FANCL

FANCL Corporation

ANNUAL REPORT 2006

For the Year Ended March 31, 2006

STAYING TRUE TO OUR VISION

PROFILE

In 1980, when using preservatives in cosmetics was the standard practice, FANCL developed the industry's first preservative-free cosmetics that women with sensitive skin could use with confidence. Since then, our basic approach to business has been about eliminating negative issues for consumers such as inconvenience and lack of confidence in products in their pursuit of health and beauty.

In 1994, we moved into the nutritional supplements field, using an integrated in-house ingredient procurement, manufacturing and sales framework to create a groundbreaking lineup of high-quality, reasonably priced supplements. Subsequent products developed by FANCL include easy-to-eat germinated brown rice with high nutritional value, and flavorsome, reasonably priced kale juice.

The FANCL brand has been built on the concept of preservative-free products that are reliable, safe and gentle. Now, as a specialist in inner and outer beauty, we are leveraging our own unique technologies and ingredients to provide products and services that offer real value based on an entirely new approach. Our goal: to raise FANCL's enterprise value.

CONTENTS

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS
Statements made in this annual report with respect to FANCL's current plans, strategies, estimates, and beliefs, as well as other statements that are not historical facts, are forward-looking statements about the future performance of FANCL. These statements are based on management's beliefs in light of information available to it at the time of the writing of this report. The actual performance of the Company could differ significantly from these forward-looking statements as a result of unpredictable factors such as changes in customer preferences, social conditions, and economic conditions. Moreover, FANCL is under no obligation to revise forward-looking statements, irrespective of new data, future events, or other developments. Readers should therefore not place undue reliance on them.

FINANCIAL HIGHLIGHTS

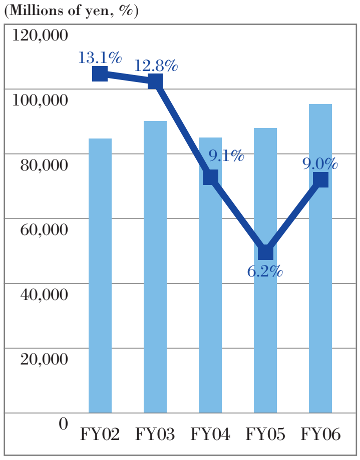
FANCL CORPORATION and Consolidated Subsidiaries
For the years ended March 31

	Millions of yen					Thousands of U.S. dollars (Note)
	2006	2005	2004	2003	2002	2006
FOR THE YEAR:						
Net sales	¥ 95,322	¥87,937	¥84,957	¥90,026	¥84,657	$811,462
Operating income	8,575	5,428	7,769	11,526	11,118	72,994
Net income	5,184	1,710	3,387	6,429	5,995	44,129
Advertising expenses	9,792	11,105	9,865	9,262	10,213	83,358
Sales promotion expenses	9,319	9,475	7,998	8,615	8,161	79,338
Net cash provided by operating activities	9,163	4,638	5,861	9,828	7,426	77,998
Net cash used in investing activities	(10,280)	(4,807)	(4,117)	(5,582)	(5,416)	(87,513)
Net cash used in financing activities	(22)	(1,090)	(4,533)	(5,432)	(2,456)	(183)
Net decrease in cash and cash equivalents	(1,139)	(1,254)	(2,809)	(1,213)	(437)	(9,698)
	Yen					U.S. dollars (Note)
PER SHARE:						
Net income	¥ 242.6	¥ 80.3	¥ 154.6	¥ 279.5	¥ 307.6	$ 2.06
Shareholders' equity	3,317.0	3,111.2	3,082.4	2,976.3	3,320.2	28.24
Cash dividends	55.0	50.0	42.5	35.0	25.0	0.47
	Millions of yen					Thousands of U.S. dollars (Note)
AT YEAR-END:						
Total assets	¥85,148	¥79,416	¥78,479	¥79,804	¥79,026	$724,848
Shareholders' equity	71,406	66,203	65,613	66,350	64,719	607,865
RATIO:	%					
Operating income margin (%)	9.0	6.2	9.1	12.8	13.1	
Advertising and sales promotion expenses ratio (%)	20.1	23.4	21.0	19.9	21.7	
ROE (%)	7.5	2.6	5.1	9.8	9.7	

Note: U.S. dollar amounts are the yen equivalent, calculated, for convenience only, at a rate of ¥117.47 = U.S. $1, the approximate Tokyo foreign exchange market rate as of March 31, 2006.

NET SALES AND OPERATING INCOME MARGIN

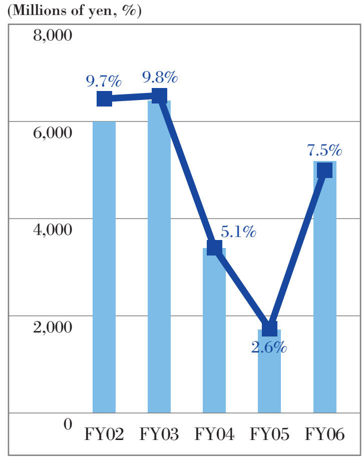
(Millions of yen, %)



■ Net Sales
— Operating Income Margin

NET INCOME AND ROE

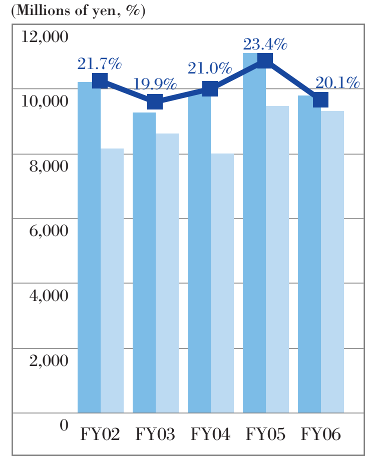
(Millions of yen, %)



■ Net Income
— ROE

ADVERTISING EXPENSES AND SALES PROMOTION EXPENSES

(Millions of yen, %)



■ Advertising Expenses
■ Sales Promotion Expenses
— Ratio of Advertising and Sales Promotion Expenses to Net Sales

TO OUR SHAREHOLDERS AND OTHER STAKEHOLDERS

I was appointed President three years ago just as FANCL reported its first-ever year of lower sales and earnings. It was a challenging time. In response, we began implementing FANCL Change & Challenge (CC) Plan Phase 1, a medium-term management plan designed to arrest this downturn and drive a recovery in growth and profitability. Progress and reform have generally been in line with our objectives since the plan's launch two years ago, providing the foundations for our next step forward.

FISCAL 2006 RESULTS

In fiscal 2006, ended March 31, 2006, consolidated sales increased 8.4% to ¥95,322 million, buoyed by higher sales of cosmetics and nutritional supplements. Operating income jumped 57.9% to ¥8,575 million, reflecting a strong performance in the high-margin Cosmetics Business, and significantly narrower losses in the Other Businesses. Net income more than tripled to ¥5,184 million.

The year-on-year growth in consolidated sales of ¥7.4 billion was primarily due to cosmetics and nutritional supplements. Cosmetics provided ¥4.2 billion of the increase thanks to the launch of revamped products and other factors. Nutritional supplements generated ¥2.1 billion of the rise due to strong demand for Co-enzyme Q_{10} and new products. The substantial increase in earnings mainly reflected stronger sales of high-margin cosmetics and more efficient use of advertising expenses. In the Other Businesses, some businesses are still not profitable, but they have significantly reduced their losses. As a result, overall, FANCL achieved top- and bottom-line growth and made steady progress during the year under review.

Kenji Fujiwara
C.E.O. and Representative Director

OUR PERFORMANCE IN FISCAL 2006

FACTORS AFFECTING SALES

Consolidated sales increase ¥7.4 billion (8.4%) year on year

(Billions of yen)

Positive factors

- FANCL cosmetics: +3.6
- ATTENIR cosmetics: +0.5
- Nutritional supplements: +2.1
- Kale juice: +0.5
- IIMONO OHKOKU: +1.2

Negative factors

- Germinated brown rice: –0.4
- Sundries, undergarments and others: –0.1

FACTORS AFFECTING OPERATING INCOME

Operating income increases ¥3.1 billion (57.9%) year on year

(Billions of yen)

Positive factors

- Increased sales: +2.6
- Lower marketing expenses: +1.5
- Cost reductions: +0.9

Negative factors

- Deteriorating margins in nutritional supplements due to rising costs: –1.2
- Higher store-related expenses: –0.7

FANCL CHANGE & CHALLENGE PLAN PHASE 1: PROGRESS REPORT

The FANCL Change & Challenge (CC) Plan Phase 1 covers the period from fiscal 2005 to fiscal 2007. This plan is designed to engineer a transition from a company led by FANCL's founder to one managed under a more expansive organizational setup. The CC Plan was also initiated to restore profitability and growth. To achieve these goals, we worked to put the sluggish Cosmetics Business back onto a growth trajectory in terms of sales and customer numbers, and to ensure Other Businesses began to generate earnings.

Concrete steps included creating a unified organization capable of responding to changes in the marketplace by upgrading the company's organizational framework, optimally allocating human resources and reforming the corporate culture. We also positioned the retail store sales channel as an area to reinforce as part of efforts to strengthen distribution channels, and worked to overhaul our marketing strategy.

These efforts have paid off. We have seen a steady improvement in performance in the Cosmetics Business driven by the launch of renewed products, while sales at existing retail stores are now growing year on year. Reflecting a steady increase in active mail-order customers and other factors, the number of customers for FANCL-branded cosmetics has recovered to a level last seen in fiscal 2000—when we posted record-high sales.

However, sales in the Germinated Brown Rice and Kale Juice businesses fell short of targets in the first year of CC Plan Phase 1, forcing us to lower our goals for the plan's final year. We are making progress in stemming losses by cutting costs, but we still have to resolve a number of remaining issues. We anticipate that it will be some time yet before these businesses are profitable.

With CC Plan Phase 1, we have achieved a recovery in our core businesses. Sales and earnings are on an upward trend as a result. But, to further strengthen our organizational framework and secure sustained earnings, we have started implementing CC Plan Phase 2, covering the period from fiscal 2007 to fiscal 2009.

FANCL CHANGE & CHALLENGE PLAN PHASE 2: TARGETS AND OVERVIEW

The first year of CC Plan Phase 2 overlaps with the last year of Phase 1. This approach is designed to ensure we derive maximum benefit from the successes now emerging in Phase 1. CC Plan Phase 2 is also intended to resolve any outstanding issues from Phase 1 and ensure we have clearly defined our growth path. Aiming to deliver sustained earnings growth, we will roll out new products to expand sales and boost profits.

Launching products that establish new market positions for FANCL will be vital to growth. In Phase 2, therefore, we will further enhance our lineup of preservative-free cosmetics by offering more functional products underpinned by solid scientific research. In Nutritional Supplements, we plan to cultivate new market segments, focusing more on customers in their 50s and above. This, together with steps to enhance our overseas presence and expand web-based sales, will support efforts to achieve growth in market segments where FANCL has not been active until now.

We have three specific strategies: enhance product development capabilities, strengthen distribution capabilities and reinforce the operating base. Based on these strategies, we are aiming to boost sales of more appealing products through stronger sales channels and the strategic use of advertising. In parallel, we will work to expand our presence in overseas markets. Additionally, we will deploy and establish an enterprise resource planning (ERP) system in order to create a robust operating base to support sustained growth.

We are targeting record sales and earnings for FANCL in the plan's final year, fiscal 2009. Concrete goals are operating income of ¥15.0 billion on consolidated sales of ¥115.0 billion, ROA of 15% and ROE of 10%.

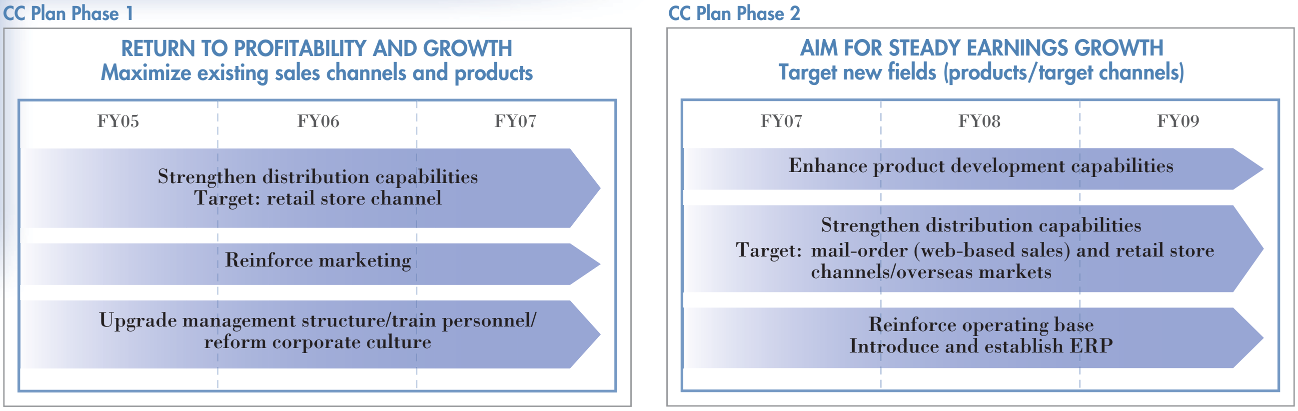
REINFORCING FANCL'S OPERATING BASE

We have almost completed upgrading the company's organizational framework and optimally allocating human resources, two of the goals of CC Plan Phase 1. Even before we started implementing this plan, FANCL boasted a strong array of resources, including superior products, a retail store network, sales expertise and highly motivated employees. However, we still do not have the framework in place to focus these resources on a unified objective and organically knit them together to generate synergies. Going forward, we need to make more progress in creating a framework to effectively leverage these resources to support sustained growth.

That's why, in Phase 2, we will push forward with the introduction of an ERP system to reinforce the operating base and conduct business activities more efficiently. This will involve optimizing logistics sites and utilizing a supply chain management (SCM) system covering all aspects of the value chain, including production, logistics and sales. Guided by a well-defined business strategy, this will support solid operational execution, helping us to sustain rising sales and earnings.

OVERVIEW OF CC PLAN PHASE 1 AND PHASE 2

CC Plan Phase 1 | CC Plan Phase 2

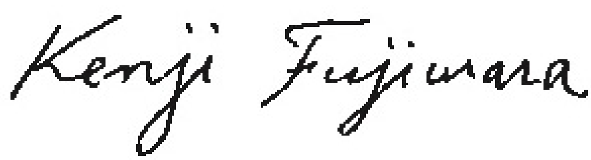


RAISING SHAREHOLDER VALUE AS A TRUSTED COMPANY

To win and retain the trust of shareholders and all other stakeholders—who are vital to our corporate activities—we are working to maintain and augment our corporate governance structure. Specifically, we have introduced an executive officer system to ensure the separation of the supervisory and executive functions of management, appointed outside directors to increase the transparency of the Board of Directors, conducted rigorous compliance, and implemented a system to strictly manage personal information. Moreover, in June this year, we appointed an additional outside director to further increase management transparency and revised the remuneration system for directors and corporate auditors, including abolishing the retirement allowance system.

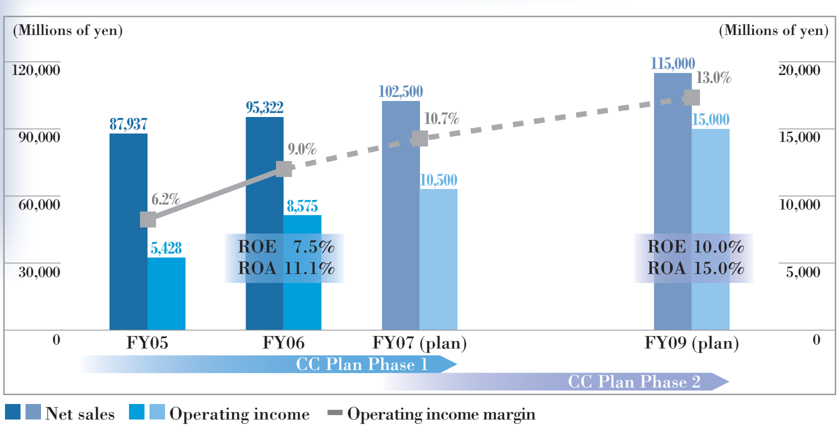
At FANCL, we give priority to returning greater profits to shareholders over the long term. Consequently, we plan to organically combine increases in the dividend, stock splits and share buybacks to return more profits to shareholders going forward.

Although FANCL's performance has stalled in the last few years, we are poised to make the jump to the next phase of growth. Leveraging our unique products, high customer service levels and other strengths, we will actively work to open up new markets to become a company capable of delivering sustained growth. With your continuing support, I hope to be able to report to you a record year of earnings for FANCL in three years' time.



Kenji Fujiwara
C.E.O. and Representative Director
August 2006

CC PLAN PHASE 1 PROGRESS REPORT AND PHASE 2 TARGETS



ENHANCING PRODUCT DEVELOPMENT

STRENGTHENING SALES CAPABILITIES

REINFORCING OUR BUSINESS BASE

STAYING TRUE TO OUR VISION

Back to Basics to Take on New Challenges

In fiscal 2005, we began implementing the FANCL Change & Challenge (CC) Plan Phase 1, incorporating reforms aimed at driving a recovery in growth and profitability.

Building on the successes of Phase 1, we started rolling out CC Plan Phase 2 in fiscal 2007. The central theme of Phase 2 is to secure sustained earnings by enhancing product development capabilities, strengthening distribution capabilities and reinforcing the operating base.

DELIVERING HIGH-QUALITY MANAGEMENT

▶ Aiming for Record Sales and Earnings in Fiscal 2009

With Phase 2, we are targeting higher sales and earnings in every year of the plan, culminating in operating income of **¥15.0 billion** on consolidated sales of **¥115.0 billion**, ROA of **15%** and ROE of **10%** in the plan's final year.

▶ Targeting Further Growth in Core Businesses and Profitability in Other Businesses

We are aiming to generate further growth in our core Cosmetics and Nutritional Supplements businesses by launching new competitive products to boost earnings. In Other Businesses, we plan to strengthen distribution capabilities to rapidly achieve profitability in the Germinated Brown Rice and Kale Juice businesses.

▶ Realizing Sustainable Growth

We will deploy an ERP system and invest ¥6.0 billion over three years to build an integrated SCM system covering all aspects of the product value chain. Through these systems, we will strengthen our corporate structure by creating a business base to support sustained growth over the long term.

ENHANCING PRODUCT DEVELOPMENT

FANCL Change & Challenge Plan Phase 1: Progress Report

Under the FANCL Change & Challenge (CC) Plan Phase 1, we have sought to achieve a recovery in earnings and growth by energizing existing product lines. Our aggressive product renewal campaign contributed to sales growth in fiscal 2006.

Cosmetic Product Renewals Drive Business

In our line of cosmetics we have three skin care brands—FENATTY, EVANTÉ and CLEARTUNE—that we are gradually uniting under a single FANCL brand. In August 2005, we combined each of these three brand's different facial washing powder products into a single FANCL Facial Washing Powder. Following this move, sales climbed 1.5 times compared to before the renewal, showing that our product strategy is heading in the right direction. Sales of *Mild Cleansing Oil*, which underwent a product renewal in fiscal 2004, and *Beauty Concentrate*, a new product containing a proprietary anti-aging ingredient, also sold well.

Stronger Lineup of Products Containing Proprietary Ingredients in Nutritional Supplements Business

In fiscal 2006, we followed our CC Plan in introducing new mineral supplement products containing Twintose, our proprietary mineral absorption enhancer, *HTC Collagen* containing a proprietary agent, and *Bright Age EX*, which contains the same anti-aging agent as *Beauty Concentrate*. All these products performed well in fiscal 2006.

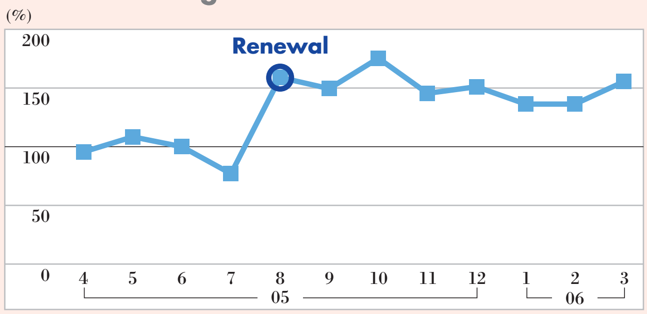
Competition is intensifying, so we are promoting a high-value-added strategy based on proprietary ingredients and technology.

Offering Flavorsome Products High in Nutritional Value in Other Businesses

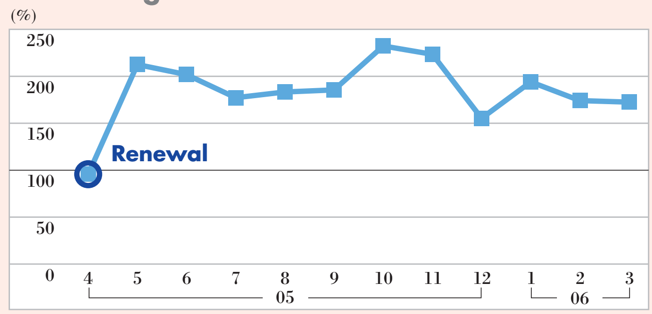
In fiscal 2006, we launched a new product in the Germinated Brown Rice Business that removes half of the bran of brown rice to bring it closer to white rice in flavor. We are using this product to approach new customer segments. In the Kale Juice Business, the newly introduced powdered kale juice with Twintose was favorably received in the market. We also launched a high-value-added frozen kale juice, *Super Kale Juice Twintose Formula*.

Year-on-year Sales Trends for Renewed Products (Cosmetics and Nutritional Supplements)

Facial Washing Powder



HTC Collagen



CC PLAN PHASE 2 STRATEGY

In CC Plan Phase 1, we targeted sales expansion through such measures as the introduction of renewed products and the reinforcement of sales capabilities. In the plan's second phase, we aim to achieve sales growth by strengthening product development to bring highly original and functional new products to market. Preparations have been completed in terms of human resources. We have already secured highly experienced personnel in the product planning and research and development fields to assist this drive, and we are now moving ahead with our sights focused on products with strong market appeal.

CC Plan Phase 2 Strategy Targets

Net Sales (Millions of yen)

	FY06	FY09 (plan)	Increased amount
Cosmetics	41,287	*50,000*	8,713
Nutritional supplements	33,246	*40,000*	6,754
Others	20,789	*25,000*	4,211
Total	95,322	*115,000*	19,678

Operating Income (Loss) (Millions of yen)

	FY06	FY09 (plan)	Increased amount
Cosmetics	5,568	*8,900*	3,332
Nutritional supplements	5,405	*7,000*	1,595
Others	(762)	*1,000*	1,762
Total	8,575	*15,000*	6,425

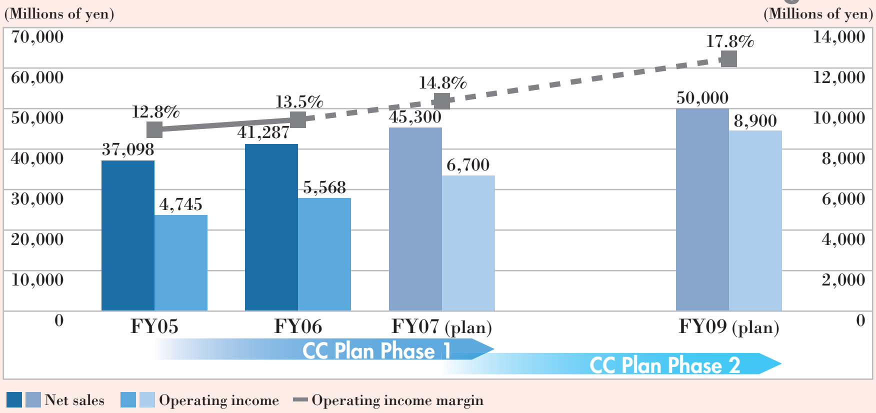
Operating Income (Loss) Margin (%)

	FY06	FY09 (plan)	Increased amount
Cosmetics	13.5	*17.8*	4.3
Nutritional supplements	16.3	*17.5*	1.2
Others	(3.7)	*4.0*	7.7
Total	9.0	*13.0*	4.0

COSMETICS

Capturing Greater Market Share Through Brand Reorganization

COSMETICS BUSINESS: Performance and Fiscal 2009 Targets



Market Recognition and Product Positioning

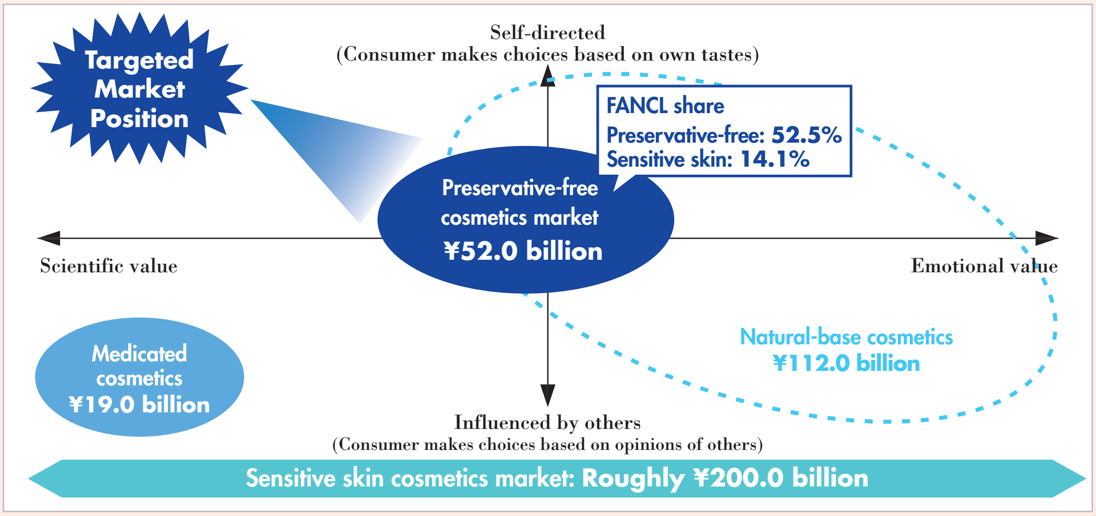
The sensitive skin cosmetics market, which did not exist until FANCL launched its first preservative-free cosmetic products, is now estimated to be approximately ¥200 billion in size. Starting around 2000, numerous competitors entered the market and the FANCL brand steadily became lost in a sea of preservative-free and natural brands. FANCL's market share currently stands at 14.1%, but we now plan to boost our share further by introducing highly functional products backed by scientific evidence.

Based on this strategy for the sensitive skin market, we are targeting consolidated sales of ¥50 billion and an operating income margin of 17.8% in three years' time.

Product Launch Plan

To capture a larger market share, we have to introduce competitive products. In the past, we have relied on the "kind on the skin, preservative-free" approach. However, circumstances call for a change. Under our

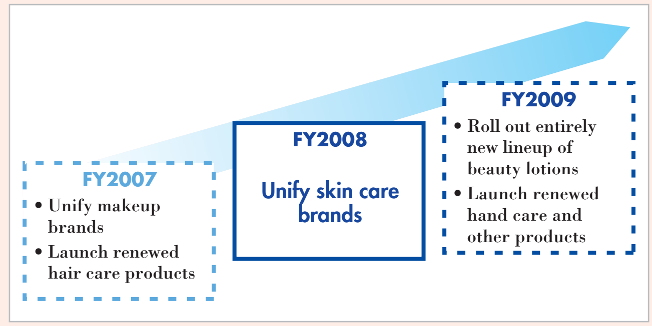
FANCL COSMETICS: Market Positioning



Source: Fuji Keizai Co., Ltd., 2004 base new product launch plan, we are developing cosmetics that customers can tangibly feel to be effective, based on the concepts of "preservative-free, natural and freshly made," as well as "highly functional."

There are three stages to the plan. In the first year, we will introduce renewed products for our hair care and makeup lines. Our focus in the second year will be the reorganization of our core skin care brands by unifying FENATTY, EVANTÉ and CLEARTUNE under a single FANCL brand, and channeling our resources into building brand recognition. In the final year, we plan to revise our beauty lotion, hand care, and other product lines.

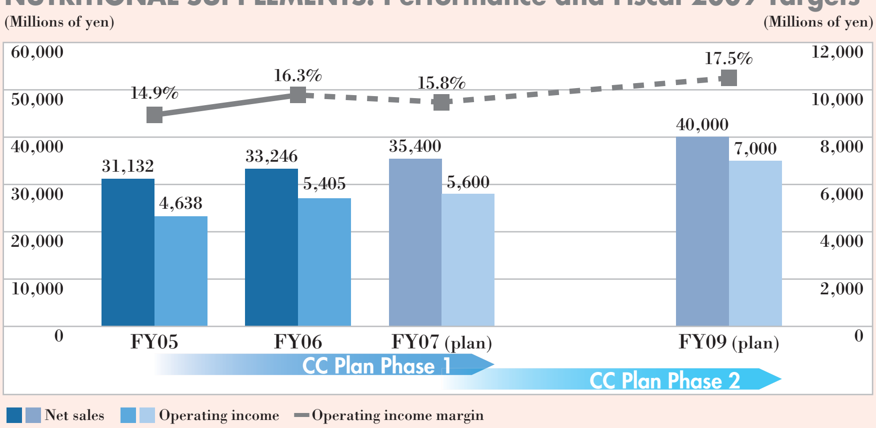
FANCL COSMETICS: Product Launch Plan



NUTRITIONAL SUPPLEMENTS

High-Value-Added Ingredients and Market Expansion

NUTRITIONAL SUPPLEMENTS: Performance and Fiscal 2009 Targets

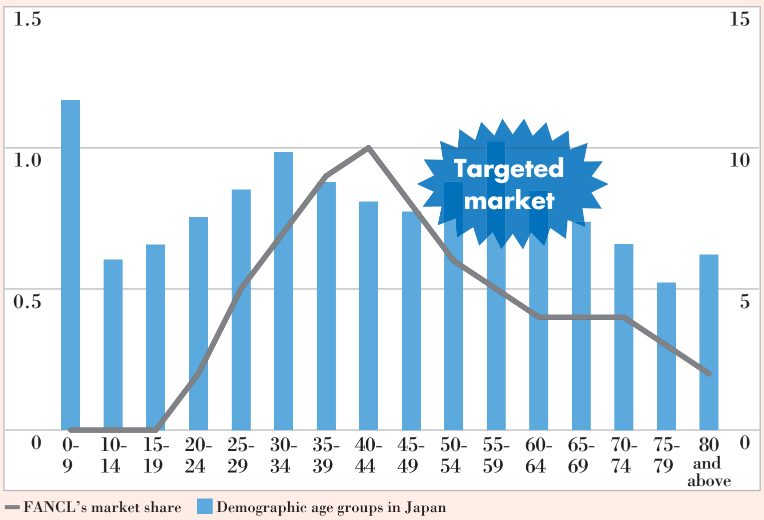


Current Position

Reflecting the health boom over the past few years, the nutritional supplement market has grown, but there are many companies in the market, resulting in extremely competitive conditions.

Our nutritional supplements are targeted primarily at women in their 30s to 40s. This emphasis is confirmed by the demographics—our share of the 30s to 40s market is high while our share of the 50s to 60s market is comparatively low. People in their 50s to 60s usually have personal health concerns and are generally more economically comfortable. Consequently, this is a

NUTRITIONAL SUPPLEMENTS: Mail-order Customers by Age Group

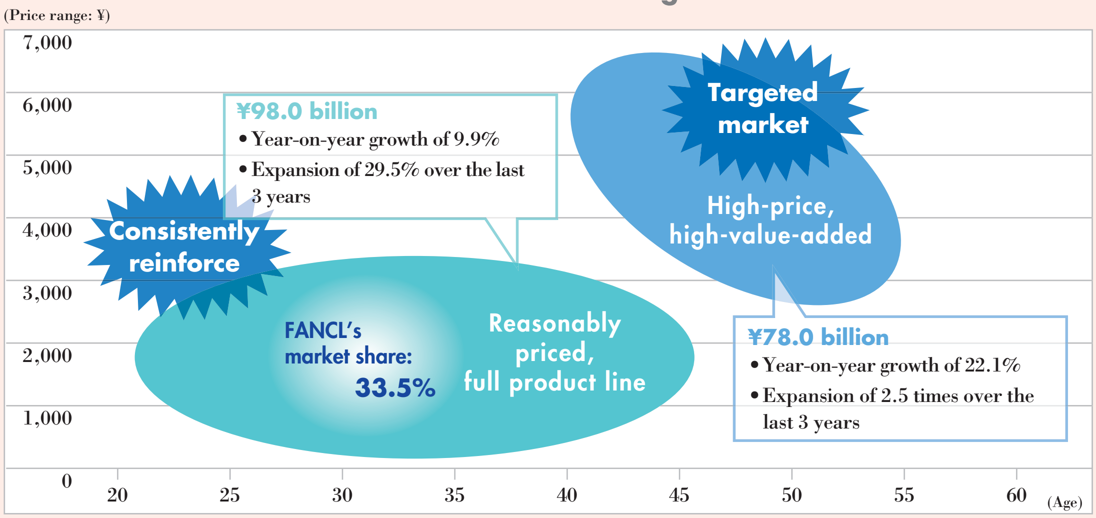


market we should target going forward, and we view the 50s to 60s segment as an essential element of our drive to capture a greater share of the overall market.

Strategies

The FANCL brand is positioned as a reasonably priced, full-line brand in the nutritional supplement market. One of the special features of this section of the market is intense competition that makes it easy to get embroiled in price competition. In light of this, in CC Plan Phase 2, we are seeking to avoid price competition and build sales by developing the high-price, high-value-added market focused on older consumers. The size of this market is still a little under ¥80 billion, but it has expanded rapidly, growing 2.5 times over the past three years. Clearly, there is still plenty of room for further growth. At the same time, we will continue to strengthen our sales of beauty products, such as beauty supplements and diet supplements mainly for women in their 30s, aiming to increase our share of the reasonably priced full-line market.

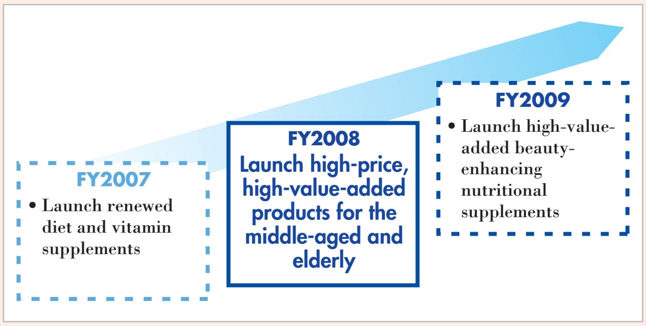
NUTRITIONAL SUPPLEMENTS: Market Positioning



Source: Total Planning Center Osaka, forecasts for 2006

Based on this strategy, we are targeting consolidated sales of ¥40 billion and an operating income margin of 17.5% in the Nutritional Supplements Business three years from now.

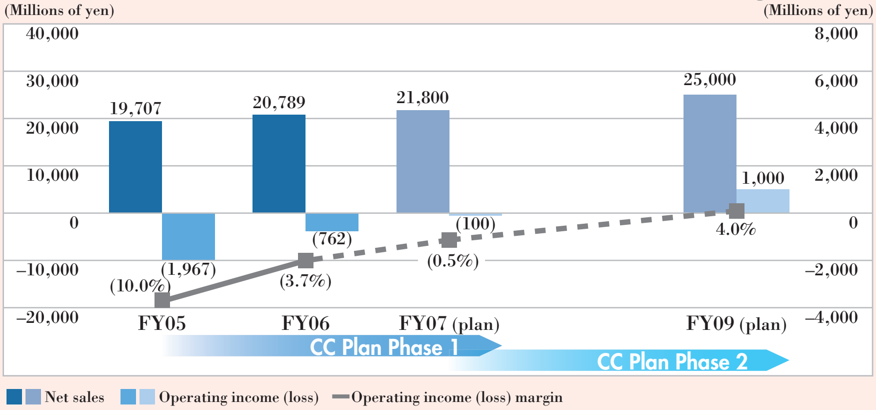
NUTRITIONAL SUPPLEMENTS: Product Launch Plan



OTHER BUSINESSES

Achieving a Quick Turnaround by Strengthening Products

OTHER BUSINESSES: Performance and Fiscal 2009 Targets



Recent Performance

Losses in Other Businesses had been ballooning until the fiscal year under review, when we successfully stemmed losses. Concentrating on strengthening our sales capabilities and the appeal of our products, we will continue efforts to improve profitability and move into the black in fiscal 2009.

Reinforcing Individual Product Strategies

In our Germinated Brown Rice Business, we are aiming to achieve profitability over the next three years by strengthening sales of *Delicious Germinated Brown Rice–Fluffy White Rice Style* and expanding our lineup of foods with germinated brown rice additives. In our Kale Juice Business, we will introduce high-margin powdered-type products and shift to high-value-added products in frozen kale juice containing Twintose, our proprietary mineral absorption enhancer. In other areas, our IIMONO OHKOKU (Kingdom of Wonderful Things) Mail-order Business moved back into the black in the fiscal year under review. Our next target in this business is to grow sales and profits further by improving the appeal of the products we offer.

STRENGTHENING SALES CAPABILITIES

FANCL Change & Challenge Plan Phase 1: Progress Report

Our fiscal 2006 goals under the CC Plan were to review marketing strategy and strengthen sales capabilities, particularly in our retail store network. Efforts to reinforce marketing led to an increase in the number of mail-order customers, while bolstering our retail store network by reenergizing the operations of existing stores and opening new stores also led to increased sales.

Mail-order Sales (Including Web-based Sales)

In fiscal 2006, the benefits of efforts to strengthen marketing under CC Plan Phase 1 were evident in the growth of active customers, particularly with our FANCL cosmetics. As of March 31, 2006, the number of FANCL cosmetics mail-order customers totaled 734,161, driving sales to a level last seen in fiscal 2000—our historical high. Mail-order sales accounted for 60.0% of these sales.

Retail Store Sales

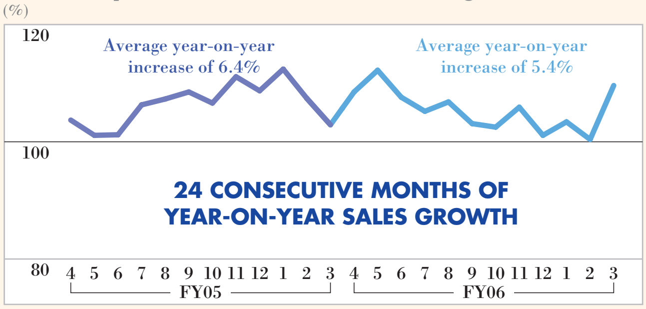
There was substantial growth in retail store sales for the second consecutive year. In addition, the contribution of retail stores to overall net sales climbed to 24.8% from 20.8% in fiscal 2004.

We have concentrated on revamping existing stores, emphasizing tangible areas, such as visual appearance and layout, and intangible aspects, such as the compensation structure for employees and the introduction of a supervisor system. As a result, existing stores continued their recent success, improving on last year's sales performance and posting 24 consecutive months of sales growth since April 2004. We are now planning to build a retail store network of 300 stores by the end of fiscal 2009, continuing a store opening program that has seen 65 new stores created over the last two years.

Wholesale Sales

Given the evolution of our business based primarily on mail-order sales, we recognize our lack of know-how in the highly competitive wholesale market. Guided by the CC Plan, we have focused on rapidly gaining strategic capabilities by hiring wholesale specialists. Among other measures, we revised our sales system that relied excessively on wholesale clients, and created shelf-allocation proposals using more precise store data collection and analysis. Illustrating the success of our efforts, wholesales have consistently contributed more than 10% of net sales over the last three years.

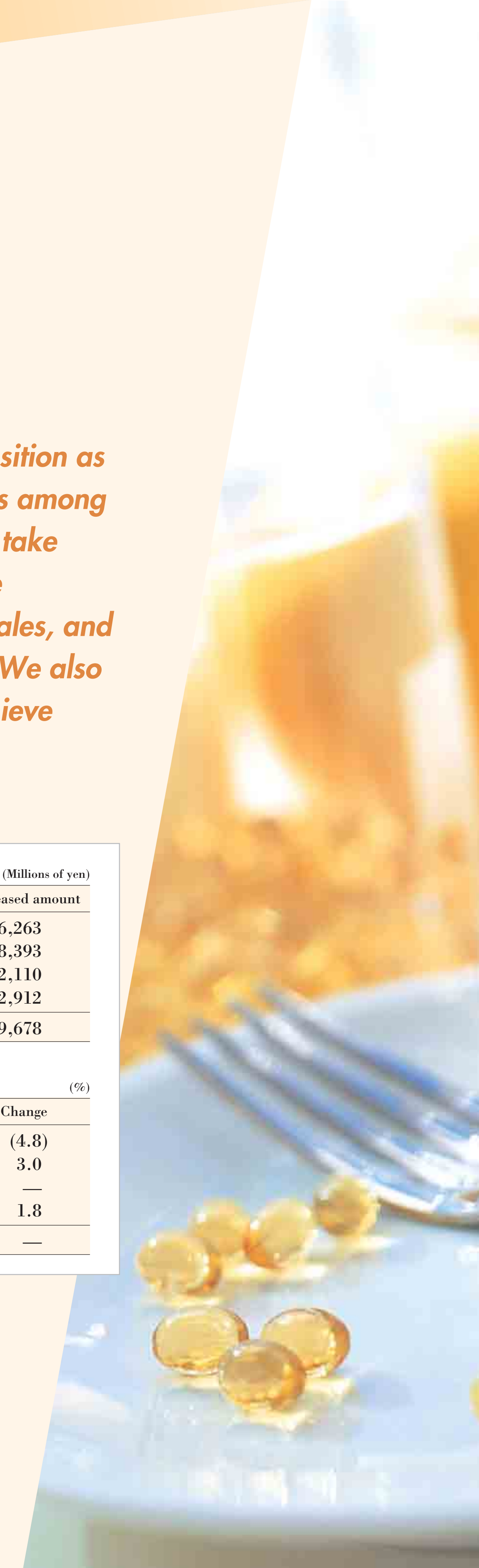
Year-on-year Performance at Existing Retail Stores



Existing retail stores: open for 13 months or longer, including stores that have changed format or been refurbished.

CC PLAN PHASE 2 STRATEGY

In CC Plan Phase 2, we are aiming to leverage our position as a multiple sales channel company to capture synergies among our three different sales channels, while continuing to take advantage of their respective characteristics. We have positioned mail-order sales, centered on web-based sales, and retail store sales as distribution routes for expansion. We also are seeking to develop overseas sales channels to achieve further growth through regional expansion.



CC Plan Phase 2 Strategy Targets by Sales Channel

Net Sales (Millions of yen)

	FY06		*FY09 (plan)*	Increased amount
Mail-order sales	57,237	**Mail-order sales**	*63,500*	6,263
Retail store sales	23,607	**Retail store sales**	*32,000*	8,393
Wholesales sales	10,390	**Wholesale sales**	*12,500*	2,110
Overseas · Other	4,088	**Overseas · Other**	*7,000*	2,912
Total	95,322	**Total**	*115,000*	19,678

Share of Net Sales (%)

	FY06		*FY09 (plan)*	Change
Mail-order sales	60.0	**Mail-order sales**	*55.2*	(4.8)
Retail store sales	24.8	**Retail store sales**	*27.8*	3.0
Wholesale sales	10.9	**Wholesale sales**	*10.9*	—
Overseas · Other	4.3	**Overseas · Other**	*6.1*	1.8
Total	100.0	**Total**	*100.0*	—

SALES CHANNEL SYNERGIES

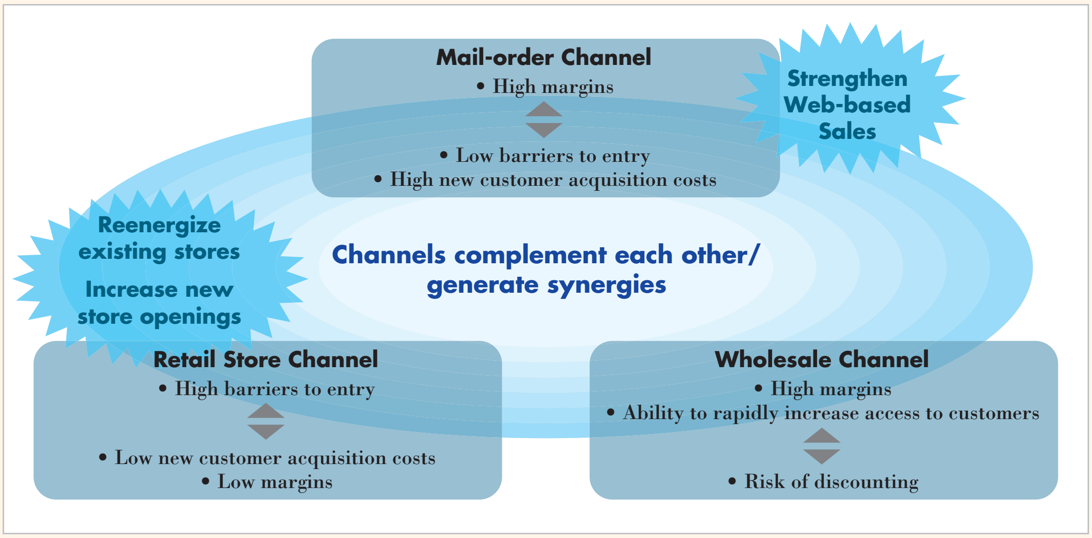
Attracting More Customers by Leveraging the Unique Characteristics of Three Different Sales Channels

FANCL boasts a multiple channel sales system comprised of mail-order, retail store, and wholesale sales. These sales channels all interact with and complement each other, generating synergies.

The mail-order format is a highly convenient sales channel for customers, but physically examining items before buying them is obviously not an option. Despite mail-order sales being a highly profitable sales channel, the cost of attracting new customers is steadily growing. Conversely, retail stores sales have relatively low profitability, but the costs of acquiring new customers are also low. In addition, from the perspective of consumers, products can be picked out by hand, and knowledgeable store staff are available to help with selection. Wholesale sales also have their advantages and disadvantages; profitability may be high, but the risk of discounting could damage brand value.

In CC Plan Phase 2, we are working to accurately understand these different characteristics and utilize them to develop complementary benefits and synergies. We are achieving this by further enhancing the

Distribution Channel Strategy



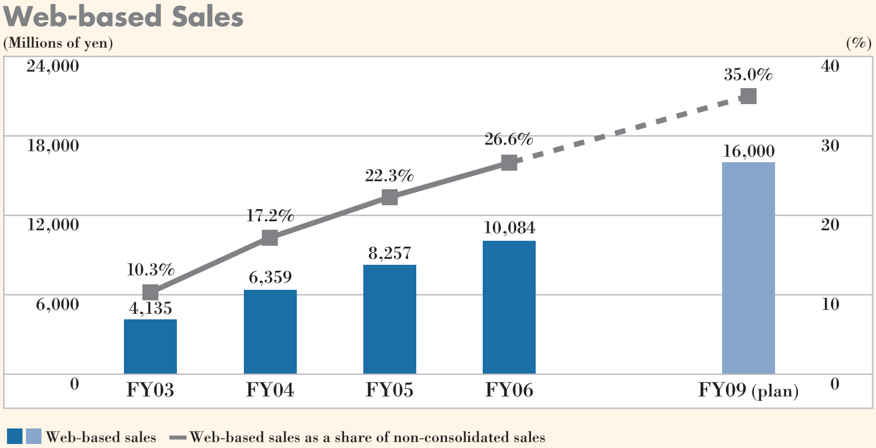
strengths of each sales channel and then using them to compensate for weaknesses in other channels. We also recognize that advertising is indispensable for increasing synergies between channels. Taking into account factors such as cost-effectiveness, advertising, brands, and target customer segments, we have chosen the optimum advertising media for each sales channel to heighten our presence in individual channels and ensure advertising translates into sales growth. Under CC Plan Phase 2, we are putting particular focus on reinforcing web-based sales and retail store sales and on developing overseas markets.

WEB-BASED SALES

Internet purchases of our products have grown rapidly, especially among the 25 to 30 age group. In the fiscal year under review, web-based sales topped ¥10 billion. With the opening up of the remaining sections of the broadcast spectrum in Japan to mobile terrestrial digital broadcasting such as "One Seg," we are expecting exciting new developments in the market. In preparation, we are building up our infrastructure during fiscal 2007 by expanding and upgrading transaction processing capabilities and upgrading security. We also are planning to expand sales by boosting customer satisfaction through additional services, such as web-based skin or health checks and digital catalogs. Currently, roughly 25% of FANCL's nonconsolidated mail-order sales are derived from the Internet. Within three years, we aim to boost this figure to 35%.

Overall, our goal in CC Plan Phase 2 is to expand mail-order sales by 10.9%, to ¥63.5 billion in fiscal 2009, up from ¥57.2 billion in the fiscal year under review.

Web-based Sales



RETAIL STORE SALES

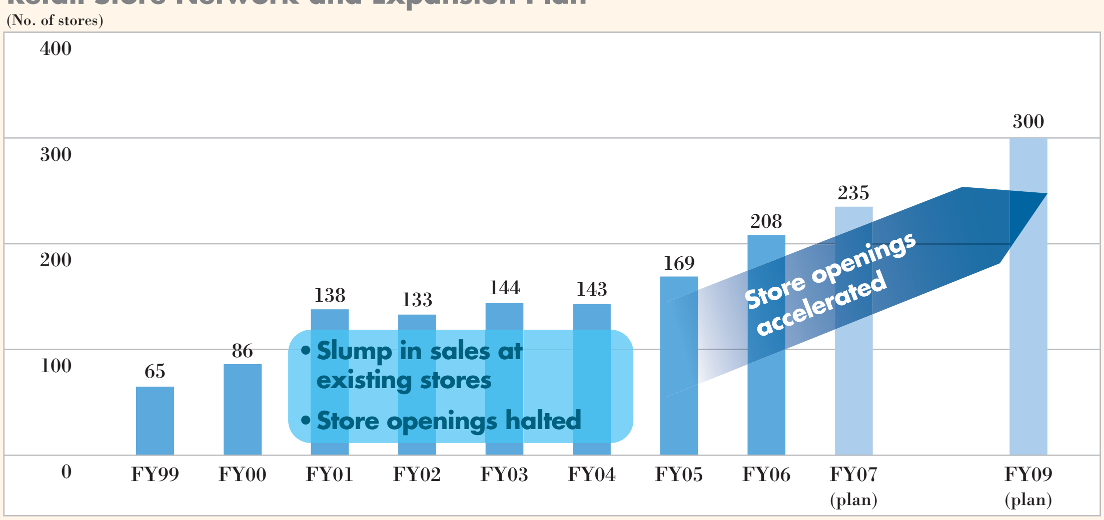
Fancl House, SOGO Yokohama store

Fancl House J, Rinku Sennan store

Retail store sales were positioned as one of the sales channels for expansion under CC Plan Phase 1. Consequently, we have been implementing measures to revitalize sales at existing retail stores as well as opening new stores. In Phase 2 of the plan, we are continuing this emphasis, targeting the building of a 300-store network by the end of fiscal 2009. Our initial target for creating this network was the end of fiscal 2007, but we decided to push back this date by two years after shifting our approach: we are now focusing on a more gradual high-quality store opening program that puts greater emphasis on training highly skilled store staff.

We are aggressively opening retail stores in the Tokyo metropolitan area, the Kinki region and in regional cities. Our plan is to open these retail stores in department stores, shopping malls and railway station buildings. To improve service quality, we are further increasing the level of training for store staff, aiming to have 160 inner and outer beauty advisors in place throughout the retail store network. Average purchase amounts at retail stores with inner and outer beauty advisors are 18% higher than those without, while the number of customers who return to the store is 1.1% higher. Our target under CC Plan Phase 2 is to reach retail store sales of ¥32.0 billion in fiscal 2009, an increase of 35.6% compared to the ¥23.6 billion in the year under review.

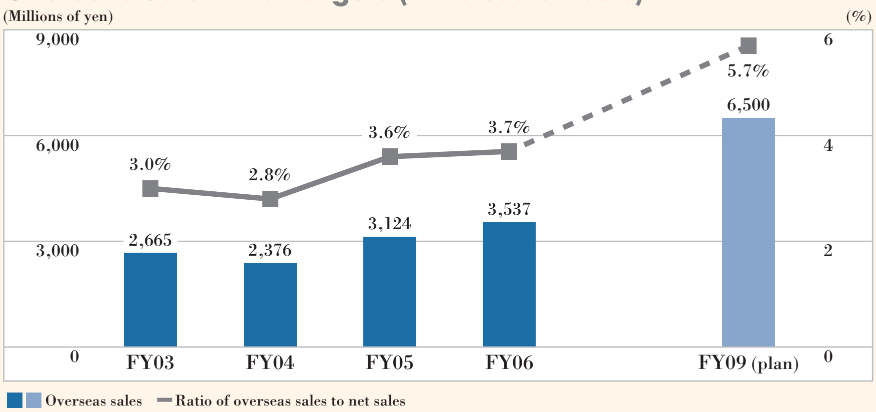
Retail Store Network and Expansion Plan



OVERSEAS SALES

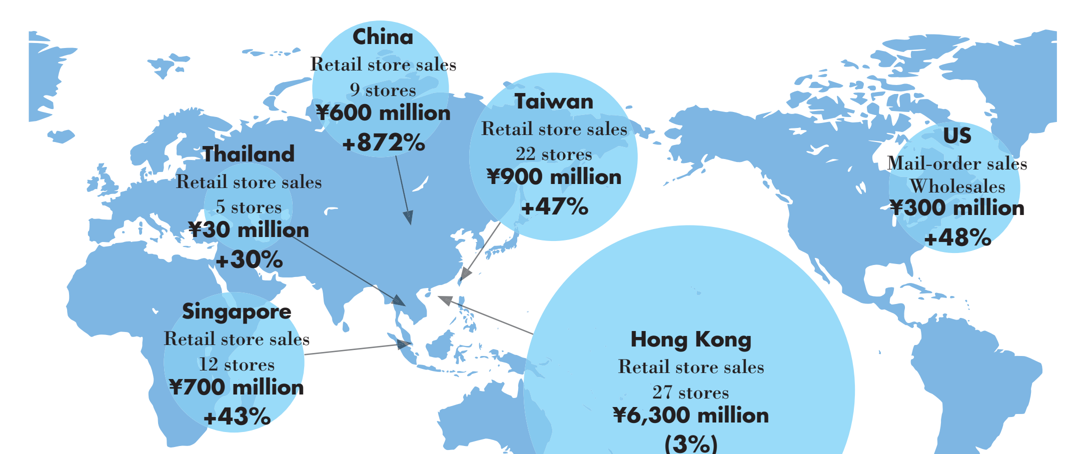
Strategically Reinforce Operations in China to Generate Overseas Retail Sales of ¥16.0 Billion

Overseas Sales and Targets (Wholesale basis)



Overseas sales are another sales channel singled out for growth under CC Plan Phase 2. Currently, our overseas sales efforts are focused on Asia, primarily Hong Kong, and the United States. However, going forward, we plan to put greater emphasis on building a stronger presence in China. We first entered the Chinese market in September 2004, and operations are developing steadily. Department stores in Shanghai and Beijing feature around 20 famous cosmetic brands from around the world, but FANCL House sales still rank in the top five. The FANCL brand is particularly strong in Shanghai, with our sales in the Yohan and Parkson department stores taking the number one spot. At the end of CC Plan Phase 2 in three years' time, we are hoping to establish a 50-store network in mainland China with sales on a par with those of Hong Kong. On a local retail basis, overseas sales amounted to roughly ¥9.0 billion in the fiscal year under review (¥3.5 billion on a wholesale basis). Over the next three years, we aim to grow this figure to ¥16.0 billion (¥6.5 billion on a wholesale basis).

Global Expansion



Upper figure: Sales (local retail)
Lower figure: yoy increase/decrease

* Fancl dissolved its distribution agreement in Indonesia in May 2006.

REINFORCING OUR BUSINESS BASE

In CC Plan Phase 2, we are introducing an enterprise resource planning (ERP) system to manage all aspects of our operations, such as logistics and inventory management. Utilizing the ERP system, we will initiate supply chain management (SCM) to control our inventories by integrating all aspects of the value chain including production, logistics, sales and end users. Through these systems, we will strengthen our corporate structure by creating a business base to support sustained growth over the long term.

Deploying ERP

Since its founding, FANCL has operated under the concepts of "products delivered fresh" and "preservative-free." Based on this approach, the date of manufacture is shown on all our products. Although most of our products reach customers within a month of production, a broader product line and our move into other sales channels such as retail stores and wholesales outside our traditional mail-order sphere have made it more difficult to deliver products while they are still fresh.

For that reason, we decided to introduce an ERP system. Using this system, we aim to remain on top of inventories in real time and optimize our distribution points. In April 2006, we got started by initiating the accounting module of the ERP system. The production and sales elements of the system are scheduled to go online in April 2007. Over a three-year period, we plan to invest a total of ¥6.0 billion in implementing the entire system.

Capital Expenditure Plan for the Next Three Years

(Millions of yen)

	FY07	FY08	FY09
IT	2,800	1,600	1,600
Stores	1,100	800	1,000
Plants/Other	2,100	1,800	1,500
Total	6,000	4,200	4,100

Enhancing Customer Satisfaction

The ERP system will allow us to better understand conditions and issues in each process in real time, enabling more rapid responses. This capability will also lead to reductions in inventories, defective products, and waste. We plan to firmly establish the ERP system within a three-year period, and build an organization that can deliver our products to customers within two weeks. Achieving this time frame for delivery will also make it possible for FANCL to use ingredients that could not be used before because of their tendency to decay. The heightened traceability of our products will also increase quality control and contribute to greater customer confidence in our products. Raising the bar on customer satisfaction will help us to further expand sales.

AT A GLANCE

	NET SALES, OPERATING INCOME (LOSS) AND OPERATING INCOME (LOSS) MARGIN	SALES CHANNEL BREAKDOWN

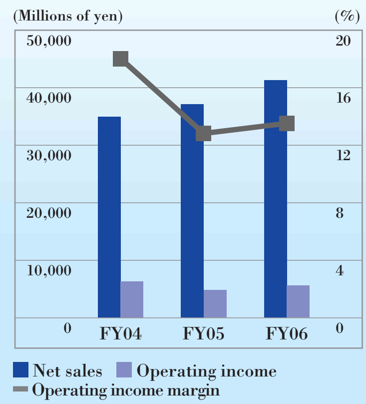
COSMETICS BUSINESS

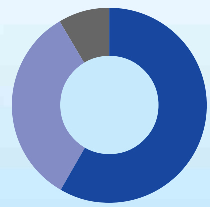
43.3%

OF TOTAL NET SALES

PRODUCTS

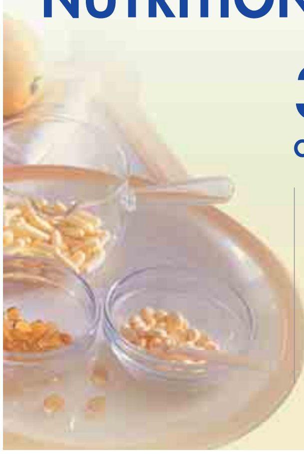
- FANCL cosmetics (Preservative-free cosmetics that contain no ingredients known to cause skin allergies)
- ATTENIR cosmetics (Attractive, quality cosmetics at reasonable prices)





- Mail-order sales 58.3%
- Retail store sales 33.2%
- Other 8.5%

NUTRITIONAL SUPPLEMENTS BUSINESS

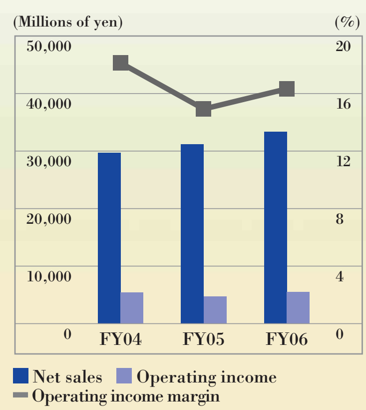


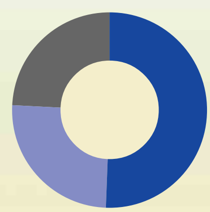
34.9%

OF TOTAL NET SALES

PRODUCTS

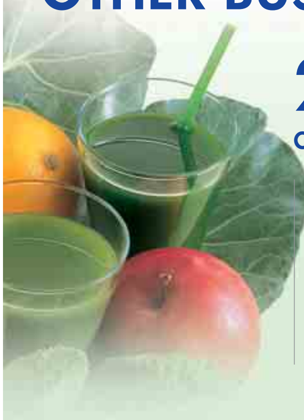
- Health supplements (High-quality nutritional supplements at competitive prices)
- Beauty supplements (Nutritional supplements for inner beauty)





- Mail-order sales 50.6%
- Retail store sales 25.2%
- Other 24.2%

OTHER BUSINESSES

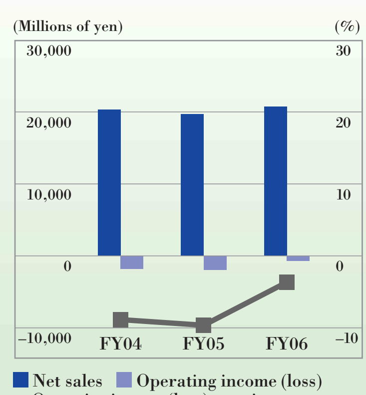


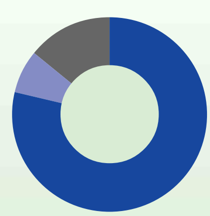
21.8%

OF TOTAL NET SALES

PRODUCTS

- Germinated brown rice
- Kale juice
- Comfort undergarments
- Health equipment and lifestyle goods





- Mail-order sales 78.7%
- Retail store sales 7.2%
- Other 14.1%

COSMETICS BUSINESS

COSMETICS BUSINESS PERFORMANCE AND TARGETS

	Millions of yen			
	2007 (plan)	2006	2005	2004
Net sales	*45,300*	41,287	37,098	34,926
FANCL cosmetics	*34,900*	31,406	27,759	26,370
ATTENIR cosmetics	*10,000*	9,518	9,042	8,147
Others	*400*	361	297	407
Gross profit	*33,700*	30,655	27,592	26,394
Selling, general and administrative expenses	*27,000*	25,087	22,847	20,111
Advertising expenses	*5,000*	5,464	5,073	3,932
Operating income	*6,700*	5,568	4,745	6,283
Operating income margin	*14.8%*	13.5%	12.8%	18.0%

	Customers		
	2006	2005	2004
Number of active customers* at fiscal year-end:			
FANCL cosmetics (Mail-order and retail store)	1,410,016	1,157,014	1,041,054
ATTENIR cosmetics (Mail-order and retail store)	453,290	432,200	372,679

** Active customers: Customers making at least one purchase during the preceding seven months.*

Fiscal 2006 Results

The Cosmetics Business posted increases in both sales and earnings during the year. Sales rose 11.3% year on year to ¥41,287 million, and operating income increased 17.3% to ¥5,568 million. The operating income margin, despite increases in advertising and sales promotion expenses, rose 0.7 of a percentage point to 13.5% from the previous fiscal year due to the increase in sales.

The two major brands in the Cosmetics Business are FANCL and ATTENIR. FANCL has been the company's main brand of preservative-free cosmetics since its establishment, while ATTENIR was launched in 1989 as a brand of attractive, quality cosmetics at reasonable prices. Sales of FANCL cosmetics increased 13.1% year on year to ¥31,406 million, while sales of ATTENIR cosmetics rose 5.3% to ¥9,518 million.

In terms of products, the Company focused on product development in FANCL cosmetics, emphasizing functionality in order to stimulate sales of skin care products. We renewed *Facial Washing Powder* in August 2005, and in December launched *Beauty Concentrate*, a beauty essence with a proprietary anti-aging agent. Sales of both of these products were strong. *Facial Washing Powder* had been sold under the FENATTY and two other brands. However, after unifying it under the FANCL name, sales have increased 1.5 times from pre-renewal levels. In ATTENIR cosmetics, sales of skin care and other products grew strongly, achieving record sales.

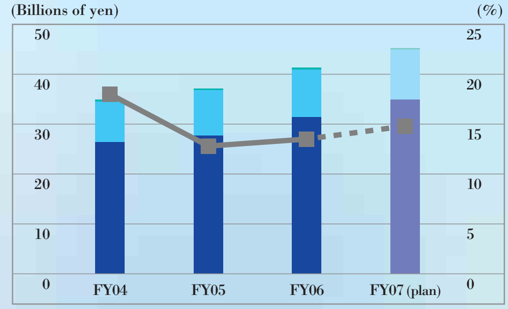
By sales channel, mail-order sales rose 5.4% year on year to ¥24,060 million. Retail store sales increased 19.4% to ¥13,721 million, due to continued strong existing-store sales, and the effect of new store openings. Other sales channels rose 26.2% to ¥3,504 million, with positive results from both overseas sales and convenience store sales.

FANCL
Facial Washing Powder

FANCL
Beauty Concentrate

ATTENIR
Inner Effector EX

COSMETICS BUSINESS NET SALES AND OPERATING INCOME MARGIN

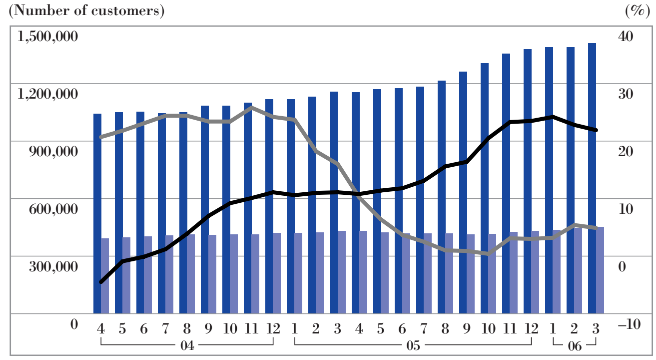


Fiscal 2007 Outlook and Strategies

In the Cosmetics Business, the Company will focus on the development of competitive products with enhanced functionality, in line with CC Plan Phase 2. During fiscal 2007, we are planning a renewal of makeup and hair care products in FANCL cosmetics. Until now, we have used preservatives in lipstick and certain other products to overcome coloration and other issues, but through research and development efforts we have now been able to make these products preservative-free. Based on this breakthrough, we are planning a renewal in August 2006. In addition, we expect continued strong sales of *Mild Cleansing Oil*, *Facial Washing Powder and Beauty Concentrate*. In ATTENIR cosmetics, we are expecting an increase in sales from a strengthening of marketing activities, such as television commercials and Internet promotions, and the renewal of skin-care products.

Forecasts for fiscal 2007 are net sales of ¥45.3 billion, operating income of ¥6.7 billion, and an operating income margin of 14.8%.

ACTIVE COSMETICS CUSTOMERS



NUTRITIONAL SUPPLEMENTS BUSINESS

NUTRITIONAL SUPPLEMENTS BUSINESS PERFORMANCE AND TARGETS

	Millions of yen			
	2007 (plan)	2006	2005	2004
Net sales	*35,400*	33,246	31,132	29,656
Gross profit	*23,100*	20,829	20,623	19,047
Selling, general and administrative expenses	*17,500*	15,424	15,985	13,676
Advertising expenses	*2,600*	1,835	3,291	2,501
Operating income	*5,600*	5,405	4,638	5,371
Operating income margin	*15.8%*	16.3%	14.9%	18.1%

	Customers		
Number of active customers* at fiscal year-end:			
Mail-order and Retail store	1,171,800	1,114,282	1,066,078

** Active customers: Customers making at least one purchase during the preceding seven months.*

Fiscal 2006 Results

The Nutritional Supplements Business also recorded an increase in both sales and earnings compared to a year earlier. Sales rose 6.8% year on year to ¥33,246 million, with operating income up 16.5% to ¥5,405 million. The operating income margin, despite a decline in the gross profit stemming from a rise in raw material costs for certain products, rose 1.4 percentage points to 16.3% from the previous fiscal year due to greater efficiency in terms of advertising and other expenses.

In terms of products, the nutritional supplements market has expanded as a result of the boom for such products as *Co-enzyme Q_{10}* and *Alpha Lipoic Acid*, though there has been a marked increase in competition. Sales of beauty supplements have been strong, including *HTC* Collagen*, launched in April 2005, which contains a proprietary agent, and *Bright Age EX*, launched in December and which includes the same anti-aging ingredients as used in our cosmetics. Ingredients for *Co-enzyme Q_{10}* could not be obtained in Japan, and overseas purchasing was one of the factors pushing up the cost ratio.

By sales channel, mail-order sales rose 0.7% year on year to ¥16,822 million. Retail store sales increased 17.0% to ¥8,393 million due to solid existing-store sales, and an increase in the number of FANCL House J stores, where nutritional supplements make up a high proportion of sales. Sales through other channels rose 10.8% to ¥8,030 million due to an increase in the number of distributors.

Fiscal 2007 Outlook and Strategies

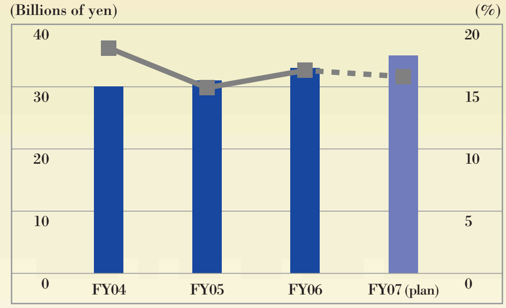
Customers for the Company's nutritional supplements include a higher percentage of people in their 30s and 40s compared to Japan's overall demographic structure, and a lower percentage in their 50s and 60s. In the

Bright Age EX

Alpha Lipoic Acid

HTC Collagen*

NUTRITIONAL SUPPLEMENTS BUSINESS NET SALES AND OPERATING INCOME MARGIN



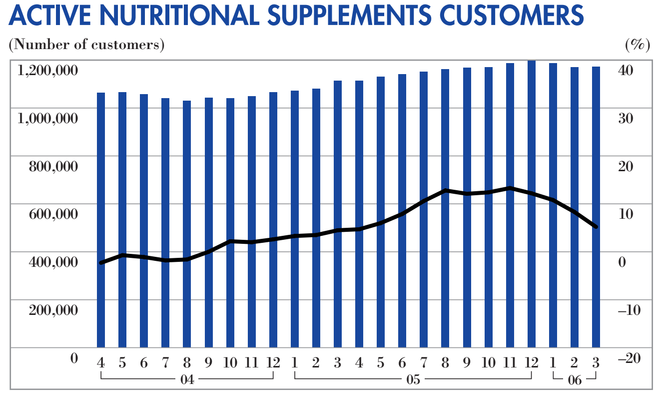
Net sales Operating income margin

Nutritional Supplements Business, in line with CC Plan Phase 2, the Company is enhancing development of higher-priced, high-value-added products targeting people in their 50s and 60s, currently the customer segment where our market share is lowest. In fiscal 2007, although we expect difficult business conditions to continue in the first half of the fiscal year due to factors such as increased competition and negative information regarding supplements in general, we expect a recovery in the second half thanks to an overhaul of Twintose-related products, a renewal of diet products, vitamins and beauty supplements—fields where we can effectively leverage our strengths, and the launch of new products. By sales channel, we are forecasting an increase in retail store sales due to the effect of new store openings, which we anticipate will drive sales higher in the Nutritional Supplements Business.

Forecasts for fiscal 2007 are net sales of ¥35.4 billion, operating income of ¥5.6 billion, and an operating income margin of 15.8%.

* HTC: *High Tripeptide Containing*

ACTIVE NUTRITIONAL SUPPLEMENTS CUSTOMERS



Number of active mail-order and retail store customers
Year-on-year change

OTHER BUSINESSES

OTHER BUSINESSES PERFORMANCE AND TARGETS

	Millions of yen			
	2007 (plan)	2006	2005	2004
Net sales	*21,800*	20,789	19,707	20,375
Germinated brown rice	*5,000*	4,549	5,026	5,383
Kale juice	*4,600*	4,029	3,524	2,985
IIMONO OHKOKU (Mail-order)	*8,800*	8,403	7,153	8,270
Others	*3,400*	3,805	4,002	3,736
Gross profit	*11,300*	10,597	9,689	10,254
Selling, general and administrative expenses	*11,400*	11,359	11,656	12,075
Advertising expenses	*3,000*	2,492	2,740	3,430
Operating income (loss)	*(100)*	(762)	(1,967)	(1,821)
Operating income (loss) margin	*(0.5%)*	(3.7%)	(10.0%)	(8.9%)

	Customers		
	2006	2005	2004
Number of active customers* at fiscal year-end:			
Germinated brown rice (Mail-order)	240,323	236,304	340,764
Kale juice (Mail-order)	125,331	99,564	113,775

** Active customers: Customers making at least one purchase during the preceding seven months.*

Fiscal 2006 Results

Sales in Other Businesses rose 5.5% year on year to ¥20,789 million in fiscal 2006. In terms of earnings, the operating loss in this segment was reduced by ¥1,205 million from ¥1,967 million in the previous period to ¥762 million, as losses narrowed in the Germinated Brown Rice Business and Kale Juice Business. This reflected tighter controls on advertising expenses, and the restoration of profitability in the IIMONO OHKOKU (Kingdom of Wonderful Things) Mail-order Business.

By business, sales in the Germinated Brown Rice Business declined 9.5% year on year to ¥4,549 million, the third consecutive period of declines. Despite the launch of *Delicious Germinated Brown Rice–Fluffy White Rice Style* in October 2005, sales did not cover the falloff in existing products.

Sales in the Kale Juice Business rose 14.3% year on year to ¥4,029 million, due to strong sales of high-margin powdered kale juice incorporating Twintose. A high-value-added frozen kale juice, *Super Kale Juice Twintose Formula*, was launched in July 2005.

Sales in the IIMONO OHKOKU Mail-order Business rose 17.5% year on year to ¥8,403 million, due to strong sales of health equipment and walking shoes developed jointly with Mizuno Corporation.

Fiscal 2007 Outlook and Strategies

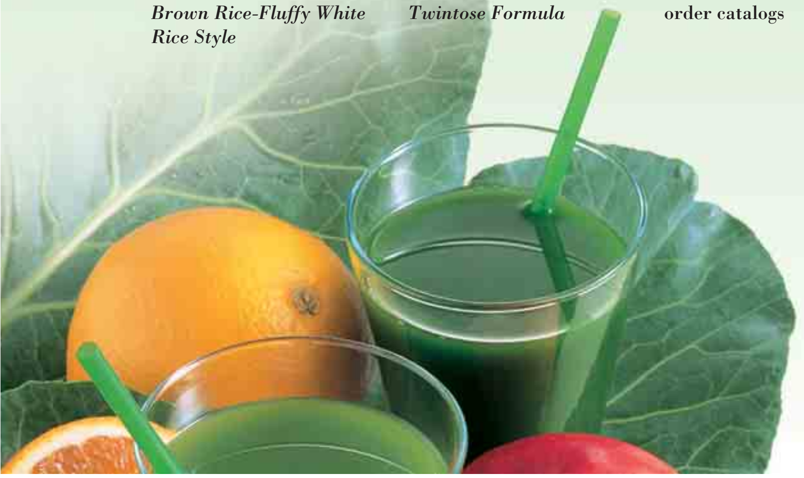
The Company plans to restore profitability to Other Businesses during CC Plan Phase 2. The IIMONO OHKOKU Mail-order Business was extensively restructured during the previous fiscal year, helping it to move back into the black in the year under review. Meanwhile, losses in the Germinated Brown Rice Business and Kale Juice Business are on a downward trend.

In the Germinated Brown Rice Business, although there is strong underlying demand from highly health-conscious customers, we have determined that taste and price are hindrances to growth. To overcome the taste problem, we launched a new product, *Delicious Germinated Brown Rice–Fluffy White Rice Style*, in October

Delicious Germinated Brown Rice-Fluffy White Rice Style

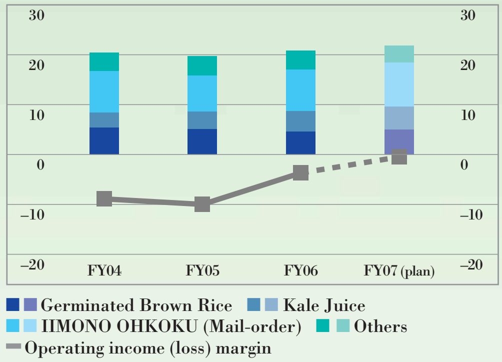
Super Kale Juice Twintose Formula

IIMONO OHKOKU mail-order catalogs



OTHER BUSINESSES NET SALES AND OPERATING INCOME (LOSS) MARGIN

(Billions of yen) (%)



2005. This product has half of the bran removed, producing a brown rice with a taste that compares favorably with white rice. Enhanced sales promotions from January 2006 have led to a recovery in sales, and we expect rising sales in fiscal 2007 to come from even greater sales promotion efforts in the year ahead. We are aiming to restore profitability in the Germinated Brown Rice Business in three years by increasing sales in this way.

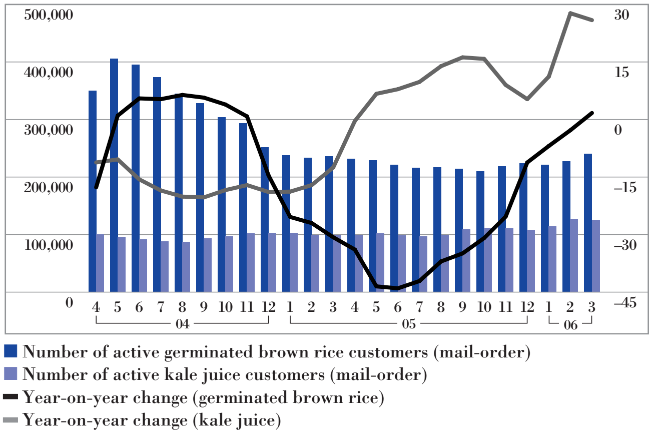
We forecast rising sales in the Kale Juice Business in fiscal 2007, driven by continued strong sales of powdered kale juice incorporating Twintose, the launch of new powdered products, and a switch to high-value-added products with Twintose, including frozen products. We expect the business to break even in fiscal 2007.

In the IIMONO OHKOKU Mail-order Business, we have already restored profitability by enhancing the product lineup, expanding the customer base and increasing sales. In fiscal 2007, our focus will be on improving the earnings ratio.

Forecasts for Other Businesses overall in fiscal 2007 are net sales of ¥21.8 billion, and taking into account the losses from FANCL Square in Ginza and other factors, an operating loss of ¥0.1 billion.

ACTIVE GERMINATED BROWN RICE AND KALE JUICE CUSTOMERS

(Number of customers) (%)



R&D

FANCL pioneered the market for preservative-free cosmetics, creating it from the ground up. Our demanding approach to the development of cosmetics free of preservatives and other additives, as well as to nutritional supplements, has continued to generate new ideas and products. This product development is supported by FANCL's clearly defined R&D policy and structure.

Fundamental Approach to R&D and Structure

FANCL has developed preservative-free cosmetics, as well as new products in the nutritional supplements field, such as easy-to-take, reasonably priced supplements, more flavorsome kale juice, and germinated brown rice that can be cooked like white rice. At the heart of this effort is our unique corporate philosophy to eliminate negative issues such as dissatisfaction, uncertainty and inconvenience from the world. It is the driving force for FANCL as an R&D-oriented company.

To realize our corporate philosophy of helping to eliminate these negative issues, we have to continue creating products with true value for consumers. Beyond this, ideas that defy conventional wisdom, as well as a cutting-edge technological approach, are indispensable. Playing a central role in this effort is the FANCL Research Institute (established as the Central Research Center in 1999; name changed in 2005). The FANCL Research Institute functions as the Company's core R&D facility, conducting activities ranging from the search for new materials and product components, to basic research based on a medical perspective and product development aimed at commercialization.

FANCL's R&D structure is composed of 113 researchers, including those with doctorate degrees in fields such as agriculture, pharmaceuticals and other sciences. Joint research is also conducted with external organizations, including universities and materials companies in other industries. Total R&D expenses in fiscal 2006 amounted to ¥1,978 million, consisting of ¥1,084 million for Cosmetics, ¥638 million for Nutritional Supplements, and ¥256 million for Other Businesses.

A Pioneer in Preservative-free Cosmetics

"Preservative-free cosmetics" is the general term for cosmetics that do not contain any of the previously designated ingredients* that could cause an allergic reaction or dermatitis.

FANCL selects the ingredients for its products from among over 10,000 cosmetic agents based on its own safety standards, and conducts repeated trials using human-derived cells and rigorous irritant evaluations with the latest three-dimensional skin models based on human skin structure. Through this steadfast preservative-free approach that avoids any questionable ingredients, the number of agents that we use in our products has been reduced to just 450, reflecting our dedication to developing absolutely safe products.

** Any of 102 ingredients that could cause dermatitis or other allergic reactions that companies were required to display as product warnings until March 2001. Presently all ingredients—not just these 102—must be displayed on product labels in accordance with government legislation.*

Pursuing Research on Inner and Outer Beauty

One of the main features of the Integrated Research Institute is that it simultaneously conducts R&D into both cosmetics and nutritional supplements.

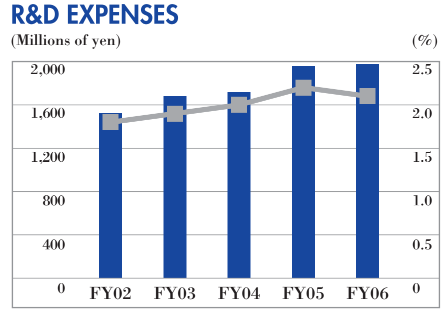
By adopting a two-faceted, internal and external approach to human beauty that encompasses cosmetic use in parallel with nutritional supplements, germinated brown rice and kale juice, the center pursues research into both inner and outer beauty, striving for better all-round health and attractiveness. During fiscal 2006, the center developed cosmetics and nutritional supplements with the proprietary anti-aging agent Silybin* Phytosome.

** A phospholipid moisturizer derived from the seeds of the Marian thistle, purified and stabilized, with high permeability and absorption.*

R&D-RELATED DATA

	FY2006	FY2005	FY2004	FY2003	FY2002
R&D Expenses (Millions of yen)	1,978	1,959	1,720	1,683	1,524
Ratio to Sales	2.1%	2.2%	2.0%	1.9%	1.8%
No. of Researchers	113	114	103	94	84
No. of Patent Applications in Japan	37	50	48	47	91

R&D EXPENSES



CORPORATE SOCIAL RESPONSIBILITY

FANCL got started in the cosmetics business out of a desire to help women who could not use regular cosmetics because of sensitive skin. Our unique policy of interacting with society has been focused on eliminating negative issues such as customer inconvenience and lack of confidence in products. We proactively carry out social contribution activities, such as supporting people with disabilities and helping them to become independent, or cooperating with regional community services and carrying out environmental activities. In all these activities, we are fully committed to fulfilling our corporate social responsibility (CSR).

Our CSR Organization

In April 2005, we launched the CSR Promotion Committee, headed by FANCL's President. This action further energized our CSR structure, creating a Company-wide approach that before had only been undertaken by the various divisions of the Company on an incremental basis. In May 2005, we published our first CSR Report, outlining our basic policies for social contribution and environmental protection. We are committed to continued disclosure of these activities to our stakeholders.

FANCL SMILE Expands Employment Opportunities for Persons With Intellectual Disabilities

In February 1999, FANCL established FANCL SMILE Co., Ltd., a non-consolidated special subsidiary dedicated to promoting the employment of persons with disabilities. At the end of fiscal 2006, the company employed 39 people with intellectual disabilities. FANCL SMILE is engaged in a variety of work for FANCL Group companies, including the layout and setup of catalogs and other documents as well as packaging work for products. In addition, FANCL SMILE staff with forklift truck licenses also work in Group companies, strongly contributing to our business. Over the long term, we aim to steadily improve this company's performance, helping to encourage other companies to employ more persons with intellectual disabilities.

Makeup Seminar Promotes Exchange With Local Communities

The FANCL Academy, our in-house training arm for educating retail store staff and other employees, also holds seminars for local communities. Traveling to facilities for the disabled or the elderly, FANCL Academy staff conduct free lectures on makeup, personal grooming and appearance, and the basics of cosmetics. These seminars give something back to local communities by explaining how to enjoy using cosmetics through the use of proper skin care methods and through demonstrations of makeup techniques.

Efforts to Reduce Environmental Impact

It is an inescapable fact that our business places a burden on the environment. However, we conduct various in-house activities to limit that impact as much as possible. In November 2002, for example, the FANCL Group attained ISO 14001 environmental management certification. In all our divisions and sections, we give consideration to energy conservation and recycling in our activities, working to reduce CO_2 emissions to ultimately help prevent global warming.

Innovative Environmentally Friendly Packaging and Containers

To make effective use of the world's limited resources, we work right from the design stage to avoid excessive packaging at all stages of production. We employ recycled paper and non-wood paper in our cosmetic packages and eliminate instruction manuals by printing explanations on packaging. In addition, we have installed a computer system that selects the optimal packaging for received mail orders depending on size and weight, choosing from seven different types of delivery cartons. We also use recycled materials in our packaging.

A certain portion of our cosmetics line, such as makeup products, is sold in refillable containers that can be used repeatedly. We have also developed refillable containers for liquid products, and as an industry first, introduced "airless compact film," which we use as a special holder for products. Using this film instead of more bulky packaging reduces the amount of waste produced and is also more economical.

Reducing CO_2 Emissions

We have implemented various measures to reduce CO_2 emissions at each of our factories. Concrete steps include installing monitoring equipment to help cut electric power usage and applying thermal jacketing to control waste heat emissions. At the FANCL Research Institute, we have created a rooftop garden that helps to conserve energy, indirectly contributing to lower CO_2 emissions. Because of the success of this system, we are considering introducing it at other facilities.

CORPORATE GOVERNANCE, COMPLIANCE, AND INVESTOR RELATIONS

BASIC STANCE ON CORPORATE GOVERNANCE:

FANCL regards the enhancement of corporate governance as an important management issue in gaining the trust of shareholders and other stakeholders. Our basic policy is to achieve business efficiency and transparency through rigorous adherence to corporate ethics and relevant laws, and through the establishment of an internal control system, including risk management.

CORPORATE GOVERNANCE STRUCTURE:
Executive Officer System

FANCL introduced the executive officer system in June 1999 to ensure the separation of the supervisory and executive functions of management. In 2004, we terminated the system of appointing directors to posts with operational responsibilities, instead appointing executive officers to serve in these posts. In 2005, the term of office of a director was shortened to one year from two years to create an optimal management structure capable of responding flexibly to changes in the business environment.

Board of Directors

The Board of Directors consists of eleven directors, including two outside directors. The Board's role is to make decisions on important operating issues and other statutory matters and to provide management oversight of the operations of FANCL and its subsidiaries on the basis of reports from managers and auditors.

Management Conference

Comprising directors and executive officers, the Management Conference screens matters to be decided by the Board of Directors in advance and deliberates on important management issues within the bounds of authority determined by the Board of Directors.

Corporate Auditors

FANCL has adopted a corporate auditor system anchored by four corporate auditors, all of whom are from outside the Company. The corporate auditors attend all meetings of the Board of Directors, Management Conferences and other important meetings, and regularly exchange opinions with senior management to ensure appropriate management oversight.

Accounting Auditor

FANCL has appointed Ernst & Young ShinNihon to be its accounting auditor and provide objective advice regarding accounting matters.

Retirement Allowance System for Directors Abolished

In June 2006, as part of reforms to the director compensation system, the Company abolished its retirement allowance system for directors because of its low correlation with company performance and strong seniority-oriented nature. FANCL has decided to replace the old system with a stock option incentive scheme.

Basic Stance on Internal Control System and Current Status

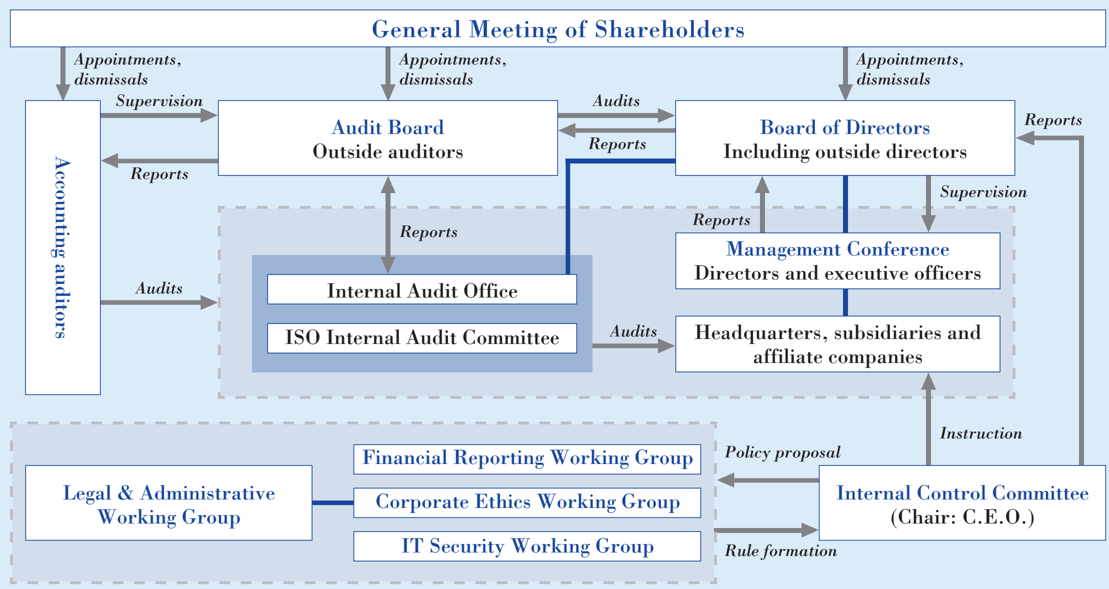
In April 2006, FANCL took several steps to strengthen its internal control system. The company unveiled its Fundamental Policy on Internal Control Systems and established an Internal Control Committee, chaired by the President.

FISCAL 2006 COMPENSATION PACKAGES FOR DIRECTORS AND CORPORATE AUDITORS

	Directors		Corporate Auditors		Total	
	Number of Directors	Amount paid	Number of Auditors	Amount paid	Total number of Directors and Auditors	Total remuneration
Compensation determined by Articles of Incorporation or by resolution of the General Meeting of Shareholders	11	¥ 159 million	5	¥41 million	16	¥ 200 million
Bonus received from allocation of retained earnings	–	–	–	–	–	–
Retirement benefits determined by resolution of the General Meeting of Shareholders	4	¥1,051 million	1	¥ 6 million	5	¥1,057 million
Total	15	¥1,210 million	6	¥48 million	21	¥1,258 million

Note: In addition to the above, two directors received ¥12 million in remuneration, including bonuses, for their concurrent service as employees.

CORPORATE GOVERNANCE SYSTEM



Current Status of Internal Control System

The Internal Audit Office and the ISO Internal Audit Committee work together in auditing business execution in the company's divisions. In addition, the Legal & Compliance Division and the Administrative Headquarters create in-house rules and regulations to ensure compliance with statutory laws and corporate ethics. They also carry out training programs and other activities to raise employee awareness of the nature and importance of compliance.

In April 2005, FANCL formed the CSR Promotion Committee to further strengthen its internal control system, including risk management. The CSR Promotion Committee oversees six working groups: Risk Management, Corporate Ethics, IT Security, Information Disclosure, Environmental Protection, and Community Service. Chaired by the C.E.O., the CSR Promotion Committee comprises directors, executive officers, and presidents of subsidiaries, and makes key decisions about the overall direction of the Group. To ensure the effective implementation of specific measures throughout the Group, members of working groups are chosen from across the Group's entire workforce.

The Internal Control Committee, formed in April 2006, has three related working groups—Financial Reporting, Corporate Ethics, and IT Security. These working groups are proceeding with measures to strengthen FANCL's corporate governance system by building an internal control system in accordance with the recently enforced Company Law and in anticipation of the scheduled introduction of the Financial Instruments and Exchange Law.

Investor Relations

FANCL is committed to disclosing information to shareholders and other stakeholders in a timely, appropriate, and speedy manner to improve management transparency.

1) Promotion of Speedy and Fair Disclosure

We disclose monthly sales data in a timely manner and strive to announce financial results as soon as possible after the end of the fiscal year. Information on financial results is uploaded to the IR section of our website as promptly as possible after official announcements of business results. We are also striving toward fair disclosure to help narrow the information disparity among stakeholders by, among other measures, offering webcasts of information meetings held for analysts, institutional investors, and the media.

Our IR activities are not limited to the domestic investor base. Senior management representatives make individual calls on European and U.S. investors once a year.

2) Internet-based Execution of Voting Rights Available

As another example of how we are utilizing the Internet to enhance shareholder convenience, online voting was made available from the June 2004 General Meeting of Shareholders as an alternative to the execution of voting rights by means of conventional mail.

FOR FURTHER INFORMATION, PLEASE CONTACT:

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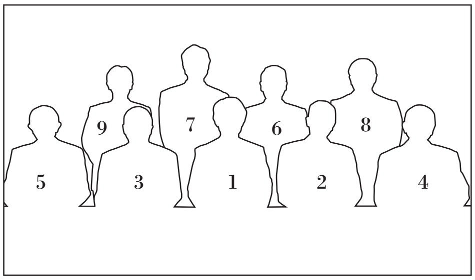
http://www.fancl.co.jp
e-mail: official@fancl.co.jp

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

DIRECTORS AND OFFICERS

(As of June 17, 2006)



1. Kenji Fujiwara
   C.E.O. and Representative Director
2. Yasuyuki Yogoro
   Senior Executive Officer and Director
3. Kazuyoshi Miyajima
   Managing Executive Officer and Director
4. Sumiya Nakajima
   Managing Executive Officer and Director
5. Yoshinori Harigae
   Managing Executive Officer and Director
6. Toshihiro Nasuno
   Managing Executive Officer and Director
7. Mitsuru Nishikawa
   Managing Executive Officer and Director
8. Yoshiharu Hayakawa
   Outside Director
9. Masakazu Iwakura
   Outside Director

C.E.O. and Representative Director

Kenji Fujiwara

Senior Executive Officer and Director

Yasuyuki Yogoro

Managing Executive Officers and Directors

Kazuyoshi Miyajima
Sumiya Nakajima
Yoshinori Harigae
Toshihiro Nasuno
Mitsuru Nishikawa

Director

Yoshifumi Narimatsu

Executive Officer and Director

Yukio Ikemori

Outside Directors

Yoshiharu Hayakawa
Masakazu Iwakura

Executive Officers

Shoji Shiba
Tomoko Tsuji
Haruki Murakami
Toshinori Ryuchi
Noburou Katase
Tomochika Yamaguchi
Takahiro Kase
Akira Yajima
Yutaka Hirano

Statutory Auditors

Taiji Yamada
Fumiko Ikeda
Katsunori Koseki
Akira Tobishima

FINANCIAL SECTION

CONTENTS

SIX-YEAR SUMMARY

FANCL CORPORATION and Consolidated Subsidiaries
For the years ended March 31

	Millions of yen					
	2006	2005	2004	2003	2002	2001
FOR THE YEAR:						
Net sales	¥ 95,322	¥87,937	¥84,957	¥90,026	¥84,657	¥65,418
Cosmetics	41,287	37,098	34,926	37,155	36,748	35,669
Nutritional supplements	33,246	31,132	29,656	29,211	28,995	25,408
Others	20,789	19,707	20,375	23,660	18,914	4,341
Net sales, by sales channel:						
Mail-order sales	57,237	54,544	54,439	59,334	56,821	43,360
Retail store sales	23,607	20,067	17,722	17,744	17,073	15,632
Others	14,478	13,326	12,796	12,948	10,763	6,426
Gross profit	62,083	57,905	55,696	58,982	56,682	47,034
Gross profit margin (%)	65.1	65.8	65.6	65.5	67.0	71.9
Selling, general and administrative expenses	53,508	52,477	47,927	47,456	45,564	38,402
Selling, general and administrative expense ratio (%)	56.1	59.7	56.4	52.7	53.9	58.7
Operating income (loss)	8,575	5,428	7,769	11,526	11,118	8,632
Cosmetics	5,568	4,745	6,283	8,099	8,406	8,320
Nutritional supplements	5,405	4,638	5,371	6,879	5,960	4,694
Others	(762)	(1,967)	(1,821)	(1,646)	(1,681)	(2,532)
Operating income margin (%)	9.0	6.2	9.1	12.8	13.1	13.2
Net income	5,184	1,710	3,387	6,429	5,995	4,867
Net income to net sales (%)	5.4	1.9	4.0	7.1	7.1	7.4
ROE (%)	7.5	2.6	5.1	9.8	9.7	8.5
Advertising expenses	¥ 9,792	¥11,105	¥ 9,865	¥ 9,262	¥10,213	¥ 8,896
Sales promotion expenses	9,319	9,475	7,998	8,615	8,161	5,810
Research and development expenses	1,978	1,959	1,720	1,683	1,524	1,294
Capital expenditures	2,592	2,257	4,864	5,397	3,589	2,727
Depreciation	2,540	2,463	2,556	2,268	2,245	2,379
Net cash provided by operating activities	¥ 9,163	¥ 4,638	¥ 5,861	¥ 9,828	¥ 7,426	¥ 6,083
Net cash used in investing activities	(10,280)	(4,807)	(4,117)	(5,582)	(5,416)	(4,838)
Net cash used in financing activities	(22)	(1,090)	(4,533)	(5,432)	(2,456)	(1,410)
Net decrease in cash and cash equivalents	(1,139)	(1,254)	(2,809)	(1,213)	(437)	(162)

	Yen					
PER SHARE:						
Net income	¥ 242.6	¥ 80.3	¥ 154.6	¥ 279.5	¥ 307.6	¥ 249.8
Shareholders' equity	3,317.0	3,111.2	3,082.4	2,976.3	3,320.2	3,051.4
Cash dividends	55.0	50.0	42.5	35.0	25.0	25.0

	Millions of yen					
AT YEAR-END:						
Total assets	¥85,148	¥79,416	¥78,479	¥79,804	¥79,026	¥75,481
Shareholders' equity	71,406	66,203	65,613	66,350	64,719	59,482
Equity ratio (%)	83.9	83.4	83.6	83.1	81.9	78.8
Interest-bearing debt	–	–	–	350	1,092	3,086
Working capital	33,037	28,622	29,214	29,805	31,082	28,456
Number of stores	208	169	143	144	133	138
Number of consolidated subsidiaries	6	6	6	6	4	3

QUARTERLY FINANCIAL AND STOCK INFORMATION/ MONTHLY SALES DATA

FANCL CORPORATION and Consolidated Subsidiaries
For the years ended March 31

	Millions of yen							
	1st Quarter		2nd Quarter		3rd Quarter		4th Quarter	
	2006	2005	2006	2005	2006	2005	2006	2005
Net sales	¥22,960	¥20,951	¥22,806	¥21,294	¥26,284	¥24,005	¥23,272	¥21,686
Cosmetics	9,992	8,870	9,745	8,982	11,293	10,176	10,257	9,069
Nutritional supplements	8,233	7,230	8,291	7,619	8,954	8,307	7,768	7,973
Others	4,735	4,850	4,770	4,693	6,037	5,521	5,247	4,642
Net sales, by sales channel:								
Mail-order sales	14,056	13,070	13,253	12,976	16,199	15,188	13,729	13,308
Retail store sales	5,621	4,594	5,753	4,914	6,226	5,410	6,007	5,147
Others	3,283	3,286	3,800	3,403	3,859	3,406	3,536	3,229
Operating income	3,288	862	884	430	3,409	2,490	994	1,645
Cosmetics	2,069	1,597	292	457	2,230	1,569	977	1,120
Nutritional supplements	1,652	611	1,129	1,118	1,550	1,540	1,074	1,368
Others	18	(843)	(157)	(622)	62	(78)	(685)	(423)
Net income (loss)	¥ 1,878	¥ 212	¥ 455	¥ (63)	¥ 2,175	¥ 1,285	¥ 676	¥ 275

	Yen							
Stock Price Range*								
High	¥ 1,483	¥ 1,293	¥ 1,923	¥ 1,333	¥ 2,150	¥ 1,350	¥ 2,837	¥ 1,483
Low	1,257	1,090	1,483	1,113	1,773	1,200	2,070	1,287

* *In March 2006, FANCL conducted a 3-for-1 stock split. The above share price is calculated assuming the stock split was conducted at the beginning of fiscal 2005.*

MONTHLY SALES

	Millions of yen											
	2005									2006		
	Apr.	May	Jun.	Jul.	Aug.	Sep.	Oct.	Nov.	Dec.	Jan.	Feb.	Mar.
Cosmetics	¥3,289	¥3,425	¥3,277	¥3,239	¥3,181	¥3,324	¥3,375	¥3,978	¥3,938	¥3,128	¥3,285	¥3,843
YoY increase	15.2%	10.7%	12.2%	4.1%	13.2%	8.6%	17.1%	13.1%	4.3%	9.4%	10.1%	19.2%
Nutritional supplements	2,698	2,661	2,872	2,743	2,561	2,986	2,880	2,878	3,195	2,566	2,408	2,791
YoY increase (decrease)	12.7%	7.8%	21.3%	9.5%	13.3%	4.7%	13.3%	6.5%	4.3%	3.6%	(4.2%)	(6.3%)
Others	1,508	1,572	1,654	1,654	1,541	1,573	1,785	2,211	2,038	1,715	1,808	1,724
YoY increase (decrease)	9.6%	(8.1%)	(6.2%)	(4.4%)	14.5%	(2.6%)	8.7%	15.9%	3.5%	18.5%	10.4%	10.7%
Total	7,497	7,659	7,804	7,637	7,284	7,883	8,041	9,069	9,172	7,409	7,502	8,359
YoY increase	13.2%	5.3%	10.7%	3.9%	13.5%	4.7%	13.8%	11.6%	4.1%	9.2%	5.1%	7.7%

MANAGEMENT'S DISCUSSION AND ANALYSIS

NET SALES

Net sales rose 8.4% year on year to ¥95,322 million due mainly to increased sales in our core Cosmetics Business and Nutritional Supplements Business.

Cosmetics Business sales rose 11.3% to ¥41,287 million, boosted by increases in income from FANCL and ATTENIR cosmetics.

Sales of FANCL cosmetics rose 13.1% to ¥31,406 million. This reflected higher sales of *Mild Cleansing Oil*, which underwent a revamp from the previous fiscal year, and *Facial Washing Powder*, as well as a strong performance by *Beauty Concentrate*, a beauty lotion containing proprietary anti-aging ingredients that was launched in December 2005. By sales channel, mail order sales rose on the back of an increase in the number of customers. Retail store sales showed a strong performance, reflecting favorable existing store sales, as in the previous fiscal year, and the positive impact of store openings. With sales to Hong Kong also robust, sales through all channels, therefore, posted an increase in the year under review.

In the ATTENIR cosmetics brand, sales reached a record high, supported by the solid performance of skin care products on the back of newly launched and updated product lines. The number of customers was also at a record-high level at the end of fiscal 2006.

Sales in the Nutritional Supplements Business grew 6.8% year on year to ¥33,246 million. This growth stemmed from increased sales of *Co-enzyme Q_{10}*, as in the previous fiscal year, and the effect of new products such as *Alpha Lipoic Acid*, *HTC Collagen*, and *Bright Age EX*. Sales increased through all channels, but growth in retail store sales and wholesale sales stood out.

Sales in Other Businesses rose 5.5% to ¥20,789 million. Although sales in the Germinated Brown Rice Business declined, this was more than offset by increased sales in the Kale Juice Business and the IIMONO OHKOKU Mail-Order Business.

Germinated brown rice sales fell 9.5% year on year to ¥4,549 million. In October 2005, FANCL launched a new product called *Delicious Germinated Brown Rice–Fluffy White Rice Style*, containing half the bran of conventional products and offering greatly improved taste. However, this failed to offset the decline in sales of existing products.

Kale Juice Business sales increased 14.3% to ¥4,029 million, due to robust sales of powder-type products containing Twintose.

IIMONO OHKOKU Mail-order Business sales grew 17.5% year on year to ¥8,403 million on the back of buoyant sales of walking shoes jointly developed with Mizuno Corporation and health equipment.

GROSS PROFIT

The gross profit margin declined 0.7 of a percentage point compared to the previous fiscal year, to 65.1%, due to a lower gross profit margin on nutritional supplements.

In the Cosmetics Business, the gross profit margin remained almost flat at 74.2%.

In the Nutritional Supplements Business, the gross profit margin decreased 3.5 percentage points to 62.7%. This was due to a rise in purchasing unit prices stemming from higher demand for *Co-enzyme Q_{10}*.

In Other Businesses, the gross profit margin rose 1.8 percentage points to 51.0%. This increase was attributable to a decline in raw material costs for germinated brown rice and the Company's shift to high-value-added kale juice.

SG&A EXPENSES

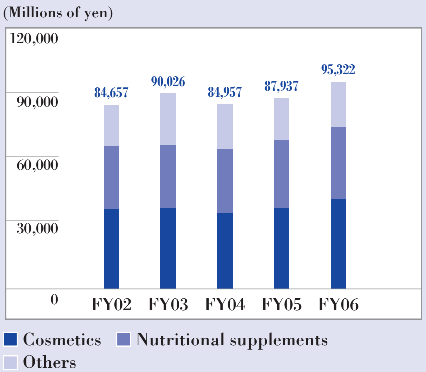
The ratio of selling, general, and administrative (SG&A) expenses to net sales decreased 3.6 percentage points to 56.1%, as the Company improved the efficiency of advertising expenses.

The ratio of marketing costs (advertising and sales promotion expenses) to net sales declined 3.3 percentage points to 20.1%, reflecting active marketing efforts in the previous year.

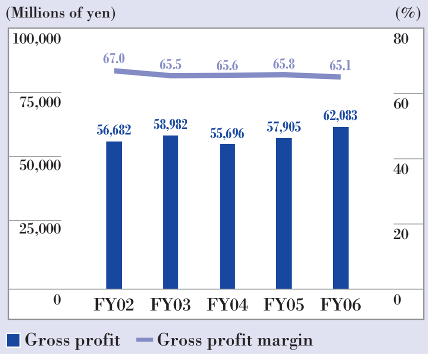
As staffing numbers at retail stores increased due to the opening of new stores, the ratio of personnel costs to sales rose by 0.8 of a percentage point to 13.0%.

In other areas, the Company took steps to reduce transportation, communications and other costs.

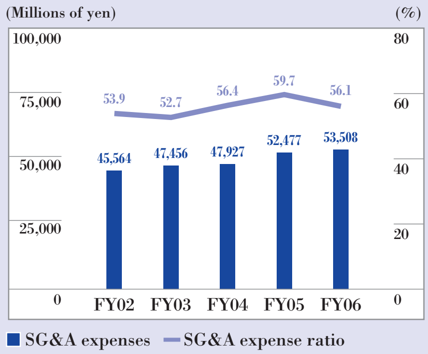
Net Sales by Business Segment



Gross Profit and Gross Profit Margin



SG&A Expenses and SG&A Expense Ratio



OPERATING INCOME

As a result of the aforementioned factors, operating income increased 57.9% year on year to ¥8,575 million, and the operating income margin rose 2.8 percentage points to 9.0%.

In the Cosmetics Business, advertising and sales promotion expenses increased, but owing to the effect of higher sales, operating income grew 17.3% to ¥5,568 million. The operating income margin rose 0.7 of a percentage point to 13.5%.

In the Nutritional Supplements Business, operating income increased 16.5% to ¥5,405 million, and the operating income margin rose 1.4 percentage points to 16.3%. Although the gross profit margin shrank due to a steep rise in the price of some raw materials, this was offset by improved efficiency, mainly in the area of advertising expenses.

Other Businesses posted an operating loss of ¥762 million, which was ¥1,205 million less than the previous fiscal year. Losses in the Germinated Brown Rice Business and the Kale Juice Business contracted, primarily due to the curbing of marketing expenses, while the IIMONO OHKOKU Mail-order Business moved into the black during the period.

OTHER INCOME (EXPENSES)

Loss on retirement of inventories decreased ¥176 million year on year to ¥505 million, as the Company took steps to control inventories more carefully.

Owing to the application of asset-impairment accounting from the year under review, impairment losses relating to land and buildings amounted to ¥238 million. However, the Company sold the land and buildings concerned during the fiscal year.

Other, net expenses improved by ¥458 million to ¥790 million. This reflected the absence in the year under review of provisions for allowance for doubtful accounts and provisions for reserves for retirement allowances for directors booked in the previous fiscal year.

INCOME BEFORE INCOME TAXES

Income before income taxes increased 95.0% year on year to ¥8,515 million. Income before income taxes as a percentage of net sales was 8.9%, up 3.9 percentage points compared with the previous fiscal year.

NET INCOME

Net income grew 203.2% year on year to ¥5,184 million, and the ratio of net income to net sales increased 3.5 percentage points to 5.4%.

Net income per share was ¥242.56. As of the end of the fiscal year under review, FANCL had no outstanding unexercised convertible bonds or equity warrants.

Return on equity (ROE) rose 4.9 percentage points compared with the previous fiscal year to 7.5%, due to the increase in net income.

ASSETS

Current Assets

Current assets rose by ¥5,886 million from the previous fiscal year-end to ¥44,966 million, mainly due to increases in cash and bank deposits and marketable securities as well as inventories. Owing to the increase in sales, cash and bank deposits, marketable securities and inventories grew by ¥1,866 million, ¥3,699 million and ¥1,016 million, respectively.

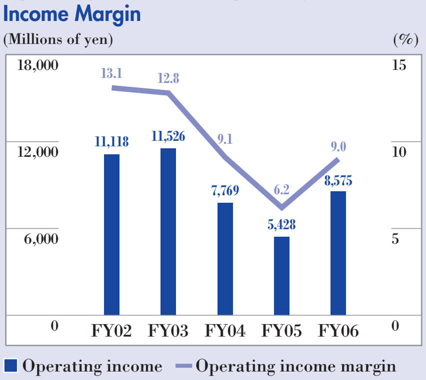
Property, Plant and Equipment, Net

Property, plant and equipment, net decreased by ¥740 million from the previous fiscal year-end to ¥25,794 million. While FANCL actively opened new stores and refurbished existing stores, this was offset by an absence of large-scale investment.

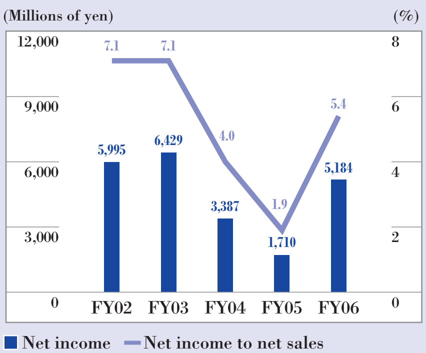
Intangible Assets

Mainly due to the consolidation of IIMONO OHKOKU Co., Ltd., the Company posted additional goodwill, which is being amortized using the straight-line method over a period of five years.

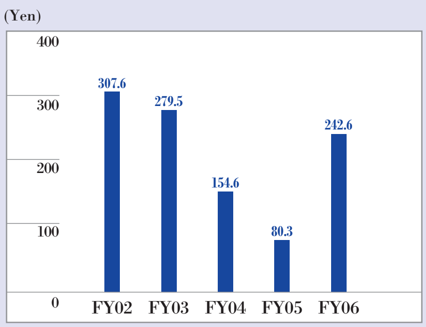
Operating Income and Operating Income Margin



Net Income and Net Income to Net Sales



Net Income per Share



Investments and Other Assets
Investments and other assets increased by ¥858 million from the previous fiscal year-end to ¥14,361 million. Other assets rose by ¥806 million due to the acquisition of unlisted bonds.

LIABILITIES

Current Liabilities
Current liabilities increased by ¥1,471 million to ¥11,929 million, mainly due to a ¥957 million increase in notes and accounts payable – trade.

Noncurrent Liabilities
Noncurrent liabilities decreased by ¥942 million to ¥1,813 million, mainly reflecting a decrease of ¥842 million in accrued retirement benefits.

SHAREHOLDERS' EQUITY

Total Shareholders' Equity
Total shareholders' equity was ¥71,406 million, up ¥5,203 million compared with the previous fiscal year-end. This reflected net income of ¥5,184 million and other factors.

Capital Expenditures
Capital expenditures during the fiscal year under review totaled ¥2,592 million, including investment in new stores and store refurbishment.

By business segment, capital expenditures totaled ¥1,304 million in the Cosmetics Business, ¥1,006 million in the Nutritional Supplements Business, and ¥280 million in Other Businesses.

No major equipment was disposed of or sold during the period.

Cash Flows
Cash and cash equivalents as of March 31, 2006 were ¥21,168 million, ¥1,139 million lower than at the end of the previous fiscal year. The main contributing factors are detailed below.

Cash Flows From Operating Activities
Net cash provided by operating activities totaled ¥9,163 million. This mainly reflected income before income taxes of ¥8,515 million and depreciation and amortization of ¥2,812 million, against income taxes paid of ¥2,813 million.

Cash Flows From Investing Activities
Net cash used in investing activities was ¥10,280 million. This was largely the result of cash used of ¥9,504 million for increase in fixed-term deposits and purchases of investment securities. Additionally, purchases of property, plant and equipment required cash of ¥1,411 million, primarily for store network expansion and refurbishment.

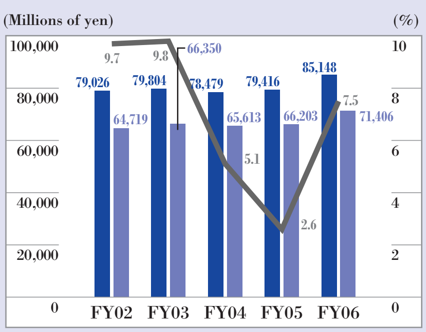
Cash Flows From Financing Activities
Net cash used in financing activities was ¥22 million. This was largely the result of ¥1,008 million derived from the sale (purchases) of treasury stock and ¥1,066 million for cash dividends paid.

In the year ending March 31, 2007, the Company expects cash used in investing activities and financing activities to be within the scope of the increase in cash flows from operating activities.

CASH FLOW INDICATORS

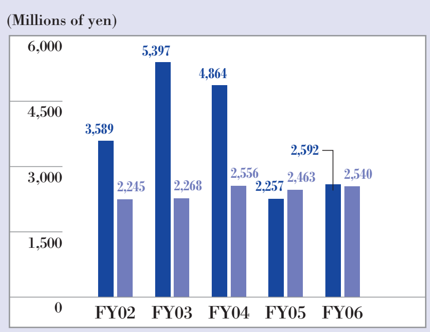
Years ended March 31	2006	2005	2004	2003	2002
Shareholders' equity ratio (%)	83.9	83.4	83.6	83.1	81.9
Shareholders' equity ratio on market-value basis (%)	183.9	110.9	95.7	114.3	113.5
Debt repayment period (years)	–	–	–	0.04	0.15
Interest coverage ratio (times)	–	–	2,930.5	756.0	200.7

Total Assets, Shareholders' Equity and ROE



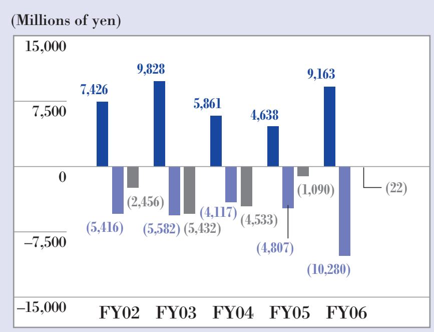
Total assets Shareholders' equity
ROE

Capital Expenditures and Depreciation



Capital expenditures Depreciation

Cash Flows



Operating activities Investment activities
Financing activities

BUSINESS RISKS

PRODUCT DEVELOPMENT AND COMPETITIVE ENVIRONMENT

In product development at the FANCL Group, the product planning and development division is responsible for formulating and proposing product plans based on customer needs and market research. In collaboration with related departments, such as the Central Research Center, it makes final decisions on commercialization. At present, the Group develops cosmetics, nutritional supplements, germinated brown rice and kale juice using its own technology, but there is no guarantee that this will result in successful development and new products. Furthermore, in light of the increasing numbers of women with sensitive skin and greater health consciousness, there are more new entrants into the markets of cosmetics for sensitive skin and nutritional supplements. Consequently, the emergence of similar products could reduce the relative competitiveness of the FANCL lineup and impact the Group's growth potential and earning capabilities.

PRODUCT MANUFACTURING AND QUALITY ASSURANCE

The FANCL Group's cosmetics, nutritional supplements and germinated rice are manufactured at five directly managed domestic factories, while kale juice and undergarment production is outsourced to subsidiaries.

Departments in charge of procurement manage all aspects of raw material purchasing and, working in cooperation with marketing departments, spread purchasing among multiple suppliers and coordinate purchases with suppliers. Nevertheless, unforeseen conditions due to external factors may make it impossible to procure planned quantities of materials. A quality assurance department has been established to improve product quality. The Company uses quality assurance meetings to verify the quality control situation in respective departments, and strives to maintain quality through on-site plant inspections and other means. However, the Group's operating results may be impacted in the event a quality issue arises.

DISASTERS AND BAD WEATHER

To minimize the effects of fire and natural disasters on its production system, the FANCL Group conducts periodic inspections and checks of all its facilities. Geographic dispersion of plants is intended to reduce risks. Nevertheless, there are no guarantees that the impact of fire or natural disaster can be fully prevented. The harvest volumes of rice and kale—raw materials for germinated brown rice and kale juice—are subject to the vagaries of the weather. The Company therefore strives to source raw materials from multiple producing areas and also stockpiles these materials. However, weather factors can cause shortages, leading to higher prices that may impact the Group's operating results.

LIMITS OF INTELLECTUAL PROPERTY PROTECTION

The Group is moving forward with securing patents and other rights to its portfolio of technologies and other intellectual property. However, legal protection in this area is not completely comprehensive and cannot cover all business development domains. Since it takes at least a year and a half from patent application to publication, there is also the possibility that the Company may develop technology for which other companies have already sought patents. Consequently, there is the possibility that patent rights may be infringed in cases where the Company has already commercialized a product prior to the publishing of a patent by another company.

LEGAL RESTRICTIONS

The Cosmetic Business is governed by the Pharmaceutical Affairs Law to ensure the quality, effectiveness and safety of pharmaceuticals, over-the-counter drugs, cosmetics and medical equipment. The FANCL Group manufactures and sells cosmetics and related products in accordance with this legislation. The Nutritional Supplement Business is subject to the Food Sanitation Law, which prescribes food standards, additives, sanitation inspections and business authorization. For foods for sale, the Nutrition Improvement Law prescribes standards for display of nutritional elements and caloric values. Supplements supplied by the Company that meet certain requirements are also subject to the regulations of the functional foods health system, which enables consumers to choose food products with peace of mind to match their dietary habits.

The Group is also governed by the Specified Commercial Transactions Law, which is designed to ensure the fair conduct of mail-order businesses for protection of consumers, and by the Law for Prevention of Unfair Premiums and Unfair Labeling, intended to prevent customer inducement by those means.

The Group has established a Compliance & Legal Division, responsible for compliance and ensuring more thoroughgoing observance of laws and regulations. Notwithstanding this, any violations that occur may affect the Group's operating results.

PERSONAL INFORMATION

The Group's use of mail order and the Internet as its main sales channels has resulted in the accumulation of personal information for many individuals. The Group strictly observes the "Guidelines for Personal Data Protection" prescribed by the Japan Direct Marketing Association, and has established a Company-wide committee to reinforce the information control system. Continuous efforts are also made with regard to employee education in this area. Nevertheless, any leak of such information outside the Company may lead to a loss of customer trust and could reduce sales and subject the Company to losses from payment of liability damages to customers.

CONSOLIDATED BALANCE SHEETS

FANCL CORPORATION and Consolidated Subsidiaries
As of March 31, 2006 and 2005

	Millions of yen		Thousands of U.S. dollars (Note 2)
ASSETS	2006	2005	2006
Current assets:			
Cash and bank deposits	¥ 19,247	¥ 17,381	$ 163,846
Marketable securities	8,625	4,926	73,424
Notes and accounts receivable – trade	8,977	8,714	76,422
Less: Allowance for doubtful accounts	(134)	(150)	(1,144)
	8,843	8,564	75,278
Inventories (Note 5)	6,680	5,664	56,866
Deferred taxes (Note 8)	525	485	4,467
Prepaid expenses and other current assets	1,046	2,060	8,905
Total current assets	44,966	39,080	382,786
Property, plant and equipment, at cost:			
Land	10,637	10,917	90,550
Buildings and structures	20,086	19,419	170,985
Machinery and equipment	9,565	9,532	81,424
Construction in progress	57	4	486
	40,345	39,872	343,445
Less: Accumulated depreciation	(14,551)	(13,338)	(123,867)
Property, plant and equipment, net	25,794	26,534	219,578
Intangible assets:			
Goodwill	27	299	227
Investments and other assets:			
Investment securities:			
Non-consolidated subsidiaries and affiliates	928	898	7,902
Other	3,812	3,609	32,450
	4,740	4,507	40,352
Guarantee deposits	2,715	2,527	23,115
Long-term loans receivable	697	660	5,931
Deferred taxes (Note 8)	150	593	1,280
Other assets	6,474	5,668	55,109
Less: Allowance for doubtful accounts	(415)	(452)	(3,530)
Total investments and other assets	14,361	13,503	122,257
Total assets	¥ 85,148	¥ 79,416	$ 724,848

LIABILITIES AND SHAREHOLDERS' EQUITY	Millions of yen 2006	Millions of yen 2005	Thousands of U.S. dollars (Note 2) 2006
Current liabilities:			
Notes and accounts payable – trade	¥ 4,007	¥ 3,050	$ 34,116
Accrued income taxes (Note 8)	2,056	1,914	17,501
Other current liabilities	5,866	5,494	49,936
Total current liabilities	11,929	10,458	101,553
Noncurrent liabilities:			
Accrued retirement benefits (Note 9)	1,471	2,313	12,518
Other long-term liabilities	342	442	2,912
Total noncurrent liabilities	1,813	2,755	15,430
Contingent liabilities (Note 12)			
Shareholders' equity (Notes 6, 7 and 17):			
Common stock, with no par value:			
Authorized—77,946,000 shares in 2006 and 2005			
Issued —23,392,200 shares in 2006 and 2005	10,795	10,795	91,897
Additional paid-in capital	11,847	11,706	100,850
Retained earnings	55,327	51,173	470,986
Net unrealized holding gain on other securities	67	27	569
Translation adjustments	(5)	(5)	(42)
Less: Treasury stock	(6,625)	(7,493)	(56,395)
Total shareholders' equity	71,406	66,203	607,865
Total liabilities and shareholders' equity	¥85,148	¥79,416	$724,848

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF INCOME

FANCL CORPORATION and Consolidated Subsidiaries
For the years ended March 31, 2006 and 2005

	Millions of yen		Thousands of U.S. dollars (Note 2)
	2006	2005	2006
Net sales	¥95,322	¥87,937	$811,462
Cost of sales	33,239	30,032	282,965
Gross profit	62,083	57,905	528,497
Selling, general and administrative expenses (Note 10)	53,508	52,477	455,503
Operating income	8,575	5,428	72,994
Other income (expenses):			
Interest and dividend income	79	57	669
Loss on retirement of inventories	(505)	(681)	(4,295)
Loss on disposal of property, plant and equipment	(131)	(335)	(1,114)
Loss on impairment of fixed assets	(238)	–	(2,022)
Loss on cancellation of lease contracts	(55)	(434)	(470)
Other, net	790	332	6,724
Income before income taxes	8,515	4,367	72,486
Income taxes (Note 8):			
Current	2,954	2,533	25,150
Deferred	377	124	3,207
	3,331	2,657	28,357
Net income	¥ 5,184	¥ 1,710	$ 44,129

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

FANCL CORPORATION and Consolidated Subsidiaries
For the years ended March 31, 2006 and 2005

	Thousands	Millions of yen						
	Common stock							
	Number of shares	Amount	Additional paid-in capital	Retained earnings	Net unrealized holding gain (loss) on other securities	Translation adjustments	Treasury stock	Total shareholders' equity
March 31, 2004	23,392	¥10,795	¥11,706	¥50,529	¥ 54	¥(5)	¥(7,466)	¥65,613
Cash dividends	–	–	–	(1,065)	–	–	–	(1,065)
Directors' bonuses	–	–	–	(1)	–	–	–	(1)
Net income	–	–	–	1,710	–	–	–	1,710
Purchase of treasury stock	–	–	–	–	–	–	(27)	(27)
Net unrealized holding gain (loss) on other securities	–	–	–	–	(27)	–	–	(27)
March 31, 2005	23,392	10,795	11,706	51,173	27	(5)	(7,493)	66,203
Cash dividends	–	–	–	(1,066)	–	–	–	(1,066)
Net income	–	–	–	5,184	–	–	–	5,184
Sale of treasury stock	–	–	141	–	–	–	868	1,009
Change in interest in investments in subsidiaries	–	–	–	36	40	–	–	76
March 31, 2006	23,392	¥10,795	¥11,847	¥55,327	¥ 67	¥(5)	¥(6,625)	¥71,406

	Thousands of U.S. dollars						
	Common stock Amount	Additional paid-in capital	Retained earnings	Net unrealized holding gain on other securities	Translation adjustments	Treasury stock	Total shareholders' equity
March 31, 2005	$91,897	$ 99,654	$435,625	$226	$(42)	$(63,783)	$563,577
Cash dividends	–	–	(9,074)	–	–	–	(9,074)
Net income	–	–	44,129	–	–	–	44,129
Sale of treasury stock	–	1,196	–	–	–	7,388	8,584
Change in interest in investments in subsidiaries	–	–	306	343	–	–	649
March 31, 2006	$91,897	$100,850	$470,986	$569	$(42)	$(56,395)	$607,865

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

FANCL CORPORATION and Consolidated Subsidiaries
For the years ended March 31, 2006 and 2005

	Millions of yen		Thousands of U.S. dollars (Note 2)
	2006	2005	2006
Cash flows from operating activities:			
Income before income taxes	¥ 8,515	¥ 4,367	$ 72,486
Adjustments to reconcile income before income taxes to net cash provided by operating activities:			
Depreciation and amortization	2,812	2,737	23,944
Loss on impairment of fixed assets	237	–	2,022
(Decrease) increase in allowance for doubtful accounts	(34)	132	(298)
Accrued retirement benefits, net of payments	86	(1)	739
Cash surrender value of insurance policies	716	439	6,096
Income from investment in silent partnership	(161)	(160)	(1,372)
Loss on disposal of property, plant and equipment	123	534	1,048
Changes in operating assets and liabilities:			
Notes and accounts receivable – trade	(263)	(899)	(2,245)
Inventories	(1,016)	(192)	(8,649)
Other current assets	1,028	(339)	8,751
Accounts payable – trade	958	(123)	8,156
Other current liabilities	(119)	(342)	(1,016)
Other noncurrent liabilities	(1,029)	(67)	(8,762)
Income taxes paid	(2,813)	(1,510)	(23,954)
Other, net	123	62	1,052
Net cash provided by operating activities	9,163	4,638	77,998
Cash flows from investing activities:			
Increase in fixed-term deposits	(1,000)	(1,500)	(8,513)
Purchases of property, plant and equipment	(1,411)	(1,703)	(12,011)
Purchases of software	(882)	(238)	(7,506)
Purchases of stock of affiliates	(30)	(226)	(257)
Increase in long-term loans receivable	(34)	(185)	(289)
Purchases of investment securities	(8,504)	(840)	(72,390)
Disposition of investment securities	1,800	115	15,319
Increase in other investments and other assets	(376)	(330)	(3,201)
Other, net	157	100	1,335
Net cash used in investing activities	(10,280)	(4,807)	(87,513)
Cash flows from financing activities:			
Change in interest in investments in subsidiaries	36	–	306
Sale (purchases) of treasury stock	1,008	(27)	8,584
Cash dividends paid	(1,066)	(1,064)	(9,073)
Other	–	1	–
Net cash used in financing activities	(22)	(1,090)	(183)
Effect of foreign exchange rate changes on cash and cash equivalents	–	5	–
Net decrease in cash and cash equivalents	(1,139)	(1,254)	(9,698)
Cash and cash equivalents at beginning of year	22,307	23,561	189,897
Cash and cash equivalents at end of year (Note 14)	¥ 21,168	¥22,307	$180,199

See notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FANCL CORPORATION and Consolidated Subsidiaries
For the years ended March 31, 2006 and 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(A) BASIS OF PREPARATION

FANCL CORPORATION (the "Company") and its consolidated subsidiaries (collectively the "Group") maintain their books of account in accordance with accounting standards generally accepted in Japan, and its overseas subsidiaries maintain their books of account in conformity with those of their countries of domicile. The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in Japan, which are different in certain respects as to the application and disclosure requirements of International Financial Reporting Standards, and have been compiled from the consolidated financial statements prepared by the Company as required by the Securities and Exchange Law of Japan. Certain reclassifications have been made to present the accompanying consolidated financial statements in a format which is familiar to readers outside Japan. Certain amounts from prior years have been reclassified to conform to the current year's presentation.

(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 revalued at their respective fair value upon 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 one foreign consolidated subsidiary are translated at the current exchange rate in effect at each balance sheet date and its 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 which 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.

Under the accounting standard governing statements of cash flows, the definition of cash and cash equivalents in the statement of cash flows and that of cash and bank deposits in the balance sheet differs with respect to certain components. A reconciliation between the cash definitions referred to above is presented in Note 14.

(E) SECURITIES

All securities owned by the Company and consolidated subsidiaries are considered available-for-sale securities and are classified as "other" securities, one of the three categories (trading, held-to-maturity and other) defined in 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 as is reflected as "Net unrealized holding gain on other securities." The cost of other securities sold has been computed by the average method. Other securities without quoted market prices are stated at cost by 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, buildings (excluding structures attached to the buildings) acquired on or after April 1, 1998 by the Company and the consolidated subsidiaries are 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 years

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 is determined based on the historical experience with write-offs 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, a period which falls within the average remaining years of service of the active participants in the plan, commencing the year following the year in which the loss was incurred.

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) DEFERRED INCOME TAXES

Deferred income taxes are recognized by the asset and liability method, under which 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 which will be in effect when the differences are expected to reverse.

(O) DERIVATIVES

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 which meet certain criteria are accounted for by the allocation method used to hedge against risk arising from fluctuation 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) APPROPRIATION OF RETAINED EARNINGS

Under the Commercial Code of Japan (the "Code"), 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 17.

On May 1, 2006, the new Corporation Law of Japan (the "Law"), which superseded the Code, went into effect. Under the Code, the Company was permitted to declare an annual dividend. Under the Law, flexible payment of dividends is permissible subject to certain limits on appropriation of retained earnings as well as to approval by resolution of the shareholders.

2. U.S. DOLLAR AMOUNTS

For the convenience of the reader, the accompanying financial statements with respect to the year ended March 31, 2006 have been presented in U.S. dollars by translating all yen amounts at ¥117.47 = US$1.00, the exchange rate prevailing on March 31, 2006. 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. CHANGE IN METHOD OF ACCOUNTING

Effective April 1, 2005, the Group adopted a new accounting standard entitled "Impairment of Fixed Assets." This standard requires that tangible and intangible fixed assets be carried at cost less depreciation and be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The Group is required to recognize an impairment loss in the statement of income or if certain indicators of assets impairment exist and if the book value of the fixed assets exceeds the undiscounted sum of their future cash flows.

The effect of the adoption of this standard was to recognize an impairment loss of ¥237 million ($2,018 thousand). However, the fixed assets from which the impairment loss was recognized were subsequently sold to third parties during the year ended March 31, 2006.

4. MARKETABLE AND INVESTMENT SECURITIES

Information regarding marketable and investment securities with quoted market prices classified as other securities at March 31, 2006 and 2005 is summarized as follows:

	Millions of yen			Thousands of U.S. dollars		
As of March 31, 2006	Acquisition cost	Carrying value	Unrealized gain	Acquisition cost	Carrying value	Unrealized gain
Securities whose carrying value exceeds their acquisition cost:						
Stock	¥66	¥179	¥113	$563	$1,521	$958
Total	¥66	¥179	¥113	$563	$1,521	$958

	Millions of yen		
As of March 31, 2005	Acquisition cost	Carrying value	Unrealized gain
Securities whose acquisition cost exceeds their carrying value:			
Stock	¥66	¥111	¥45
Total	¥66	¥111	¥45

Other securities without quoted market prices at March 31, 2006 and 2005 are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
Carrying value	2006	2005	2006
Current assets:			
Money management funds	¥ 922	¥3,927	$ 7,847
Commercial paper	6,697	1,000	57,011
Bonds	1,006	–	8,566
Noncurrent assets:			
Unlisted stock (excluding securities traded over-the-counter)	104	130	888
Unlisted foreign bonds	800	800	6,810
	¥9,529	¥5,857	$81,122

5. INVENTORIES

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

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Merchandise	¥1,400	¥ 556	$11,916
Finished goods	1,411	1,888	12,013
Raw materials	2,965	2,306	25,237
Work in process	653	662	5,558
Supplies	251	252	2,142
	¥6,680	¥5,664	$56,866

6. SHAREHOLDERS' EQUITY

The Commercial Code of Japan 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 the sum of the legal 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.

Under the new Corporation Law effective May 1, 2006, the requirements stated above have not been changed.

7. 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 4 directors and 42 employees of the Company in accordance with the Commercial Code of Japan. Under this plan, the maximum number of 166,920 shares were granted.

The exercise price per stock option was set at ¥16,540. As outlined in the plan, this price will be adjusted in accordance with a specified formula for stock splits, reverse stock splits or for other cases. The stock options became exercisable effective June 29, 2001 and may be exercised through June 28, 2009.

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 this plan, a maximum of 396,100 shares were granted to the individuals referred to above.

The exercise price per stock option was set at ¥4,100. As outlined in the plan, this price will be adjusted in accordance with a specified formula for stock splits, reverse stock splits or for other cases. The stock options became exercisable effective July 1, 2004 and may be exercised through June 29, 2007.

On June 19, 2004, the shareholders of the Company approved a stock option plan to grant warrants to purchase shares of the Company's common stock to directors and employees of the Company and its subsidiaries in accordance with the Commercial Code of Japan. Under this plan, a maximum of 623,800 shares were granted to the individuals referred to above.

The exercise price per stock option was set at ¥3,650. As outlined in the plan, this 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 3, 2006 through June 30, 2009.

8. 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 2006 and 2005. 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, 2006 and 2005 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Deferred tax assets:			
Accrued enterprise taxes	¥ 194	¥ 170	$1,652
Accrued bonuses	370	318	3,146
Allowance for doubtful accounts	165	128	1,404
Accrued severance benefits	594	915	5,059
Depreciation	19	66	164
Net loss carried forward	399	593	3,396
Other	163	205	1,390
	1,904	2,395	16,211
Valuation allowance	(652)	(791)	(5,552)
	1,252	1,604	10,659
Deferred tax liabilities:			
Unrealized intercompany profit on land	232	232	1,975
Unrealized revaluation gain on land with respect to acquisition of IIMONO OHKOKU Co., Ltd.	164	165	1,401
Other	181	129	1,537
	577	526	4,913
Net deferred tax assets	¥ 675	¥1,078	$5,746

9. 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 its consolidated subsidiaries (except for one consolidated subsidiary) participate in the multi-employer Welfare Pension Fund Plan (the "Fund") under the Welfare Pension Insurance Law of Japan.

The funded status of the defined benefit pension plans for the years ended March 31, 2006 and 2005 is summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Projected benefit obligation	¥1,563	¥1,451	$13,306
Fair value of plan assets	(638)	(530)	(5,436)
Funded status	925	921	7,870
Unrecognized actuarial net loss	(27)	0	(230)
Net retirement benefit obligation	952	921	8,100
Prepaid pension cost	330	274	2,810
Accrued retirement benefits	¥1,282	¥1,195	$10,910

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 ¥189 million ($1,608 thousand) and ¥1,117 million have been included in accrued retirement benefits in the consolidated balance sheets at March 31, 2006 and 2005, respectively.

Retirement benefit expenses for the years ended March 31, 2006 and 2005 were composed of the following:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Service cost-benefits earned during the year	¥219	¥179	$1,866
Interest cost on projected benefit obligation	16	19	139
Expected return on plan assets	(15)	(11)	(130)
Amortization of unrecognized actuarial net loss	28	42	235
Contributions to the Fund	267	193	2,272
Special additional retirement payments	–	127	–
Retirement benefit expenses	¥515	¥549	$4,382

In the table above, retirement benefit expenses determined by a simplified method at the consolidated subsidiaries have been included in the service cost-benefits earned during each 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, 2006 and 2005 were principally as follows:

	2006	2005
Discount rate	1.75%	1.75%
Expected rate of return on plan assets	3.00%	3.00%
Actuarial cost method	Unit credit actuarial cost method	
Amortization period for actuarial difference	5 years*	5 years*

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

10. RESEARCH AND DEVELOPMENT EXPENSES

Research and development expenses charged to income for the years ended March 31, 2006 and 2005 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Research and development expenses	¥1,978	¥1,959	$16,839

11. 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, 2006 and 2005 would have been as follows:

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Machinery and equipment	¥6,422	¥5,550	$54,672
Accumulated depreciation	2,580	2,043	21,966
	¥3,842	¥3,507	$32,706

The following presents the future minimum lease payments subsequent to March 31, 2006 under finance leases which do not transfer ownership:

March 31, 2006	Millions of yen	Thousands of U.S. dollars
Minimum lease payments:		
Due within one year	¥ 840	$ 7,150
Due after one year	3,049	25,960
	¥3,889	$33,110

Lease expenses related to finance leases which do not transfer ownership for the years ended March 31, 2006 and 2005 amounted to ¥967 million ($8,235 thousand) and ¥911 million, respectively. Depreciation related to these leases for the years ended March 31, 2006 and 2005 would have been ¥884 million ($7,527 thousand) and ¥840 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.

12. CONTINGENT LIABILITIES

(1) Contingent liabilities as of March 31, 2006 amounted to ¥2,218 million ($18,885 thousand) and represented guarantees of borrowings incurred by the twenty 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.

In addition to the guarantees stated above, the land of ¥591 million ($5,038 thousand) and the plant of ¥1,742 million ($14,834 thousand) located in the Nagareyama area were pledged as collateral for the above borrowings.

(2) At March 31, 2006, the Company had guaranteed bank loans totaling $282 thousand (¥33 million) made by FANCL INTERNATIONAL, INC., a nonconsolidated subsidiary.

13. AMOUNTS PER SHARE

In accordance with the accounting standard for earnings per share, 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.

	Yen		U.S. dollars
	2006	2005	2006
Net income:			
– Basic	¥ 242.56	¥ 80.29	$ 2.06
– Diluted	240.78	80.23	2.05
Net assets	¥3,317.02	¥3,111.15	$28.24

14. SUPPLEMENTARY CASH FLOW INFORMATION

The following table represents a reconciliation of cash and bank deposits with cash and cash equivalents at March 31, 2006 and 2005:

	Millions of yen		Thousands of U.S. dollars
Year ended March 31,	2006	2005	2006
Cash and bank deposits	¥19,247	¥17,381	$163,846
Marketable securities	8,625	4,926	73,424
Marketable securities pledged as collateral for a period more than three months	(6,704)	–	(57,071)
Cash and cash equivalents	¥21,168	¥22,307	$180,199

15. DERIVATIVES AND HEDGING ACTIVITIES

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

The Company has implemented internal regulations under which they will hedge any significant exchange risk.

No specific disclosure for derivatives has been made as all the Company's open positions principally met the criteria for deferral hedge accounting.

16. 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 wholesalers, retail stores and by mail, a nutritional supplements business in which various supplements are sold through wholesalers, retail stores and by mail, and other businesses which includes sales of miscellaneous goods, personal ornaments, underwear, medical and health products, housewares, germinated brown rice, kale juice, etc. 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, 2006 and 2005 is summarized as follows:

BUSINESS SEGMENTS

	Millions of yen					
Year ended March 31, 2006	Cosmetics business	Nutritional supplements business	Other businesses	Total	Eliminations or corporate	Consolidated
I. Sales and operating income						
Sales to external customers	¥41,287	¥33,246	¥20,789	¥95,322	¥ –	¥95,322
Intersegment sales or transfers	–	–	–	–	–	–
Total sales	41,287	33,246	20,789	95,322	–	95,322
Operating expenses	35,719	27,841	21,551	85,111	1,636	86,747
Operating income (loss)	¥ 5,568	¥ 5,405	¥ (762)	¥10,211	¥(1,636)	¥ 8,575
II. Total assets, depreciation and capital expenditures						
Total assets	¥26,590	¥15,918	¥14,137	¥56,645	¥28,503	¥85,148
Depreciation	1,262	694	525	2,481	59	2,540
Capital expenditures	1,304	1,006	280	2,590	2	2,592

	Millions of yen					
Year ended March 31, 2005	Cosmetics business	Nutritional supplements business	Other businesses	Total	Eliminations or corporate	Consolidated
I. Sales and operating income						
Sales to external customers	¥37,098	¥31,132	¥19,707	¥87,937	¥ –	¥87,937
Intersegment sales or transfers	–	–	–	–	–	–
Total sales	37,098	31,132	19,707	87,937	–	87,937
Operating expenses	32,353	26,494	21,674	80,521	1,988	82,509
Operating income (loss)	¥ 4,745	¥ 4,638	¥(1,967)	¥ 7,416	¥(1,988)	¥ 5,428
II. Total assets, depreciation and capital expenditures						
Total assets	¥26,174	¥13,384	¥14,199	¥53,757	¥25,659	¥79,416
Depreciation	1,322	522	527	2,371	92	2,463
Capital expenditures	1,008	499	750	2,257	–	2,257

	Thousands of U.S. dollars					
Year ended March 31, 2006	Cosmetics business	Nutritional supplements business	Other businesses	Total	Eliminations or corporate	Consolidated
I. Sales and operating income						
Sales to external customers	$351,465	$283,022	$176,975	$811,462	$ –	$811,462
Intersegment sales or transfers	–	–	–	–	–	–
Total sales	351,465	283,022	176,975	811,462	–	811,462
Operating expenses	304,069	237,007	183,461	724,537	13,931	738,468
Operating income (loss)	$ 47,396	$ 46,015	$ (6,486)	$ 86,925	$(13,931)	$ 72,994
II. Total assets, depreciation and capital expenditures						
Total assets	$226,355	$135,509	$120,341	$482,205	$242,643	$724,848
Depreciation	10,745	5,908	4,467	21,120	505	21,625
Capital expenditures	11,100	8,561	2,386	22,047	15	22,062

Unallocatable operating expenses included under "Eliminations or corporate" for the years ended March 31, 2006 and 2005 amounted to ¥1,636 million ($13,931 thousand) and ¥1,988 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, 2006 and 2005 amounted to ¥28,503 million ($242,643 thousand) and ¥25,659 million, respectively, and consisted principally of cash and cash equivalents, short-term investments, land, funds for long-term investments (investment securities and other) and the cash surrender value of certain of the Company's insurance policies.

GEOGRAPHICAL SEGMENTS

Since sales of the Company and its domestic consolidated subsidiaries for the years ended March 31, 2006 and 2005 constituted more than 90% of consolidated sales, 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, 2006 and 2005, no disclosure of overseas sales has been presented.

17. SUBSEQUENT EVENT

The following appropriation of retained earnings of the Company, which has not been reflected in the consolidated financial statements for the year ended March 31, 2006, was approved at a meeting of the shareholders held on June 17, 2006:

	Millions of yen	Thousands of U.S. dollars
Cash dividends (¥30 = U.S.$0.26 per share)	¥645	$5,498

REPORT OF INDEPENDENT AUDITORS

THE BOARD OF DIRECTORS
FANCL CORPORATION

We have audited the accompanying consolidated balance sheets of FANCL CORPORATION and consolidated subsidiaries as of March 31, 2006 and 2005, 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 express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of FANCL CORPORATION and consolidated subsidiaries at March 31, 2006 and 2005, and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in Japan.

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended March 31, 2006 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 2.

Ernst & Young ShinNihon

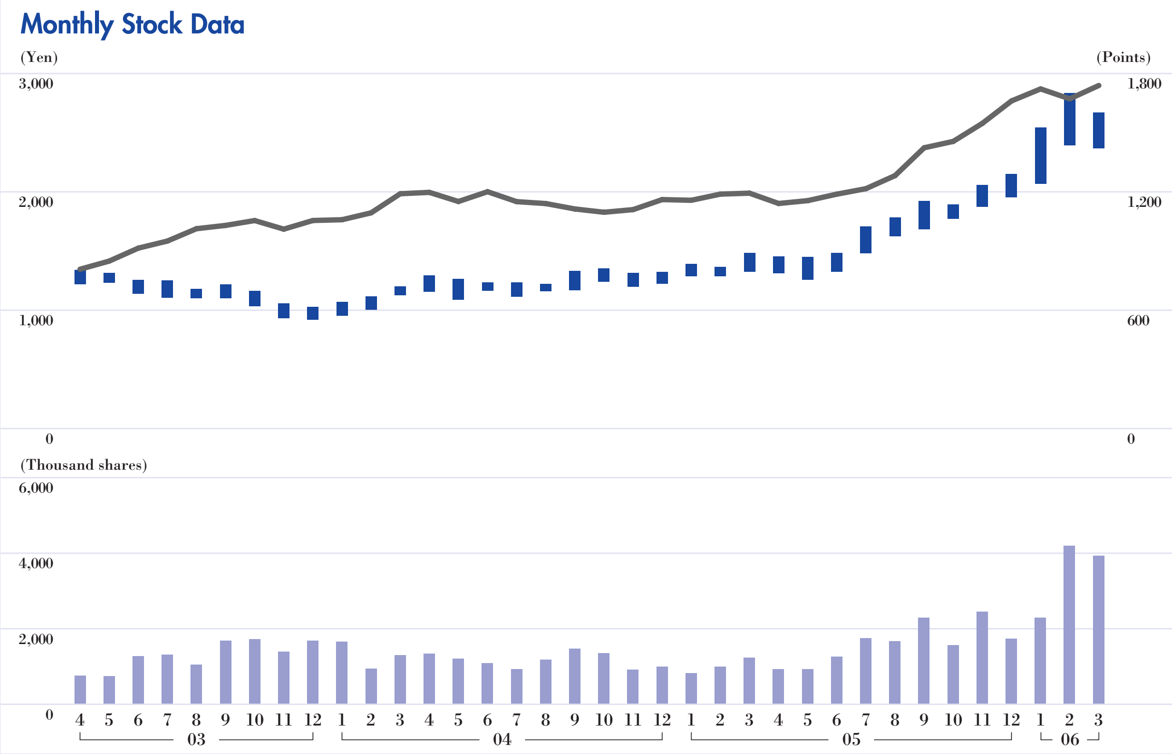
June 17, 2006

SHAREHOLDER INFORMATION

MARKET PRICE RANGE PER SHARE OF COMMON STOCK, AND TRADING VOLUME

	2005									2006		
	Apr.	May	Jun.	Jul.	Aug.	Sep.	Oct.	Nov.	Dec.	Jan.	Feb.	Mar.
High (¥)	1,457	1,450	1,483	1,710	1,787	1,923	1,893	2,060	2,150	2,543	2,837	2,670
Low (¥)	1,313	1,257	1,327	1,483	1,627	1,687	1,773	1,877	1,953	2,070	2,393	2,370
Trading volume (Thousand shares)	925	933	1,266	1,748	1,671	2,291	1,570	2,454	1,739	2,285	4,193	3,931

Note: In April 2006 (ex-rights date March 28), FANCL conducted a 3-for-1 stock split. The above share price is calculated assuming the stock split was conducted at the beginning of fiscal 2005.

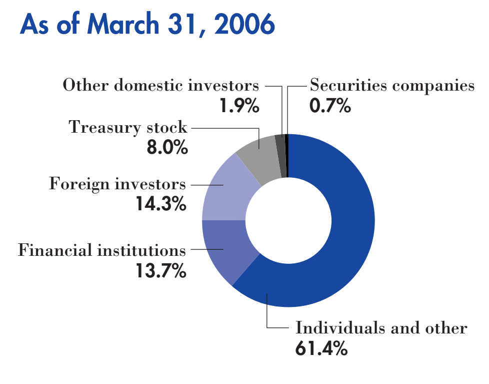


■ Monthly stock price range — TOPIX close ■ Monthly trading volume

COMPOSITION OF SHAREHOLDERS

(Percentage of ownership)

	2004		2005		2006
	Mar.	Sep.	Mar.	Sep.	Mar.
Individuals and other	62.4	59.2	58.2	56.2	61.4
Financial institutions	16.3	16.5	18.0	16.9	13.7
Foreign investors	9.5	12.9	12.5	15.5	14.3
Treasury stock	9.0	9.0	9.0	8.7	8.0
Other domestic investors	2.1	2.0	2.0	1.8	1.9
Securities companies	0.7	0.4	0.3	0.9	0.7



CORPORATE INFORMATION

(As of March 31, 2006)

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)

COMMON STOCK

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

Note: Totals post 3-for-1 stock split on April 1, 2006 are as follows.
Authorized shares: 233,838,000
Outstanding shares: 70,176,600

PAID-IN CAPITAL

¥10,795,161,280

NUMBER OF SHAREHOLDERS

26,303

NUMBER OF FULL-TIME EMPLOYEES

626

TRANSFER AGENT AND REGISTRAR

Mizuho Trust & Banking Co., Ltd.
1-2-1 Yaesu, Chuo-ku,
Tokyo 103-8670, Japan
http://www.mizuho-tb.co.jp/daikou/

ANNUAL MEETING OF SHAREHOLDERS

Held in mid-June in Kanagawa

CONSOLIDATED SUBSIDIARIES

ATTENIR CORPORATION
NICOSTAR Co., Ltd.
IIMONO OHKOKU Co., Ltd.
FANCL Hatsuga Genmai Co., Ltd.
FANCL ASIA (PTE.,) LTD.
FANCL Biken Co., Ltd.

FANCL Corporation

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

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