer beauty campaign at Lawson stores both translated into higher sales, but performance in this segment was held back by falling demand for the Support Series and diet supplements, which both sold well in fiscal 2002. In mail-order sales, intensifying competition in the market hindered efforts to win new customers and led to falling prices. Although sales of nutritional supplements grew at Genki Station stores, demand in the FANCL House sales channel fell, particularly for diet supplement products.

Sales in Other Businesses recorded a significant increase, rising 25.1% to ¥23,660 million. This was mainly due to higher sales in the Germinated Brown Rice Business and the Kale Juice Business.

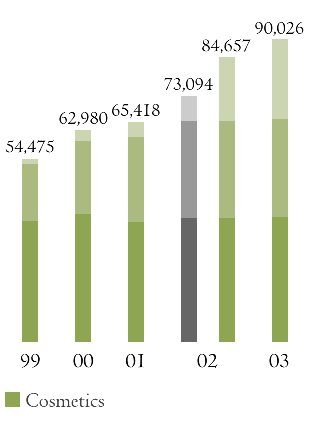
Sales in the Germinated Brown Rice Business more than doubled compared with the previous year, up 104.9% at ¥6,844 million. This sales growth was fueled by greater market visibility for our germinated brown rice product after it was featured on a popular health information television program, and steadily rising OEM demand to the Japan Rice Millers and Distributors Cooperative and the Hokuren Federation of Agricultural Cooperatives.

In the Kale Juice Business, an increase in the number of customers signing annual contracts for regular mail-order deliveries boosted mail-order sales 3.5 times year on year. And combined with sales in the retail-store and wholesale channels, sales jumped 126.2% to ¥2,501 million.

Sales at NGC Co., Ltd., a mail-order company also included in Other Businesses, declined 5.5% to ¥10,936 million. Strong sales of fitness equipment were outweighed by falling sales of gardening products and cooling/heating products, which had posted strong sales in the previous period.

NET SALES BY BUSINESS SEGMENT

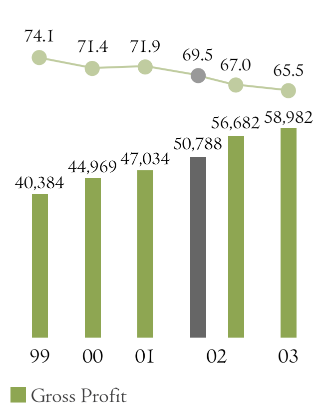
(¥ Million)



* Gray column: excluding the results of newly consolidated NGC and FHG.

GROSS PROFIT/
GROSS PROFIT MARGIN

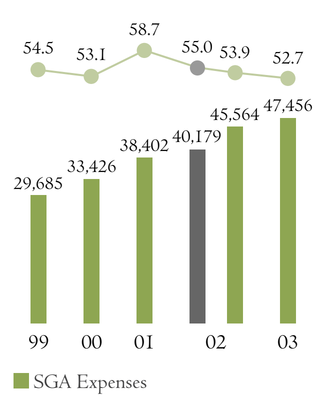
(¥ Million/%)



* Gray column: excluding the results of newly consolidated NGC and FHG.

SGA EXPENSES/
SGA EXPENSE RATIO

(¥ Million/%)



* Gray column: excluding the results of newly consolidated NGC and FHG.

In Related Businesses, sales rose 16.4% to ¥3,376 million, primarily reflecting healthy demand for household sundries and comfort undergarments, which more than covered falling publishing sales as the readership base declined.

GROSS PROFIT

The gross profit margin decreased 1.5 percentage points from the previous fiscal year to 65.5%. This was mainly attributable to costs associated with the launch of plant-based hard-capsule nutritional supplements, a greater proportion of net sales generated by products in the Other Businesses segment, which have lower margins compared with products sold by the core cosmetic and nutritional supplement businesses, and an increase in sales through the wholesale channel.

In the Cosmetics Business, the gross profit margin improved 0.2 of a percentage point to 76.5%. This primarily reflected a greater proportion of sales generated by higher margin products such as basic skincare products, despite a rise in sales via the wholesale channel. In the Nutritional Supplements Business, the gross profit margin declined 2.5 percentage points to 65.6%. The main causes were the above-mentioned launch of plant-based hard-capsule nutritional supplements and more products sold through the wholesale channel. In Other Businesses, the gross profit margin improved 1.2 percentage points to 48.2%, reflecting an improvement in the gross profit margin in the Germinated Brown Rice and Kale Juice Businesses in line with sales growth.

SELLING, GENERAL AND ADMINISTRATIVE (SG&A) EXPENSES

The ratio of SG&A expenses to net sales declined 1.2 percentage points to 52.7%. This improvement was chiefly due to a fall in advertising expenses, which outweighed an increase in transport and subcontracting expenses. Although advertising was aggressively used to promote FANCL's germinated brown rice and kale juice products, advertising was significantly reduced in the Nutritional Supplements Business, in line with a greater focus on efficiency in this segment. As a result, total advertising expenses fell 9.3% year on year to ¥9,261 million, representing a ratio to net sales of 10.3%, 1.8 percentage points lower than the previous period.

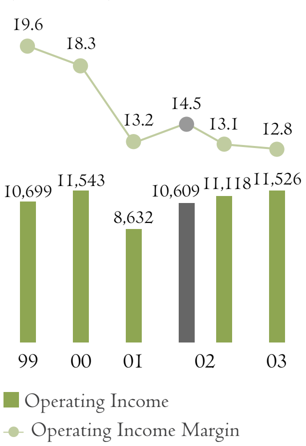
Transport expenses grew in the Germinated Brown Rice and Kale Juice Businesses, in line with higher sales, while subcontracting expenses increased due to higher system outsourcing costs to IBM Corporation.

OPERATING INCOME

Operating income increased 3.7% to ¥11,526 million, while the operating income margin declined 0.3 of a percentage point to 12.8%.

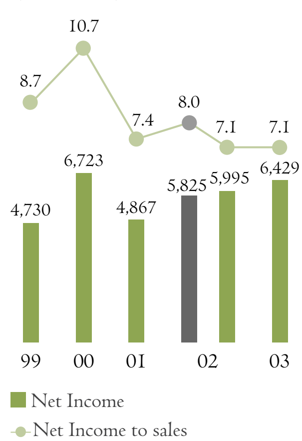
Operating income in the Cosmetics Business declined 3.7% to ¥8,099 million, while the operating income margin fell 1.1 percentage points to 21.8%. This reflected an increase in store opening costs and higher sales promotion expenses related to the start of the inner & outer beauty campaign in Lawson convenience stores. In the Nutritional Supplements Business, the launch of plant-based hard-capsule nutritional supplements had a negative impact on the gross profit margin, although advertising expenses were substantially pared back. These were the main factors in the 15.4% rise in operating income to ¥6,879 million, and the 2.9 percentage point improvement in the operating income margin to 23.5%. Other Businesses posted an operating loss of ¥1,646 million, on a par with the operating loss in the previous period. Despite a substantial improvement in profitability in the Germinated Brown Rice Business, this operating loss was chiefly due to a significant widening of losses in the Kale Juice Business and losses in Related Businesses.

OPERATING INCOME/
OPERATING INCOME MARGIN
(¥ Million/%)



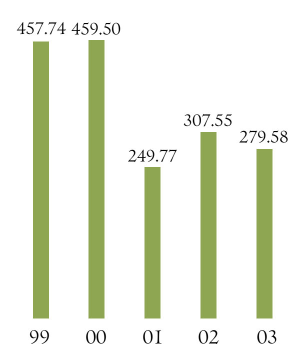
* Gray column: excluding the results of newly consolidated NGC and FHG.

NET INCOME/
NET INCOME TO SALES
(¥ Million/%)



* Gray column: excluding the results of newly consolidated NGC and FHG.

NET INCOME PER SHARE
(¥)



OTHER INCOME (EXPENSES)

Interest and dividend income was ¥44 million, largely unchanged from the previous period. Interest expense fell ¥23 million year on year to ¥14 million due to the repayment of debt.

Other, net expenses decreased ¥103 million from ¥581 million in the previous period, to ¥478 million. This improvement was attributable to an increase in other, net income of ¥262 million to ¥854 million, outweighing the increase in other, net expenses of ¥159 million to ¥1,332 million. Insurance reimbursements and other factors resulted in the rise in other, net income, while other, net expenses increased due to a loss of ¥521 million related to the retirement and disposal of equipment at the former Nagano factory of FANCL Hatsuga Genmai Co., Ltd., and an impairment loss of ¥66 million on bank stocks and other investments.

INCOME BEFORE INCOME TAXES

Income before income taxes increased 5.1% to ¥11,078 million, while income before income taxes as a percentage of net sales was 12.3%, 0.2 of a percentage point lower than the previous period.

NET INCOME

FANCL recorded net income of ¥6,429 million for the year under review, 7.2% higher than fiscal 2002. The ratio of net income to net sales remained largely unchanged at 7.1%.

Net income per share was ¥279.58. As of the end of this fiscal year, the Company did not have any outstanding unexercised convertible bonds or debt equity warrants.

During the year under review, FANCL repurchased and retired treasury stock to the value of ¥4,091 million. This led to an increase in ROE of 0.1 of a percentage point, to 9.8%.

ASSETS

Current Assets

Current assets decreased ¥2,353 million to ¥41,208 million, chiefly due to declines in cash and cash equivalents, inventories, as well as prepaid expenses and other current assets. Cash and cash equivalents decreased ¥1,165 million primarily due to the transfer of ¥1,000 million to time and savings deposits, while inventories declined ¥380 million, reflecting efforts to pare back stocks of ingredients used in nutritional supplements. Prepaid expenses and other current assets fell ¥987 million, attributable to income from temporary payments related to the leaseback of equipment used in the manufacture of germinated brown rice.

Property, Plant and Equipment

Property, plant and equipment increased ¥2,055 million to ¥26,109 million, mainly due to an increase in buildings and structures as well as construction in progress. Buildings and structures rose ¥2,055 million, following the completion of the FANCL Square building in Ginza, Tokyo. Construction in progress increased due to expenses related to the acquisition of a new factory in Shiga prefecture, scheduled to come on stream in September 2003.

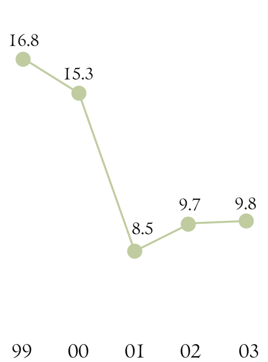
Intangible Assets

Goodwill related to the consolidation of NGC Co., Ltd. in the year ended March 2002 was recorded. FANCL amortizes goodwill evenly over a period of five years.

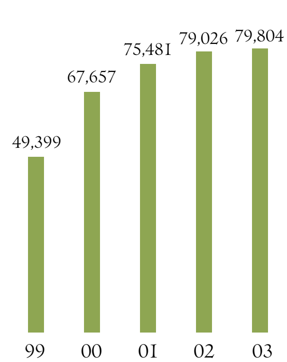
Investments and Other Assets

Investments and other assets rose ¥1,268 million to ¥11,643 million, mainly reflecting the above mentioned transfer of ¥1,000 million in cash and cash equivalents to time and savings deposits.

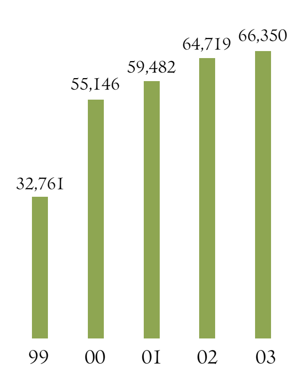
ROE
(%)



TOTAL ASSETS
(¥ Million)



SHAREHOLDERS' EQUITY
(¥ Million)



LIABILITIES

Current Liabilities

Repayment of short-term bank loans led to a decrease of ¥1,076 million in current liabilities, to ¥11,403.

Noncurrent Liabilities

Noncurrent liabilities increased ¥223 million to ¥2,051 million, attributable to the booking of long-term debt for the lease of germinated brown rice manufacturing equipment.

SHAREHOLDERS' EQUITY

Total Shareholders' Equity

Despite repurchasing and retiring treasury stock to the value of ¥2,030 million, total shareholders' equity at the end of the fiscal year stood at ¥66,350 million, ¥1,631 million higher than at the end of the previous year. This increase reflected net income for the year of ¥6,429 million.

Capital Investment

In the year ended March 31, 2003, FANCL carried out capital investment totaling ¥4,753 million. Major investments during the year included the completion of the FANCL Square building in Ginza, Tokyo, and software.

In the Cosmetics Business, capital investment totaled ¥2,030 million, primarily for the purchase of land and buildings for a new factory in Shiga prefecture, scheduled to start operations in September 2003. The Nutritional Supplements Business made capital investments of ¥88 million at its Yokohama Food Plant. In Other Businesses capital investment totaling ¥40 million was made at the Nagano plant to enhance germinated brown rice production capabilities. Capital investment related to the construction of the FANCL Square building in Ginza, Tokyo, totaled ¥1,748 million.

No major equipment was eliminated or sold during this fiscal year.

CASH FLOWS

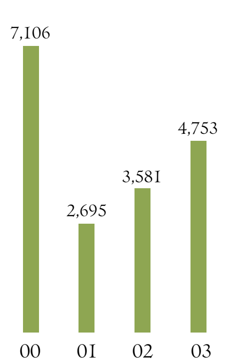
Although net cash provided by operating activities increased, increases in both net cash used in investing activities and net cash used in financing activities led to a ¥1,165 million decrease in cash and cash equivalents at the end of the year, to ¥26,370 million.

Net cash provided by operating activities amounted to ¥9,828 million, an increase of ¥2,402 million compared with the previous year. The main components were ¥11,078 million in income before income taxes, ¥2,527 million in depreciation and amortization, and a ¥399 million decrease in inventories, which were partly offset by ¥5,114 million in income taxes paid.

Net cash used in investing activities totaled ¥5,582 million, an increase of ¥166 million compared with the previous year, due to factors including ¥1,000 million, net, for the payment and termination of time and saving deposits and ¥4,170 million in payment for purchase of property, plant and equipment.

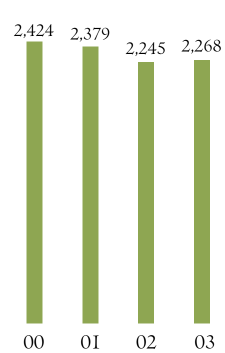
Net cash used in financing activities was ¥5,432 million, an increase of ¥2,976 million compared with the previous year. Factors included a ¥4,159 million payment for purchase of treasury stock, the repayment of long-term debt totaling ¥743 million, and ¥530 million in cash dividends paid.

CAPITAL INVESTMENT
(¥ Million)



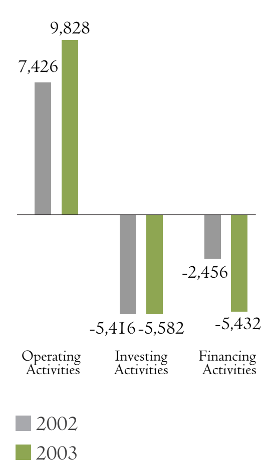
* Consolidated data for capital investment was not prepared prior to fiscal 2000.

DEPRECIATION
(¥ Million)



* Consolidated data for depreciation was not prepared prior to fiscal 2000.

CASH FLOWS
(¥ Million)



CONSOLIDATED BALANCE SHEETS

FANCL CORPORATION and Consolidated Subsidiaries
As of March 31, 2003 and 2002

	Millions of yen		Thousands of U.S. dollars (Note 2)
ASSETS	2003	2002	2003
Current assets:			
Cash and cash equivalents	¥26,370	¥27,535	$219,384
Notes and accounts receivable – trade	8,221	8,298	68,394
Less: Allowance for doubtful accounts	(173)	(176)	(1,439)
	8,048	8,122	66,955
Inventories *(Note 3)*	5,103	5,483	42,454
Deferred taxes *(Note 7)*	767	514	6,381
Prepaid expenses and other current assets	920	1,907	7,654
Total current assets	41,208	43,561	342,828
Property, plant and equipment, at cost *(Note 4)*:			
Land	10,202	10,317	84,875
Buildings and structures	16,129	14,074	134,185
Machinery and equipment	8,570	8,593	71,298
Construction in progress	2,029	643	16,880
	36,930	33,627	307,238
Less: Accumulated depreciation	(10,821)	(9,573)	(90,025)
Property, plant and equipment, net	26,109	24,054	217,213
Intangible assets:			
Goodwill	844	1,036	7,022
Investments and other assets:			
Investment securities:			
Non-consolidated subsidiaries and affiliates	642	795	5,341
Other	306	388	2,546
	948	1,183	7,887
Long-term loans receivable	1,011	1,122	8,411
Deferred taxes *(Note 7)*	357	257	2,970
Other assets	9,607	8,097	79,925
Less: Allowance for doubtful accounts	(280)	(284)	(2,329)
Total investments and other assets	11,643	10,375	96,864
Total assets	¥79,804	¥79,026	$663,927

LIABILITIES AND SHAREHOLDERS' EQUITY	Millions of yen 2003	Millions of yen 2002	Thousands of U.S. dollars (Note 2) 2003
Current liabilities:			
Current portion of long-term debt *(Note 4)*	¥ 350	¥ 742	$ 2,912
Accounts payable – trade	3,341	7,376	27,795
Accrued income taxes *(Note 7)*	2,772	2,850	23,062
Other current liabilities	4,940	1,511	41,098
Total current liabilities	11,403	12,479	94,867
Noncurrent liabilities:			
Long-term debt *(Note 4)*	–	350	–
Accrued retirement benefits *(Note 8)*	1,490	1,350	12,396
Other long-term liabilities	561	128	4,667
Total noncurrent liabilities	2,051	1,828	17,063
Contingent liabilities *(Note 11)*			
Shareholders' equity *(Notes 5, 6 and 15)*:			
Common stock:			
Authorized – 77,946,000 shares in 2003 and 2002			
Issued – 23,392,200 shares in 2003			
– 19,493,500 shares in 2002	10,795	10,795	89,809
Additional paid-in capital	11,706	11,706	97,388
Retained earnings	48,027	42,245	399,559
Net unrealized holding loss on other securities	(10)	(18)	(83)
Less: Treasury stock	(4,168)	(9)	(34,676)
Total shareholders' equity	66,350	64,719	551,997
Total liabilities and shareholders' equity	¥79,804	¥79,026	$663,927

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF INCOME

FANCL CORPORATION and Consolidated Subsidiaries
For the years ended March 31, 2003 and 2002

	Millions of yen		Thousands of U.S. dollars (Note 2)
	2003	2002	2003
Net sales	¥90,026	¥84,657	$748,969
Cost of sales	31,044	27,975	258,270
Gross profit	58,982	56,682	490,699
Selling, general and administrative expenses *(Note 9)*	47,456	45,564	394,809
Operating income	11,526	11,118	95,890
Other income (expenses):			
Interest and dividend income	44	45	366
Interest expense	(14)	(37)	(116)
Other, net	(478)	(581)	(3,977)
Income before income taxes	11,078	10,545	92,163
Income taxes *(Note 7)*:			
Current	5,001	4,745	41,606
Deferred	(352)	(195)	(2,929)
	4,649	4,550	38,677
Net income	¥ 6,429	¥ 5,995	$ 53,486

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

FANCL CORPORATION and Consolidated Subsidiaries
For the years ended March 31, 2003 and 2002

	Thousands	Millions of yen					
	Common stock		Additional paid-in capital *(Note 6)*	Retained earnings *(Notes 6 and 15)*	Net unrealized holding (loss) gain on other securities	Treasury stock	Total shareholders' equity
	Number of shares	Amount					
March 31, 2001	19,493	¥10,795	¥11,706	¥36,978	¥ 5	¥ (2)	¥59,482
Decrease resulting from initial consolidation of subsidiaries		–	–	(3)	–	–	(3)
Decrease resulting from decrease in interest in subsidiaries after allocation of new shares to a third party		–	–	(238)	–	–	(238)
Cash dividends		–	–	(487)	–	–	(487)
Net income		–	–	5,995	–	–	5,995
Purchase of treasury stock		–	–	–	–	(7)	(7)
Net unrealized holding loss on other securities		–	–	–	(23)	–	(23)
March 31, 2002	19,493	10,795	11,706	42,245	(18)	(9)	64,719
Decrease resulting from initial consolidation of subsidiaries		–	–	(115)			(115)
1.2-for-1 stock split	3,899	–	–	–	–	–	–
Cash dividends		–	–	(532)	–	–	(532)
Net income		–	–	6,429	–	–	6,429
Purchase of treasury stock		–	–	–	–	(4,159)	(4,159)
Net unrealized holding loss on other securities		–	–	–	8	–	8
March 31, 2003	23,392	¥10,795	¥11,706	¥48,027	¥(10)	¥(4,168)	¥66,350

	Thousands of U.S. dollars *(Note 2)*					
	Common stock	Additional paid-in capital *(Note 6)*	Retained earnings *(Notes 6 and 15)*	Net unrealized holding (loss) gain on other securities	Treasury stock	Total shareholders' equity
	Amount					
March 31, 2002	$89,809	$97,388	$351,456	$(158)	$ (75)	$538,420
Decrease resulting from initial consolidation of subsidiaries	–	–	(957)	–	–	(957)
1.2-for-1 stock split	–	–	–	–	–	–
Cash dividends	–	–	(4,426)	–	–	(4,426)
Net income	–	–	53,486	–	–	53,486
Purchase of treasury stock	–	–	–	–	(34,601)	(34,601)
Net unrealized holding loss on other securities	–	–	–	75	–	75
March 31, 2003	$89,809	$97,388	$399,559	$(83)	$(34,676)	$551,997

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

FANCL CORPORATION and Consolidated Subsidiaries
For the years ended March 31, 2003 and 2002

	Millions of yen		Thousands of U.S. dollars (Note 2)
	2003	2002	2003
Cash flows from operating activities:			
Income before income taxes	¥11,078	¥10,545	$ 92,163
Adjustments to reconcile income before income taxes to net cash provided by operating activities:			
Depreciation and amortization	2,527	2,504	21,023
Accrued retirement benefits, net of payments	114	119	948
Loss on devaluation of investment securities	–	258	–
Cash surrender value, net of payments	178	121	1,481
Loss on disposal of property, plant and equipment	617	145	5,133
Changes in operating assets and liabilities:			
Notes and accounts receivable – trade	86	(359)	715
Inventories	399	(692)	3,319
Other current assets	1,068	(1,305)	8,885
Accounts payable – trade	(316)	(28)	(2,629)
Other current liabilities	(530)	537	(4,409)
Other noncurrent liabilities	(161)	(225)	(1,339)
Income taxes paid	(5,114)	(4,166)	(42,546)
Other, net	(118)	(28)	(981)
Net cash provided by operating activities	9,828	7,426	81,763
Cash flows from investing activities:			
Payment of fixed-term deposits	(1,500)	(500)	(12,479)
Proceeds from fixed-term deposits	500	–	4,159
Purchases of property, plant and equipment	(4,170)	(3,560)	(34,692)
Proceeds from sale of property, plant and equipment	12	1,390	100
Purchases of software	(386)	(699)	(3,211)
Purchases of stock of affiliates	(5)	(381)	(42)
Proceeds from liquidation of a subsidiary	–	221	–
Collection of long-term loans receivable	121	61	1,007
Increase in other investments and other assets	(311)	(1,948)	(2,587)
Other, net	157	–	1,306
Net cash used in investing activities	(5,582)	(5,416)	(46,439)
Cash flows from financing activities:			
Repayment of short-term bank loans	–	(1,170)	–
Repayment of long-term debt	(743)	(823)	(6,181)
Purchases of treasury stock	(4,159)	(23)	(34,601)
Cash dividends paid	(530)	(487)	(4,409)
Other	–	47	–
Net cash used in financing activities	(5,432)	(2,456)	(45,191)
Effect of foreign exchange rate changes on cash and cash equivalents	(27)	9	(225)
Net decrease in cash and cash equivalents	(1,213)	(437)	(10,092)
Cash and cash equivalents at beginning of year	27,535	27,947	229,077
Cash and cash equivalents of newly consolidated subsidiaries at beginning of year	48	25	399
Cash and cash equivalents at end of year	¥26,370	¥27,535	$219,384

See notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FANCL CORPORATION and Consolidated Subsidiaries
For the years ended March 31, 2003 and 2002

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(A) BASIS OF PREPARATION

FANCL CORPORATION (the "Company") and its consolidated subsidiaries (collectively the "Group") maintain their accounting records and prepare their financial statements in accordance with accounting principles and practices generally accepted in Japan. The accompanying consolidated financial statements have been compiled from the financial statements prepared by the Company as required by the Securities and Exchange Law of Japan and in conformity with accounting principles and practices generally accepted and applied in Japan. Accordingly, the consolidated financial position, results of operations and cash flows presented in the accompanying financial statements may differ in certain material respects from accounting principles and practices generally accepted in countries and jurisdictions other than Japan. Certain reclassifications have been made to present the accompanying consolidated financial statements in a format which is familiar to readers outside Japan.

(B) BASIS OF CONSOLIDATION

The accompanying consolidated financial statements include the accounts of the Company and all its subsidiaries over which substantial control is exerted through either majority ownership of voting stock and/or by other means. All significant intercompany balances and transactions have been eliminated in consolidation. Investments in non-consolidated subsidiaries and affiliates (companies over which the Company has the ability to exercise significant influence) are stated at cost because of their immateriality.

All assets and liabilities of the subsidiaries are revaluated at fair value on acquisition, if applicable, and the excess of cost over underlying net assets at the date of acquisition is amortized over a period of five years on a straight-line basis.

(C) FOREIGN CURRENCY TRANSLATION

All assets and liabilities denominated in foreign currencies of the Company and the domestic consolidated subsidiaries are translated at the current exchange rates in effect at each balance sheet date when not hedged by forward foreign exchange contracts, or at the contracted rates of exchange when hedged by forward foreign exchange contracts. The resulting foreign exchange gain or loss is recognized as other income or expense.

Assets and liabilities of a foreign consolidated subsidiary are translated at the current exchange rates in effect at each balance sheet date and revenue and expense accounts are translated at the average rate of exchange in effect during the year. Translation adjustments are presented as a component of shareholders' equity in the accompanying consolidated financial statements.

(D) CASH EQUIVALENTS

All highly liquid investments, generally with a maturity of three months or less when purchased, which are readily convertible into known amounts of cash and are so near maturity that they represent only an insignificant risk of any change in their value attributable to changes in interest rates, are considered cash equivalents.

(E) SECURITIES

All securities owned by the Company and consolidated subsidiaries are classified into other (available-for-sale) securities which is one of three categories (trading, held-to-maturity and other) defined by the accounting standard for financial instruments.

Other securities with quoted market prices are carried at fair market value. The difference between the acquisition cost and the carrying value of other securities, including unrealized holding gain or loss, is recognized as a component of shareholders' equity under "Net unrealized holding loss on other securities." The cost of other securities sold has been computed based on the average method. Other securities without quoted market prices are stated at cost based on the average method.

(F) INVENTORIES

Finished goods, merchandise, work in process and raw materials are stated at cost by the average method. Supplies are stated at cost by the last purchase price method.

(G) DEPRECIATION AND AMORTIZATION

Depreciation of property, plant and equipment of the Company and consolidated subsidiaries is calculated primarily by the declining-balance method based on the estimated useful lives of the respective assets. However, effective the year ended March 31, 1999, buildings (excluding structures attached to the buildings) acquired on and after April 1, 1998 by the Company and consolidated subsidiaries have been depreciated by the straight-line method. The following summarizes the estimated useful lives of property, plant and equipment by major category:

Buildings and structures	3 – 50 years
Machinery and equipment	2 – 22

Intangible assets are amortized by the straight-line method. The cost of software intended for internal use is amortized by the straight-line method over an estimated useful life of 5 years.

(H) LEASES

Finance leases other than those which transfer the ownership of the leased assets to the lessee are not capitalized, but are accounted for by a method similar to that applicable to operating leases.

(I) RESEARCH AND DEVELOPMENT EXPENSES

Research and development expenses are charged to income when incurred.

(J) ALLOWANCE FOR DOUBTFUL ACCOUNTS

The allowance for doubtful accounts is provided at an amount sufficient to cover possible losses on the collection of receivables, and has been determined based on historical write-off experience plus an estimated amount for probable doubtful accounts after a review of the collectibility of individual receivables.

(K) ALLOWANCE FOR EMPLOYEES' BONUSES

The allowance for employees' bonuses represents a provision for the future payment of employees' bonuses.

(L) RETIREMENT BENEFITS

Employees with three years or more of service are generally entitled to receive a lump-sum payment upon termination of employment with the Company, the amount of which is determined by reference to their basic rate of pay, length of service and the conditions under which the termination occurs.

The Company participates in a contributory defined benefit pension plan which entitles employees of the Company upon retirement at age 60 or more to either a lump-sum payment or pension annuity payments for life, or a combination of both, based on their length of service, salary at the time of retirement and number of years of participation in the plan.

Accrued retirement benefits for employees have been provided based on an estimate of the retirement benefit obligation and the pension fund assets.

Unrecognized actuarial net loss is amortized by the straight-line method over 5 years as a period within the average remaining service period of active employees when incurred commencing the following year.

The Company also provides an accrual for retirement allowances for directors and statutory auditors at the full amount which would be required to be paid if all directors and statutory auditors retired at the balance sheet date based on the Company's internal regulations.

(M) STOCK ISSUANCE EXPENSES

Stock issuance expenses are charged to income when incurred.

(N) INCOME TAXES

Deferred income taxes are recognized by the liability method. Under the liability method, deferred tax assets and liabilities are determined based on the difference between financial reporting and the tax bases of the assets and liabilities, and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

(O) DERIVATIVE FINANCIAL INSTRUMENTS

Derivative financial instruments are carried at fair value with any changes in unrealized gain or loss charged or credited to operations, except for those which meet the criteria for deferral hedge accounting under which unrealized gain or loss is deferred as an asset or a liability. Forward foreign exchange contracts that meet certain criteria are accounted for by the allocation method, which is utilized to hedge against risk arising from fluctuations in foreign exchange rates.

The Group does not make an assessment of the effectiveness of its hedging activities because the relationship between the anticipated cash flows fixed by hedging activities and the avoidance of market risk is so clear that there is no need to evaluate the effectiveness of each hedge against the respective underlying hedged item.

(P) ACCOUNTING STANDARD FOR TREASURY STOCK AND REDUCTION OF LEGAL RESERVE

Effective the year ended March 31, 2003, the Company and consolidated subsidiaries adopted a new accounting standard for treasury stock and the reduction of legal reserves (Accounting Standard No. 1 issued by the Accounting Standards Board of Japan; "ASBJ") which took effect on April 1, 2002. The effect of the adoption of this new standard was immaterial.

(Q) APPROPRIATION OF RETAINED EARNINGS

Under the Commercial Code of Japan, the appropriation of retained earnings with respect to a given financial period is made by resolution of the shareholders at a general meeting held subsequent to the close of such financial period. The accounts for that period do not, therefore, reflect such appropriations. See Note 15.

(R) RECLASSIFICATIONS

In addition, certain reclassifications have been made to the prior year's financial statements to conform them to the current year's presentation.

2. U.S. DOLLAR AMOUNTS

For the convenience of the reader, the accompanying financial statements with respect to the year ended March 31, 2003 have been presented in U.S. dollars by translating all yen amounts at ¥120.20 = US$1.00, the exchange rate prevailing on March 31, 2003. This translation should not be construed as a representation that yen have been, could have been, or could in the future be, converted into U.S. dollars at the above or any other rate.

3. INVENTORIES

Inventories at March 31, 2003 and 2002 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2003	2002	2003
Merchandise	¥ 371	¥ 305	$ 3,084
Finished goods	1,876	1,957	15,608
Raw materials	2,192	2,494	18,236
Work in process	434	508	3,612
Supplies	230	219	1,914
	¥5,103	¥5,483	$42,454

4. LONG-TERM DEBT

Long-term debt at March 31, 2003 and 2002 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2003	2002	2003
Loans from banks, insurance companies and others, due 2004 at rates from 1.45% to 1.88%	¥350	¥1,092	$2,912
Less: Current portion	350	742	2,912
	¥ –	¥ 350	$ –

At March 31, 2003, buildings and structures of ¥1,300 million ($10,816 thousand) and land of ¥1,422 million ($11,832 thousand) were pledged as collateral for long-term debt of ¥350 million ($2,912 thousand) including the current portion. In addition, buildings and structures of ¥1,948 million ($16,210 thousand) and land of ¥591 million ($4,923 thousand) were pledged as collateral for the indebtedness of others.

The aggregate annual maturities of long-term debt subsequent to March 31, 2003 are summarized as follows:

Year ending March 31,	Millions of yen	Thousands of U.S. dollars
2004	¥350	$2,912
	¥350	$2,912

5. SHAREHOLDERS' EQUITY

On October 1, 2001, an amendment (the "Amendment") to the Commercial Code of Japan (the "Code") became effective. The Amendment eliminates the stated par value of the Company's outstanding shares, which resulted in all outstanding shares having no par value as of October 1, 2001. The Amendment also provides that all share issuances after September 30, 2001 will be of shares with no par value. Prior to the date on which the Amendment came into effect, the Company's shares of common stock had a par value of ¥50 per share.

The Code provides that an amount equal to at least 10% of the amounts to be disbursed as distributions of earnings be appropriated to the legal reserve until such reserve and additional paid-in capital equals 25% of the common stock account. The Code also stipulates that, to the extent that the sum of the additional paid-in capital account and the legal reserve exceeds 25% of the common stock account, the amount of any such excess is available for appropriation by resolution of the shareholders.

The retained earnings account in the accompanying consolidated financial statements at March 31, 2003 included the legal reserve of ¥267 million ($2,221 thousand).

On March 6, 2002, the Board of Directors approved a 1.2-for-1 stock split effective May 20, 2002. The Company's stated capital was not affected by this stock split. The number of shares in issue as of May 20, 2002 increased by 3,898,700 shares to 23,392,200 shares. Net income per share for the prior year has not been restated to reflect this stock split.

6. STOCK OPTION PLANS

On June 28, 1999, the shareholders approved a stock option plan to grant warrants to purchase shares of the Company's common stock to the 5 directors and 47 employees of the Company in accordance with the Commercial Code of Japan. Under the plan, 6,240 shares per director and from 1,560 shares to 4,680 shares per employee (for an aggregate number of 154,440 shares) were granted.

The price was set at ¥16,540 per stock option.

As outlined in the Company's stock option plan, this exercise price will be adjusted in accordance with a specified formula for stock splits, reverse stock splits or for other cases.

The stock options will become exercisable during the period from June 29, 2001 to June 28, 2009.

On June 24, 2000, the shareholders approved a stock option plan to grant warrants to purchase shares of the Company's common stock to 264 employees in accordance with the Commercial Code of Japan. Under the plan, a maximum of 113,400 shares were granted to the employees of the Company, which will be allocated in a range of 360 shares to 1,200 shares per employee.

The price was set at ¥13,667 per stock option.

As outlined in the Company's stock option plan, this exercise price will be adjusted in accordance with a specified formula for stock splits, reverse stock splits or for other cases.

The stock options will become exercisable during the period from July 1, 2002 to June 30, 2005.

On June 16, 2002, the shareholders of the Company approved a stock option plan to grant warrants to purchase shares of the Company's common stock to directors, statutory auditors and employees of the Company and its subsidiaries in accordance with the Commercial Code of Japan. Under the plan, a maximum of 500,000 shares were granted to the individuals referred to above.

The stock option price is to be determined by multiplying the higher of ¥4,060 or the final price per share of the Company's common stock traded on the Tokyo Stock Exchange on the day prior to the date of the granting of the options, by a factor of 100.

As outlined in the Company's stock option plan, this exercise price will be adjusted in accordance with a specified formula for stock splits, reverse stock splits or for other cases.

The stock options will become exercisable during the period from July 1, 2004 to June 29, 2007.

7. INCOME TAXES

Income taxes applicable to the Company and consolidated subsidiaries comprise corporation tax, inhabitants' taxes and enterprise tax which, in the aggregate, resulted in a statutory tax rate of approximately 42% for 2003 and 2002. The effective tax rates reflected in the accompanying consolidated statements of income differ from the statutory tax rate primarily due to the effect of permanent nondeductible expenses for tax purposes.

The significant components of deferred tax assets and liabilities at March 31, 2003 and 2002 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2002	2003
Deferred tax assets:			
Accrued enterprise taxes	¥ 277	¥ 267	$ 2,304
Accrued bonuses	280	208	2,329
Allowance for doubtful accounts	161	138	1,339
Accrued severance benefits	533	457	4,434
Depreciation	57	56	474
Net loss carried forward	154	–	1,282
Other	134	104	1,115
	1,596	1,230	13,277
Deferred tax liabilities:			
Unrealized intercompany profit on land	232	232	1,930
Unrealized revaluation gain on land with respect to acquisition of NGC Co., Ltd.	165	170	1,373
Other	76	57	632
	473	459	3,935
Net deferred tax assets	¥1,123	¥ 771	$ 9,342

8. RETIREMENT BENEFITS

The Company and consolidated subsidiaries have defined benefit pension plans and lump-sum retirement payment plans which cover substantially all employees who terminate their employment. In addition to these plans, the Company and consolidated subsidiaries except for a consolidated subsidiary have established a multi-employer welfare pension fund (the "Fund") pursuant to the Welfare Pension Insurance Law of Japan.

The funded status of the defined benefit pension plans for the year ended March 31, 2003 and 2002 is summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2002	2003
Projected benefit obligation	¥1,517	¥1,388	$12,621
Fair value of plan assets	(394)	(328)	(3,270)
Funded status	1,123	1,060	9,351
Unrecognized actuarial net loss	(186)	(191)	(1,550)
Net retirement benefit obligation	937	869	7,801
Prepaid pension cost	181	135	1,507
Accrued retirement benefits	¥1,118	¥1,004	$ 9,308

The consolidated subsidiaries have adopted a simplified method permitted for the calculation of the projected benefit obligation.

Retirement allowances for directors and statutory auditors in the amount of ¥ 371 million ($3,084 thousand) and ¥346 million were included in accrued retirement benefits in the consolidated balance sheets at March 31, 2003 and 2002, respectively.

Retirement benefit expenses for the year ended March 31, 2003 and 2002 were composed of the following:

	Millions of yen		Thousands of U.S. dollars
	2003	2002	2003
Service cost - benefits earned during the year	¥188	¥152	$1,564
Interest cost on projected benefit obligation	16	23	133
Expected return on plan assets	(7)	(5)	(58)
Amortization of unrecognized actuarial net loss	40	(15)	333
Contributions to welfare pension fund	178	169	1,481
Retirement benefit expenses	¥415	¥304	$3,453

In the table above, retirement benefit expenses determined by a simplified method at the consolidated subsidiaries have been included in service cost - benefits earned during the year.

The Company and consolidated subsidiaries have accounted for the contributions to the Fund as retirement benefit expenses. This accounting treatment is permitted under the accounting standard for retirement benefits because it is difficult for the Company and the consolidated subsidiaries to reasonably calculate the value of the pension plan assets based on their contributions.

The assumptions used in the actuarial calculation other than those stated above for the years ended March 31, 2003 and 2002 were principally as follows:

	2003	2002
Discount rates	1.75%	1.75%
Expected rate of return	3.00%	3.00%
Actuarial cost method	Unit credit actuarial cost method	
Amortization period for actuarial differences	5 years *	5 years *
Amortization period for transition obligation arising from the initial adoption of new accounting standard	–	1 year

* Amortized by the straight-line method over a certain period, which falls within the estimated average remaining years of service of the active participants, commencing the year subsequent to the period when the actuarial difference was calculated.

9. RESEARCH AND DEVELOPMENT EXPENSES

Research and development expenses charged to income for the years ended March 31, 2003 and 2002 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2002	**2003**
Research and development expenses	**¥1,683**	¥1,524	**$14,002**

10. LEASES

The Group holds certain machinery and equipment under finance leases which do not transfer the ownership to the lessee. These leases are not capitalized, but are accounted for by a method similar to that applicable to operating leases. If such leases had been capitalized, the acquisition costs and accumulated depreciation of the leased assets at March 31, 2003 and 2002 would have been as follows:

	Millions of yen		Thousands of U.S. dollars
	2003	2002	**2003**
Machinery and equipment	**¥5,229**	¥3,708	**$43,502**
Accumulated depreciation	**1,618**	1,202	**13,461**
	¥3,611	¥2,506	**$30,041**

The following presents the future minimum lease payments subsequent to March 31, 2003 under finance leases which do not transfer ownership:

March 31, 2003	Millions of yen	Thousands of U.S. dollars
Minimum lease payments:		
Due within one year	¥ 736	$ 6,123
Due after one year	2,874	23,910
	¥3,610	$30,033

Lease expenses related to finance leases which do not transfer ownership for the years ended March 31, 2003 and 2002 amounted to ¥827 million ($6,880 thousand) and ¥681 million, respectively. Depreciation related to these leases for the years ended March 31, 2003 and 2002 would have been ¥ 778 million ($6,473 thousand) and ¥627 million, respectively, if the leases had been capitalized.

For the purpose of presentation of the above pro forma amounts, depreciation of the leased assets has been calculated by the straight-line method over the lease terms assuming a nil residual value.

11. CONTINGENT LIABILITIES

Contingent liabilities as of March 31, 2003 amounted to ¥1,776 million ($14,775 thousand) and represented guarantees of borrowings incurred by the nineteen industrial corporations (including the Company) which are members of the Nagareyama Industrial Cooperative Association (the "Association") for the purposes of financing their purchases of manufacturing and other facilities located in the Nagareyama City area and the land upon which such facilities are situated. The Company has guaranteed such borrowings jointly and severally with the other eighteen members of the Association.

12. AMOUNTS PER SHARE

In accordance with a new accounting standard for earnings per share which became effective April 1, 2002, basic net income per share is computed based on the net income available for distribution to shareholders of common stock and the weighted average number of shares of common stock outstanding during each year. Diluted net income per share is computed based on the net income available for distribution to the shareholders and the weighted average number of shares of common stock outstanding during each year assuming full dilution of common stock equivalents. Net assets per share is also computed based on the weighted average number of shares of common stock outstanding during each year. Since there were no potentially dilutive convertible bonds or warrants outstanding as of March 31, 2003 and 2002, diluted net income per share has not been presented.

Net income per share for the year ended March 31, 2002 has been recomputed based on this new accounting standard and is restated in the accompanying financial statements.

	Yen		U.S. dollars
	2003	2002	2003
Net income			
– Basic	¥ 279.58	¥ 307.55	$ 2.32
– Diluted	–	–	–
Net assets	¥2,976.31	¥3,320.23	$24.76

13. DERIVATIVE AND HEDGING ACTIVITIES

The Company utilizes derivative financial instruments such as forward exchange contracts for the purpose of hedging its exposure to adverse fluctuations in foreign currency exchange rates, but does not enter into such transactions for speculative or trading purposes.

The Company may from time to time enter into forward exchange contracts in order to manage certain risks arising from adverse fluctuations in the exchange transactions. The Company has implemented internal regulations under which they will so hedge any significant exchange risks.

No specific disclosure for derivatives has been made as the Company's derivatives principally have only positions which meet the criteria for deferral hedge accounting.

14. SEGMENT INFORMATION

The Company and consolidated subsidiaries are primarily engaged in the manufacture and sales of products mainly in Japan in three segments: a cosmetics business in which various cosmetics are sold through stores and by mail, a nutritional supplements business in which various supplements are sold through stores and by mail, and other business which includes publishing and sales of miscellaneous goods, personal ornaments, herbs and herbal products, underwear and unmilled sprouted rice. This segmentation has been adopted for internal management purposes.

The business segment information of the Company and consolidated subsidiaries for the years ended March 31, 2003 and 2002 is summarized as follows:

BUSINESS SEGMENTS

Year ended March 31, 2003	Millions of yen: Cosmetics business	Nutritional supplements business	Other businesses	Total	Eliminations or corporate	Consolidated
I. Sales and operating income						
Sales to external customers	¥37,155	¥29,211	¥23,660	¥90,026	¥ –	¥90,026
Intersegment sales or transfers	–	–	–	–	–	–
Total sales	37,155	29,211	23,660	90,026	–	90,026
Operating expenses	29,056	22,332	25,306	76,694	1,806	78,500
Operating income (loss)	¥ 8,099	¥ 6,879	¥ (1,646)	¥13,332	¥ (1,806)	¥11,526
II. Total assets, depreciation and capital expenditures						
Total assets	¥23,017	¥11,172	¥ 9,200	¥43,389	¥36,415	¥79,804
Depreciation	1,218	597	375	2,190	78	2,268
Capital expenditures	2,475	349	374	3,198	2,199	5,397

Year ended March 31, 2002	Millions of yen: Cosmetics business	Nutritional supplements business	Other businesses	Total	Eliminations or corporate	Consolidated
I. Sales and operating income						
Sales to external customers	¥36,748	¥28,995	¥18,914	¥84,657	¥ –	¥84,657
Intersegment sales or transfers	–	–	–	–	–	–
Total sales	36,748	28,995	18,914	84,657	–	84,657
Operating expenses	28,342	23,035	20,595	71,972	1,567	73,539
Operating income (loss)	¥ 8,406	¥ 5,960	¥ (1,681)	¥12,685	¥ (1,567)	¥11,118
II. Total assets, depreciation and capital expenditures						
Total assets	¥21,229	¥12,049	¥10,229	¥43,507	¥35,519	¥79,026
Depreciation	1,293	632	239	2,164	81	2,245
Capital expenditures	1,057	634	1,898	3,589	–	3,589

Year ended March 31, 2003	Thousands of U.S. dollars: Cosmetics business	Nutritional supplements business	Other businesses	Total	Eliminations or corporate	Consolidated
I. Sales and operating income						
Sales to external customers	$309,110	$243,020	$196,838	$748,968	$ –	$748,968
Intersegment sales or transfers	–	–	–	–	–	–
Total sales	309,110	243,020	196,838	748,968	–	748,968
Operating expenses	241,730	185,791	210,532	638,053	15,025	653,078
Operating income (loss)	$ 67,380	$ 57,229	$ (13,694)	$110,915	$ (15,025)	$ 95,890
II. Total assets, depreciation and capital expenditures						
Total assets	$191,489	$ 92,945	$ 76,539	$360,973	$302,954	$663,927
Depreciation	10,133	4,967	3,120	18,220	649	18,869
Capital expenditures	20,590	2,903	3,103	26,606	18,294	44,900

Unallocatable operating expenses included under “Eliminations or corporate” for the years ended March 31, 2003 and 2002 amounted to ¥1,806 million ($15,025 thousand) and ¥1,567 million, respectively, and consisted of operating expenses incurred in the Administration Department of the Company. Corporate assets included under “Eliminations or corporate” for the years ended March 31, 2003 and 2002 amounted to ¥36,415 million ($302,953 thousand) and ¥35,519 million, respectively, and consisted principally of cash and cash equivalents, short-term investments, land and funds for long-term investments (investment securities and other) of the Company.

GEOGRAPHICAL SEGMENTS

Since none of the Company’s consolidated subsidiaries or branches were located in countries or regions other than Japan for either of the years ended March 31, 2003 and 2002, geographical segment information has not been presented.

OVERSEAS SALES

Since overseas sales were less than 10% of consolidated sales for the years ended March 31, 2003 and 2002, no disclosure of overseas sales has been presented.

15. SUBSEQUENT EVENTS

The following appropriations of retained earnings of the Company, which have not been reflected in the consolidated financial statements for the year ended March 31, 2003, were approved at a meeting of the shareholders held on June 15, 2003:

March 31, 2003	Millions of yen	Thousands of U.S. dollars
Cash dividends (¥22.50= U.S.$0.19 per share)	**¥502**	**$4,173**

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

The Board of Directors
FANCL CORPORATION

We have audited the accompanying consolidated balance sheets of FANCL CORPORATION and consolidated subsidiaries as of March 31, 2003 and 2002, and the related consolidated statements of income, shareholders' equity, and cash flows for the years then ended, all expressed in yen. These financial statements are the responsibility of the Company's management. Our responsibility is to independently express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of FANCL CORPORATION and consolidated subsidiaries at March 31, 2003 and 2002, and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles and practices generally accepted in Japan.

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended March 31, 2003 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 2 to the consolidated financial statements.

Shin Nihon & Co.

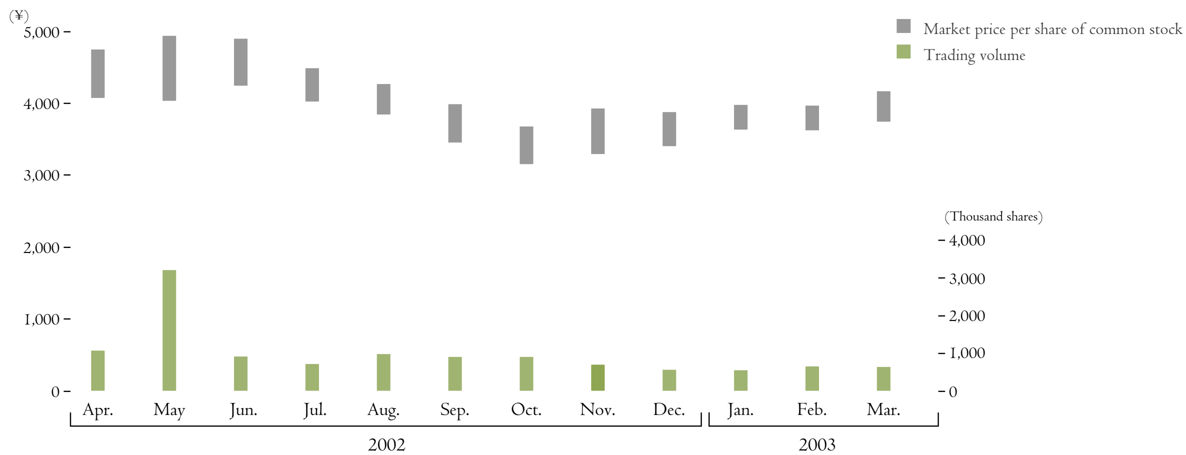
June 15, 2003

See Note 1 to the consolidated financial statements which explains the basis of preparation of the consolidated financial statements of FANCL CORPORATION and consolidated subsidiaries under Japanese accounting principles and practices.

CORPORATE DATA

Market Price per Share of Common Stock and Trading Volume

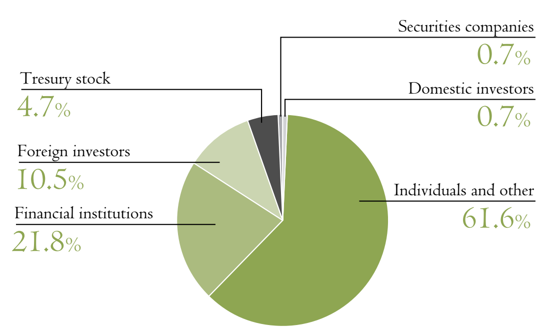
	2002									2003		
	Apr.	May	Jun.	Jul.	Aug.	Sep.	Oct.	Nov.	Dec.	Jan.	Feb.	Mar.
High (¥)	4,760	4,950	4,910	4,500	4,280	4,000	3,690	3,940	3,890	3,990	3,980	4,180
Low (¥)	4,070	4,030	4,240	4,020	3,840	3,450	3,150	3,290	3,400	3,630	3,620	3,740
Trading Volume (Thousand shares)	1,095	3,228	941	743	1,005	929	925	721	590	579	678	663



Composition of Shareholders

(Percentage of ownership)

	2001		2002		2003
	Mar.	Sep.	Mar.	Sep.	Mar.
Individuals and other	63.5	60.1	61.7	62.6	61.6
Financial institutions	24.5	26.0	24.4	23.0	21.8
Foreign investors	9.8	11.9	12.0	11.1	10.5
Treasury stock	0.0	0.0	0.0	1.4	4.7
Domestic investors	1.3	1.0	0.9	0.8	0.7
Securities companies	0.9	1.0	1.0	1.1	0.7



Mar. 2003

Directors and Officers

(As of June 15, 2003)

Chairman and Representative Director

Kenji Ikemori

President and Representative Director

Kenji Fujiwara

Managing Directors

Yoshifumi Narimatsu

Kazuyoshi Miyajima

Takayoshi Okada

Directors

Hisashi Yamamoto

Takao Kokubu

Katsuhiko Matsumoto

Kenichi Ishiwata

Kenichi Sugama

Sumiya Nakajima

Statutory Auditors

Michihiro Yoneda

Fumiko Ikeda

Katsunori Koseki

Corporate Executive Officers

Takao Ishida

Shuji Miyahara

Noburou Katase

Akira Yajima

Yutaka Hirano

Investor Information

(As of March 31, 2003)

Head Office

89-1 Yamashita-cho, Naka-ku, Yokohama,
Kanagawa-ken 231-8528, Japan
Tel: 81(45)226-1200

Established

August 1981

Common Stock Listing

Tokyo Stock Exchange, First Section
(Code: 4921)

Paid-in Capital

¥10,795,161,280

Number of Shareholders

19,505

Common Stock

Authorized Shares: 77,946,000
Outstanding Shares: 23,392,200

Number of Full-time Employees

605

Transfer Agent and Registrar

UFJ Trust Bank Limited
10-11, Higashisuna, 7-chome, Koto-ku,
Tokyo 137-8081, Japan
Tel: 81(3)5683-5111

Annual Meeting of Shareholders

In the middle of June in Kanagawa

Consolidated Subsidiaries

ATTENIR CORPORATION

NICOSTAR Co., Ltd.

NGC Co., Ltd.

FANCL Hatsuga Genmai Co., Ltd.

FANCL ASIA (PTE) LTD

FANCL Biken Co., Ltd.

Investor Relations

For further information, please contact:
Investor Relations Department
Tel: 81(45)226-1470
http://www.fancl.co.jp/

FANCL
CORPORATION

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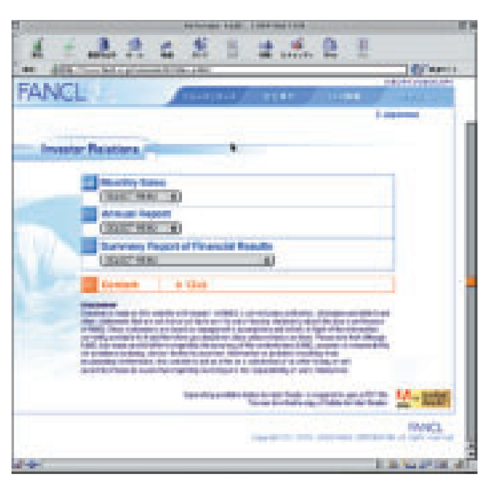
Yokohama, Kanagawa-ken 231-8528, Japan
Head Office phone: 81(45)226-1200



http://www.fancl.co.jp/corporate/ir/index_e.html

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