H2O RETAILING CORPORATION

FINANCIAL REPORT 2008

RETAILING

Profile

Hankyu Department Stores, Inc. was established in 1929 in Umeda, Osaka, as the world's first railway terminal department store by Mr. Ichizo Kobayashi, the founder of the Hankyu Corporation. Helped by the ability of a railway terminal to attract customers, the store grew together with the Umeda area, and a succession of stores in other areas were subsequently opened.

In 1947 the Company was spun off from Hankyu Corporation and formed the Hankyu Department Stores Group.

On 1st October 2007, Hankyu Department Stores, Inc. changed its name to H2O RETAILING CORPORATION and became a holding company in accordance with the management integration between Hankyu Department Stores, Inc. and Hanshin Department Store, Ltd.

Currently, the Group consists of 48 subsidiaries and 7 affiliates that operate retail businesses, including its core-department store operations, supermarket operations and shopping center operations.

Contents

General Business Conditions

Ⅰ. Business Performance

During the term under review, the Company took various steps to achieve its goals under its long-term business plan, the Grand Prix 10 (GP10) Plan, which runs through fiscal 2014. On 1st October 2007, we made a new start as H_2O RETAILING CORPORATION, after our management integration with The Hanshin Department Store, Ltd.

After the management integration, we relaunched our long-term business plan as GP10 Plan ver. 2. Under our new operating structure, we are working to leverage the benefits of the management integration as soon as possible, expand our scale of operations and firm up our business base, positioning us to achieve our target under the relaunched long-term plan of operating income of ¥40 billion.

Business results for the term include those of The Hanshin Department Store Group and revenues of the newly opened, in February 2008, Hankyu Department Store MEN'S menswear store. With the further addition of the full-term sales of Hankyu Nissho Store, which became a subsidiary in July 2006, consolidated sales climbed 19.1% year-on-year to ¥471,617 million, with operating and net income growing by double-digit margins to record highs.

By segment, our core Department Store Business sales were ¥351,435 million, up 20.5% year-on-year, with operating income ¥13,587 million, a 15.2% increase. In the Supermarket Business, sales rose 14.7 % year-on-year to ¥89,785 million, and operating income jumped 42.5 % to ¥1,425 million—a significant increase in both revenues and profit. In the Property Management Business, sales totaled ¥9,686 million, a 4.3% increase over the previous fiscal year, while Other Businesses saw sales rise 23.0% to ¥20,711 million.

Results for the term

	Millions of yen	YoY %	(Reference) Forecasts at end of first half Millions of yen
Net sales	471,617	119.1	473,000
Operating income	17,114	115.9	17,000
Net income	9,450	116.7	9,400

Below are details of the performance of each business segment.

Department Store Business

In the Department Store Business, sales of womenswear and other clothing were adversely affected by high summer and autumn temperatures. Measures to attract customers included management integration-related commemorative sales and Christmas and Valentine's Day joint promotions at Hankyu and Hanshin department stores.

At the Umeda Main Store of Hankyu Department Store, womenswear had a difficult year, but sales of cosmetics, fashion accessories and food and drinks were strong. Another boost came from a special menswear promotion in February 2008 at the nearby Hep Navio commercial complex, where we opened one of Japan's largest menswear emporium, MEN'S, with six floors of high-class apparel. Since the opening of this store, which boasts an overwhelmingly competitive lineup, including brands being sold for the first time in Japan, and a floor layout based on style, we have won new customers who live not only in Kansai but also in the Chugoku, Shikoku and Chubu areas, and customers who do not usually use department stores. In the two months since its opening, the store's sales have totaled ¥4.8 billion, approximately twice the level for menswear in the same period of the previous term. As a result, sales at the Umeda Main Store rose 1.5% year-on-year to ¥173.1 billion.

Of the 10 branches in the Hankyu Department Store chain, 6 including Senri Hankyu, Kawanishi Hankyu and Sakai Kitahanada Hankyu, posted higher sales year-on-year, As a result, sales for all branches edged up 0.4%. Another year of big increases in revenues was posted at Sakai Kitahanada Hankyu store, which saw nearly double-digit growth in sales of food items and children's apparel after a refurbishment in March 2007. However, at Yurakucho Hankyu, which suffered from intensified competition, womenswear, the mainstay product, had a difficult year with sales declining 5.0% year-on-year despite an overhaul of sales areas carrying beauty and relaxation products for women professionals. Sales rose 4.2% year-on-year at the Oi Hankyu Food Hall, which had been loyally supported by its local community since opening in 1953, due partly to a closing sale at the end of March 2008. Closure was planned ahead of a Hankyu redevelopment project near JR Oimachi railway station. As a result of the foregoing, total sales of Hankyu Department Store rose 0.6% year-on-year to ¥292.0 billion.

Turning to The Hanshin Department Store, second-half over-the-counter sales at the Umeda Main Store remained flat from the previous year. A poor sales performance in clothing was offset by an increase in customers attracted by a Hanshin Tigers supporters' merchandise promotion in October and by various events to mark the 50th anniversary of the Company's founding. In March 2008, we began operations at our third satellite store, Hanshin Mikage (total sales area: 5,900m^2) within the Mikage Classe commercial complex opened in the Mikage (Kobe, Hyogo Prefecture) residential area within the Hanshin railway lines' area. Drawing on our expertise built up at the Umeda Main Store, Hanshin Nishinomiya store and Sannomiya Hanshin Food Hall, we worked to create a store rooted firmly in its community and offering a higher class of daily products. Since its opening, this store has been very well received by local residents, especially its food and beverage zones. As a result of these factors, second-half sales at The Hanshin Department Store totaled ¥57.8 billion.

From April 2007, holders of Hankyu Department Stores' Persona Card and The Hanshin Department Store's Emerald Card have been granted the convenience to use either card in the stores of either chain. As this move has generated publicity, the number of customers who use the cards has increased. The combined card use in both stores totaled ¥10.9 billion, with the cards accounting for 3.9% of total sales at both main stores.

As a result of the foregoing, sales of the Department Store Business, including the business results of The Hanshin Department Store since October 2007, increased 20.5% year-on-year to ¥351,435 million. Operating income also jumped 15.2% to ¥13,587 million.

Department Store Business

	Millions of yen	YoY %
Sales	351,435	120.5
Operating income	13,587	115.2

Supermarket Business

We have positioned the Supermarket Business as the second core business after the Department Store Business and are working to expand the scale of our operations in this area. As a result of refurbishment measures, such as the reconstruction and expansion of floor space at Hankyu Oasis, Inc.'s Seiwadai store (Kawanishi, Hyogo Prefecture), customer numbers have risen, pushing up sales at established stores of Hankyu Oasis and Hankyu Family Store, Co., Ltd. by 2.4% year-on-year. Another top-line contribution came from our closure of two underperforming stores and the opening of a Hankyu Oasis store at Kusatsu, Shiga Prefecture, under our scrap-and-build policy.

In addition, we introduced point cards for our Hankyu Family Store outlets in October 2007, enabling points to be accumulated and used at any of our three supermarket operators. As a result of these measures, along with discount coupons and joint promotions, the number of customers rose, contributing to higher sales.

In January 2008, we laid the groundwork for the development of private brand products through a business alliance with Valor Co., Ltd., a food-centred (rather than general merchandise) supermarket chain in the Chubu area.

We also took measures to expand centralised purchasing, leveraging economies of scale and overhauling our order system to eliminate waste and errors. These measures improved profitability, leading to a 0.8 point increase in the gross margin.

Lifted also by inclusion of the full-year business results of Hankyu Nissho Store, which became a subsidiary in July 2006, sales in the Supermarket Business rose 14.7% year-on-year to ¥89,785 million, Operating income aiso jumped 42.5% to ¥1,425 million.

Supermarket Business

	Millions of yen	YoY %
Sales	89,785	114.7
Operating income	1,425	142.5

Property Management Business

In the Property Management Business, mainly the operation of commercial facilities, We decided to close down and completely overhaul the Hankyu Oimachi Daily Shoppers building in Shinagawa Ward, Tokyo. The overhaul is part of a redevelopment project near JR Oimachi Station in which Ours Inn Hankyu, a Group business hotel adjacent to Daily Shoppers, will be combined with commercial facilities.
To facilitate this project, in October 2007, we established the Oi Development Co., Ltd. as a subordinate holding company to coordinate the Property Management Business.

Hankyu Shopping Center Development Co., Ltd, which operates and manages commercial facilities, saw revenues improve at three out of five directly managed properties, including Mosaic Ginza Hankyu (Chuo Ward, Tokyo), while established shopping centres performed steadily. The miscellaneous merchandise outlet “Can Meet”, being developed within station premises, also increased sales, with revenues rising at JR Shinagawa (Tokyo) and Omiya (Saitama Prefecture) stations. Further sales growth is expected with the launch of operations at a third “Can Meet” store within JR Tokyo station.

At the same time, Ours Inn Hankyu, which operates business hotels, boosted revenues and profits on the back of hotel-based training courses for the spring intake of new corporate employees which that yielded strong occupancy rates.

As a result of the foregoing, sales in the Property Management Business rose 4.3% year-on-year to ¥9,686 million, and operating income increased 8.2% to ¥1,747 million.

Property Management Business

	Millions of yen	YoY %
Net sales	9,686	104.3
Operating income	1,747	108.2

Other Businesses

At Hankyu Kitchen Yell Co., Ltd., which operates various home delivery services, business was expanded by extending its operating area in April 2007 to include Hirakata and Neyagawa cities in Osaka Prefecture. At the same time, the company enhanced operating ratios and increased average spending per customer by shifting in January 2008 from deliveries every second day to daily deliveries and by adding to our catalogue products for those concerned about food safety (after a number of food scares in Japan in 2007). As a result of these convenience enhancing measures, sales increased 7.7% year-on-year.

Profitability also increased at all subsidiaries of this business, with revenues and profits rising notably at Hankyu Seisakusho Co., Ltd., which designs and installs interior fittings for retail outlets, and With System Corporation, which designs and operates data-processing systems. As a result, sales in Other Businesses, including the results since October 2007 of five subsidiaries of The Hanshin Department Store, Ltd. including Hanshin Shoji Co., Ltd., which markets womenswear, increased 23.0% year-on-year to ¥20,711 million. Operating income in Other Businesses soared 205.0% year-on-year to ¥1,031 million.

Other Businesses

	Millions of yen	YoY %
Sales	20,711	123.0
Operating income	1,031	305.0

Management Issues to be Resolved

Under GP10 Plan ver. 2, we are pursuing growth strategies and expanding our business scale through new store openings. At the same time, we are strengthening our business base to support an expansion of business scope through strengthened profitability at our established stores and various other businesses.

In the Department Store Business, we will open a new store tentativery named Nishinomiya Hankyu, (total store area: 25,000m^2) as the core element of Hankyu Nishinomiya Gardens at Hankyu Nishinomiya-Kitaguchi Station (Nishinomiya, Hyogo Prefecture), which is scheduled to open in the autumn of 2008.

At the Umeda Main Store of The Hanshin Department Store, we will launch a refurbishment of the sales areas in the second half of the current term, aiming to raise profitability by focusing on fashion operations in addition to our renowned and popular food basement.

Meanwhile, in the Supermarket Business, we aim to strengthen profitability by new store openings, mainly Hankyu Oasis and Hankyu Family Store, as well as launching operations at our new delicatessen factory and developing private-brand merchandise under an agreement with Valor, Ltd., a partner since January 2008.

In the Property Management Business, we launched the redevelopment project near JR Oimachi Station in Tokyo in April 2008, aiming at a grand opening in 2014.

To create a more efficient business structure, we have decided to merge Hankyu Department Stores, Inc. and The Hanshin Department Store, Ltd. and merge five companies in the Supermarket Business on 1st October 2008. Through this new overhaul, we aim to bring forward the benefits of integration and expand market share in the Kansai region through diversification of our retail enterprises, a core strategy in GP10 Plan ver. 2.

Management’s Discussion and Analysis of Financial Condition and Results of Operations

Overview

Hankyu Department Stores, Inc. made a new start on 1st October 2007 after its management integration with The Hanshin Department Store Group, resulting in a new entity, H_2O RETAILING CORPORATION.

On a consolidated basis, the Company booked record profits and double-digit growth in sales and operating and net income. This was primarily the result of including the business results of Hanshin Department Store Group in the second half. Other factors were the opening of Hankyu Department Stores' MEN'S emporium and including the full-term earnings of Hankyu Nissho Store, which was included in the scope of consolidation in July 2007.

Operating Performance

Net Sales

Sales rose ¥75,667 million year-on-year to ¥471,617 million (US$4,716,170 thousand) on a consolidated basis.

In the Department Store Business, menswear sales doubled year-on-year at the Hankyu Department Store Umeda Main Store thanks to sales at the MEN'S emporium, which began business in February 2008 and made up for sluggish sales of womenswear. With 6 out of 10 Hankyu department stores increasing sales, stores other than the main store retained their sales momentum with a 0.4% rise year-on-year. Hanshin Department Store’s second-half sales were roughly in line with their level a year earlier, with the number of customers increased by promotions such as a Hanshin Tigers supporters’ merchandise sale.

In the Supermarket Business, refurbishment of established stores lead to an increase in the number of customers visiting the stores. We also took measures to improve profitability, opening the first Hankyu Oasis store in Shiga Prefecture and closing two others under our scrap-and-build programme for this business. Further contributions to sales came from the increase in the number of customers due to the introduction of joint point programmes and joint business planning by the three supermarket businesses.

In the Property Management Business, revenues overall grew 4.3% year-on-year, with steady growth of 3.9% at Hankyu Shopping Center Development Co., Ltd., where revenues increased at three out of five directly-managed shopping centres.

In Other Businesses, revenues increased 23.0% overall, with Hankyu Kitchen Yell Co., Ltd., which operates home delivery services, posting a 7.7% increase on the back of greater efficiency and increased per-customer spending following expansion of operational areas and measures to improve convenience by shifting to daily delivery rather than delivery every second day.

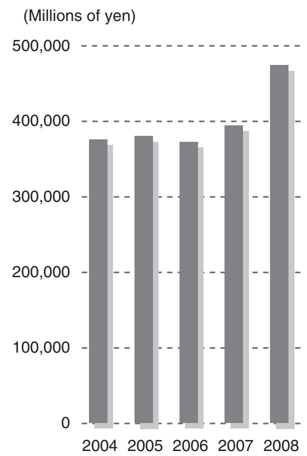
Gross Profit

Gross profit increased a substantial ¥20,345 million year-on-year to ¥136,929 million (US$1,369,290 thousand) on a consolidated basis. As with sales, a major contribution came from including the results of the Hanshin Department Store Group within the scope of consolidation for the second half of the reporting period.

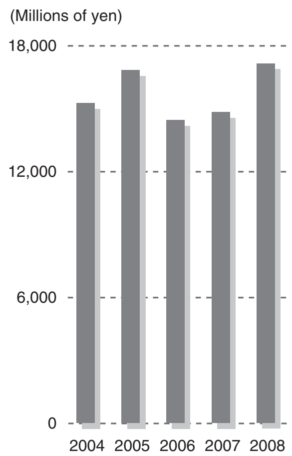
Selling, General and Administrative Expenses and Operating Income

Selling, general and administrative expenses increased ¥17,994 million year-on-year on a consolidated basis to ¥119,815 million (US$1,198,150 thousand). This was mainly attributable to consolidation of Hanshin Department Store Group. Operating income increased by ¥2,351 million year-on-year to ¥17,114 million (US$171,140 thousand), and the operating income margin was almost unchanged from the previous year, at 3.6%.

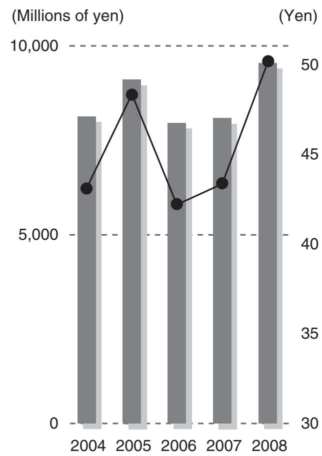
Net Sales



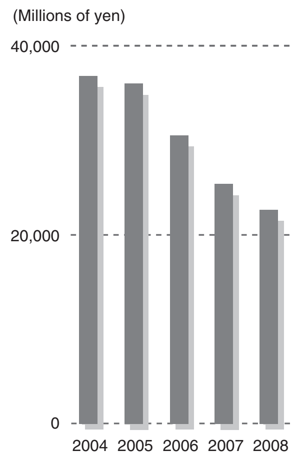
Operating Income



■ Net Income
● Net Income per Share



Debt



Other Income and Expenses

The Company posted a ¥268 million loss on equity method investments for the reporting period that caused equity in earnings/losses of affiliated companies to worsen by ¥368 million year-on-year, the Company having posted a ¥99 million gain for the previous fiscal year. On the other hand, the Company increased net interest and dividend income by ¥43 million to ¥791 million.

Despite an extraordinary gain of ¥2,819 million due chiefly to a ¥2,391 million gain on the sale of property, plant, equipment and intangibles at Mosaic Realty and two other companies, extraordinary losses of ¥3,955 million were booked by the Company mainly as a result of a ¥1,131 million loss on provision of reserve for redemption of gift certificates, impairment losses of ¥867 million at Hankyu Nissho Store and three other companies, and an ¥812 million loss on the disposal of property, plant, equipment and intangibles.

As a result of the foregoing, income before income taxes on a consolidated basis increased by ¥2,598 million year-on-year to ¥16,905 million (US$169,050 thousand).

Net Income

Net income increased ¥1,350 million year-on-year to ¥9,450 million (US$94,500 thousand). Return on equity came in at 6.2% compared with 5.7% a year earlier. Earnings per share (EPS) stood at ¥50.07, up from ¥43.23 in the previous term, and fully diluted EPS was ¥45.19, an increase from ¥38.99 in the previous term.

Financial Position

1) Assets, Liabilities and Equity

Total assets increased by ¥55,020 million year-on-year to end the term at ¥337,778 million (US$3,377,780 thousand). A decline of ¥4,727 million due mainly to a fall in unrealised gains on investments in securities was more than outweighed by increases in cash on hand and in banks from consolidation of the Hanshin Department Store Group (¥14,093 million), trade receivables (¥6,775 million), inventories (¥2,636 million), buildings and structures (¥4,548 million) and goodwill (¥9,164 million).

Total liabilities increased ¥35,925 million from the end of the previous term to ¥173,791 million (US$1,737,910 thousand). This rise was due chiefly to increases in trade accounts payable (¥10,169 million), gift coupon-related liabilities (¥6,203 million) and employees' severance and retirement benefits following the consolidation of Hanshin Department Store Group (¥5,132 million).

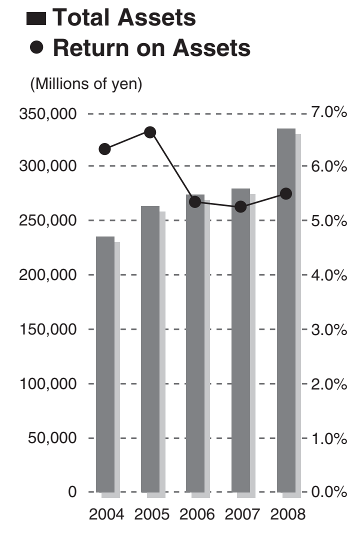
Net assets increased ¥19,095 million from the previous year-end to ¥163,987 million (US$1,639,870 thousand). The main factors were an increase in retained earnings from net income of ¥9,450 million and a ¥19,608 million increase in capital surplus after the share exchange with The Hanshin Department Store, Ltd., which outweighed a ¥2,241 million decrease in retained earnings after dividend payment and ¥6,130 million decline in net unrealised holding gains on securities, chiefly shareholdings.

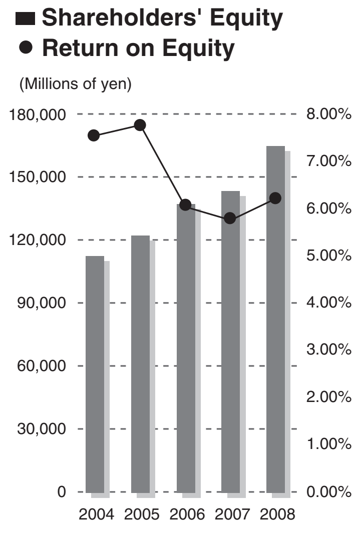
In line with the conversion of Oi Development Co., Ltd. (now known as Ours Inn Hankyu Co., Ltd.) into a wholly-owned subsidiary, minority interests decreased by ¥1,607 million to ¥89 million.

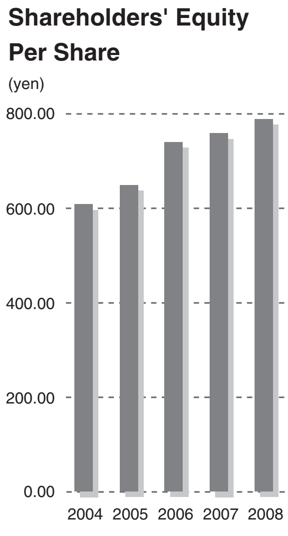
2) Cash Flows

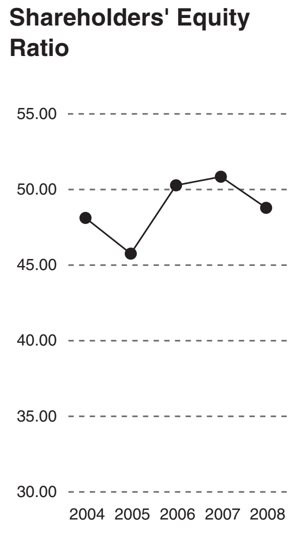
Cash and cash equivalents at the year-end totalled ¥54,688 million (US$546,880 thousand), an increase of ¥14,093 million from the previous fiscal year-end.

Net cash provided by operating activities totaled ¥20,107 million (US$201,070 thousand), a year-on-year increase of ¥1,274 million. The main factors were an increase of ¥2,598









million in income before income taxes that outweighed an increase of ¥1,593 million in income taxes paid.

Net cash provided by investing activities amounted to ¥17,552 million (US$175,520 thousand), a year-on-year increase of ¥20,629 million. The main factors here were ¥21,336 million in proceeds from the purchase of stock of a subsidiary accompanied by a change in the scope of consolidation.

Net cash used in financing activities increased by ¥9,425 million year-on-year to ¥23,616 million (US$236,160 thousand). The main factor was an increase of ¥18,521 million in additions to treasury stock (through acquisition of own stock) prior to the management integration with The Hanshin Department Store, Ltd. that outweighed a ¥2,800 million reduction in repayments of short-term borrowings and a ¥5,817 million fall in payments for the redemptions of bonds.

This left the Group with an interest coverage ratio (net cash provided by operating activities divided by interest paid) of 265.2 times, and a ratio of interest-bearing liabilities to cash flow (net cash from operating activities) of 1.1 times. Despite the ongoing construction work at the Hankyu Department Store Umeda Main Store, the Group's financial position remains sound.

Risk Disclosures

The profitability and sales of the Companies could be affected by the below risk factors. These risks, however, do not cover all the risks which could affect the future operations or future financial condition of the Companies. The factors related to the future are what the Companies thought could happen as of 31st March, 2008.

(1) Business environment

1. The business environment for retailers

The rising dependency ratio (ageing population with falling birthrate) and increasing competition among various kinds of retailers in the market could change the business environment for retailers and affect the profitability of the Companies.

2. The rebuilding of the Umeda Main Store

The Company began rebuilding its Umeda Main Store in 2005. The first phase of reconstruction will be completed for partial opening in the autumn of 2009, and the fully completed grand opening is scheduled in the spring of 2012. The new Umeda Main Store will be one of the biggest stores in Japan and is expected to be much more profitable than the existing store. During the construction period, however, net sales will decrease due to a reduction of the sales area. Also, there are a number of other development plans underway in the Umeda area, which will become one of the largest retail zones in Japan. This will make the area more attractive for shopping than other areas, but competition could intensify. These background factors could also affect the profitability of the Companies.

(2) Changes in laws, regulations and other government policies

1. Store openings and extensions

In Japan, the law concerning large retail stores governs the opening of new department stores and supermarkets by the Companies. This law requires that new store openings and existing store extensions with sales areas of more than 1,000m^2 must undergo inspection by local authorities to avoid affecting the surrounding living environment. This could influence the Companies' future store opening plans.
Other laws and regulations concerning antitrust, environment, recycling and consumer protection could affect the Companies.

2. Consumption tax rate

A rise in the consumption tax rate could depress personal spending. This could lead to a decrease in the sales of the Companies.

(3) Natural environment and accidents

1. Unusual climate

Cold summers and unseasonably warm winters could affect profitability since sales of fashionable clothes are an important part of the Companies' overall sales.

2. Natural disasters and accidents

Natural disasters and accidents, including earthquakes, floods, typhoons and fires, could damage property of the Companies.

(4) Other

1. Safety of items sold

The Companies ensure the high quality of items sold through special quality control committees. Epidemics and other public health related issues such as BSE, however, could depress domestic consumption of food products and influence sales.

2. Control of customer information

The Companies have strict internal rules for protecting customer information. Any accidental or criminal leak, however, could damage the Companies' reputation and decrease sales.

3. Systemic risk

Earthquakes, fires, electricity problems and computer viruses could damage the information systems of the Companies and have a negative influence on efficiency and profitability.

Corporate Governance

Fundamental Stance on Corporate Governance
The Company is working to strengthen corporate governance, focusing on management's supervision function and transparency.

We have appointed outside directors and outside corporate auditors, and the management is reviewed by the Board of Directors and the Board of Corporate Auditors. Management is also reviewed by shareholders and investors through company information willingly disclosed at shareholders' meetings, in business reports, in letters to shareholders and through other IR activities.

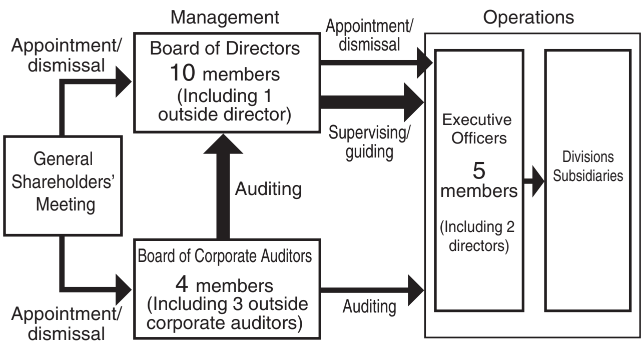
We introduced an executive officer system in April 2002 and shortened the term of office for directors to one year in June 2002. As a result, the Company has changed to a system in which the responsibility of executive officers for operations and the responsibility of the directors for management and supervision have been clarified.

Company Organisation and Internal Control Systems
The information below outlines the situation regarding company organisation and internal control systems as of June 2008, when the financial statements were submitted.

1) Internal Governance Organisation
Regarding corporate governance, the Company employs the corporate auditor system rather than the so-called "committee system." Three of our four corporate auditors are outside corporate auditors, and one of the ten directors is an outside director.

Chart 1 below illustrates the system for operations and management auditing.

(Chart 1)

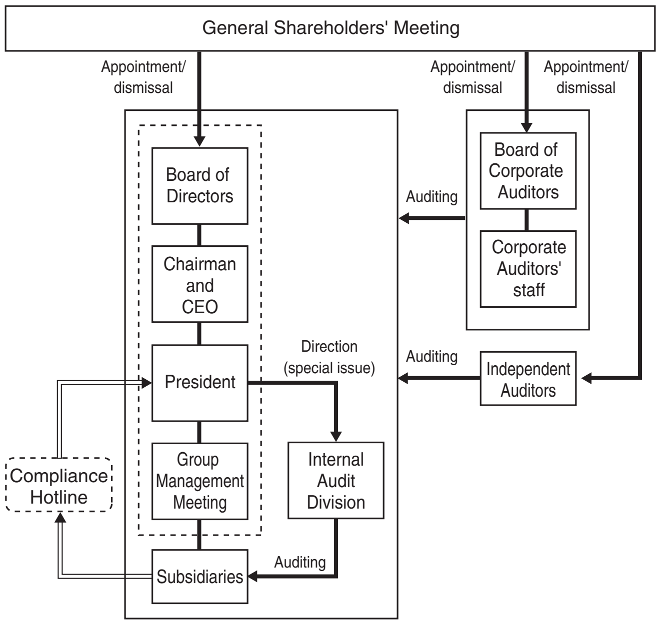


The Company employs the executive officer system. Each director on the Board of Directors individual and the Board of Directors collectively, supervise the performance of the executive officers.

Each corporate auditor on the Board of Corporate Auditors individually and the Board of Corporate Auditors collectively monitor the performance of each executive officer, each director and the Board of Directors.

2) Internal Control and Risk Management Systems

(Chart 2)



The H_2O RETAILING Group has a code of conduct stipulating basic principles so that executives and employees will act based on the Companies' ethics, laws, rules and regulations. The Companies strive to make the code of conduct embraced by both executives and employees. Lectures are held in each subsidiary to enhance consciousness of compliance and to develop a mastery of the basic knowledge of compliance. To this end, the Company appoints an outside director and outside corporate auditors with the knowledge and experience necessary to promote compliance and establish the appropriate risk management systems.

Furthermore, the Companies have compliance meetings as an organisation to execute policies related to compliance. The Companies also appoint the presidents of each subsidiary (Department Store Business: executive officers of Hankyu Department Stores and the Hanshin Department

Store in charge of General Affairs; Supermarket Business: an executive officer of Hanshoku in charge of General Affairs) as the responsible staff for the promotion of information gathering and education on compliance.

Moreover, a Group Compliance Hotline, or whistleblower system, has been established, and a Compliance Hotline has also been established in Hankyu Department Stores, the Hanshin Department Store and Hanshoku, the core business companies within the Group.

As for the Risk Management Systems, the Companies have established risk management regulations, which include guidelines for risk prevention, for reporting risks whey they occur, measures to take when risks occur and how to implement those measures, thereby stipulating basic policies and rules relating to risk management.

The Companies have appointed staff for compliance in every subsidiary to promote information gathering, communication and prompt response to risks, thereby building a compliance network. To prevent risks and minimise the loss caused when risks occur, compliance meetings are held regularly.

3) Internal Audits, Corporate Auditors' Audits and Accounting Audits

The Company has four corporate auditors. Three are outside corporate auditors and one is a full-time auditor from within the Company. Nine auditors' meetings were held during the term.

All corporate auditors attend Board of Directors' meetings, and the full-time corporate auditor attends weekly full-time directors' "830" meetings. The corporate auditors express opinions at these meetings as needed and interview staff in subsidiaries and in each division about the performance of their duties. They also review operation audits through reports from the internal audit division and reinforce auditing functions by reviewing reports from independent auditors, as well as exchanging opinions.

The internal audit division (2 members) is under the direct control of the president and is responsible for internal audits. It makes proposals for improvements based on regular interviews and regular on-site audits and tries to improve the efficiency and quality of audits by reporting the results of internal audits to and regularly exchanging opinions with the corporate auditors.

The Company has designated KPMG AZSA & Co. as its accounting auditing firm. The certified public accountants who executed the accounting audit were Mr.Takashi Yoshida, Mr.Yusuke Kawasaki and Mr.Katsuhiro Wakita. Five other certified public accountants and fourteen other staff assisted them with the audit.

4) Relationships with Outside Director and Outside Corporate Auditors

The Kansai Electric Power Co., Inc., where outside director Mr.Yosaku Fuji works as an adviser, is a corporate customer of the Company, and the Company sells products to Kansai Electric Power Co., Inc. Mr.Fuji resigned as a director of Kansai Electric Power Co., Inc. on 28 June 2007.

Toho Co., Ltd., where outside corporate auditor Mr. Hideyuki Takai is the president and representative director, is a corporate customer of Hankyu Department Stores, Inc. and sells products to Toho Co., Ltd. Toho Co., Ltd. rented store space for Yurakucho Hankyu in Tokyo to Hankyu Department Stores, Inc. from April to September 2007.

Outside corporate auditor Mr.Takeshi Nakagawa has no special interests in the Company. Outside corporate auditor Mr.Toshihisa Takamura is a lawyer and has no special interests in the Company.

Compensation for Directors and Corporate Auditors

The Company paid a total of ¥291 million ($2,910 thousand) in compensation to directors and corporate anditors, ¥283 million ($2,830 thousand) to the directors (¥8 million to outside director) and ¥46 million ($460 thousand) to corporate auditors (¥21 million to outside corporate auditors).

The Company paid an audit fee of ¥42 million ($420 thousand) to KPMG AZSA & Co. Of this total, ¥37 million ($370 thousand) was for the services stipulated in Article 2, Paragraph 1 of the Certified Public Accountant Law and ¥5 million ($50 thousand) was for other services.

Five-Year Summary

H2O RETAILING CORPORATION and Consolidated Subsidiaries

	Millions of yen					Thousands of U.S. dollars (Note1)
Years ended 31st March	2004	2005	2006	2007	**2008**	**2008**
For the year:						
Net sales	¥384,556	¥385,675	¥381,285	¥395,950	**¥471,617**	**$4,716,170**
Cost of sales	271,916	272,210	268,044	279,365	**334,688**	**3,346,880**
Gross profit	112,640	113,465	113,241	116,585	**136,929**	**1,369,290**
Selling, general and administrative expenses	97,421	96,582	98,649	101,821	**119,815**	**1,198,150**
Interest expense	528	338	97	125	**72**	**720**
Income before income taxes	14,744	15,650	13,349	14,308	**16,905**	**169,050**
Net income	8,101	9,107	7,922	8,100	**9,450**	**94,500**
Per share data (in yen and dollars)						
Net income - basic	42.89	48.24	42.28	43.23	**50.07**	**0.50**
Net income - diluted	42.89	45.17	38.13	38.99	**45.19**	**0.45**
Cash dividends	12.50	12.50	12.50	12.50	**12.50**	**0.13**
At year-end:						
Inventories	¥11,578	¥12,664	¥12,355	¥13,050	**¥15,686**	**$156,860**
Property, plant and equipment (book value)	71,038	70,352	66,473	74,788	**80,892**	**808,920**
Total assets	237,029	266,119	276,175	282,759	**337,778**	**3,377,780**
Long-term debt	32,180	29,677	22,000	23,044	**21,159**	**211,590**
Shareholders' equity	113,350	121,835	138,568	143,195	**163,897**	**1,638,970**
Ratio analysis:						
Gross profit / Net sales (%)	29.29	29.42	29.70	29.44	**29.03**	
Income before income taxes / Net sales (%)	3.83	4.06	3.50	3.61	**3.58**	
Net income / Net sales (%)	2.11	2.36	2.08	2.05	**2.00**	
Net income /Total assets (%)	3.39	3.62	2.92	2.90	**3.05**	
Net income / Shareholders' equity (%)	7.57	7.74	6.08	5.75	**6.15**	
Shareholders' equity / Total assets (%)	47.82	45.78	50.17	50.64	**48.52**	
Long-term debt / Shareholders' equity (times)	0.28	0.24	0.16	0.16	**0.13**	
Net sales / Inventories (times)	33.21	30.45	30.86	30.34	**30.07**	
Net sales / Total assets (times)	1.62	1.45	1.38	1.40	**1.40**	

Note 1: U.S. dollar amounts represent translations of yen amounts at the rate of ¥100 = U.S.$1.00.

2: Effective 1st April 2006, the Company adopted the new accounting standard for presentation of net assets in the balance sheet and related guidance (Accounting Standards Board Statement No. 5, "Accounting Standard for Presentation of Net Assets in the Balance Sheet" and Financial Standards Implementation Guidance No. 8, "Implementation Guidance for Accounting Standard for Presentation of Net Assets in the Balance Sheet"). The prior year amount of shareholders' equity has not been restated.

3: As for "Net income / Total assets," the Company uses the average of total assets at the beginning and end of the year. As for "Net income / Shareholders' equity," the Company uses the average of shareholders' equity at the beginning and end of the year.

4: In the five-year summary, Shareholders' equity means Net assets excluding Minority interests in the consolidated subsidiaries.

Consolidated Balance Sheets

As of 31st March, 2006, 2007 and 2008	Millions of yen 2006	Millions of yen 2007	Millions of yen 2008	Thousands of U.S. dollars (Note1) 2008
Assets				
Current assets:				
Cash on hand and in banks (Note 7)	¥48,947	¥45,719	¥59,812	$598,120
Notes and accounts receivable				
Trade	16,528	17,824	24,599	245,990
Other	1,836	2,511	3,572	35,720
Allowance for doubtful receivables	(313)	(303)	(278)	(2,780)
	18,051	20,032	27,893	278,930
Inventories (Note 4)	12,355	13,050	15,686	156,860
Deferred tax assets (Note 14)	3,447	3,228	4,113	41,130
Prepaid expenses and other (Note 3 and 8)	2,812	2,836	3,845	38,450
Total current assets	85,612	84,865	111,349	1,113,490
Investments and long-term loans:				
Investment securities (Note 3)	79,738	65,165	60,565	605,650
Investments in nonconsolidated subsidiaries and affiliates	926	1,009	882	8,820
Long-term loans	2,309	2,592	2,159	21,590
Long-term loans to employees	172	130	237	2,370
Total investments and long-term loans	83,145	68,896	63,843	638,430
Property, plant and equipment				
Land (Note 7 and 16)	28,833	32,747	32,869	328,690
Buildings and structures (Note 7)	90,967	105,535	121,064	1,210,640
Machinery and equipment	11,793	13,552	18,092	180,920
Construction in progress	12	196	376	3,760
	131,605	152,030	172,401	1,724,010
Accumulated depreciation	(65,132)	(77,242)	(91,509)	(915,090)
Total property, plant and equipment	66,473	74,788	80,892	808,920
Other assets:				
Long-term leasehold deposits (Note 5)	33,625	36,980	40,743	407,430
Goodwill (Note 2)	—	9,774	18,938	189,380
Intangibles	2,807	3,162	5,985	59,850
Long-term deferred tax assets (Note 14)	4,185	3,535	14,084	140,840
Long-term deferred tax assets related to land revaluation (Note 16)	—	308	—	—
Interest swaps	227	132	69	690
Other assets	310	502	1,983	19,830
Allowance for doubtful receivables	(209)	(183)	(108)	(1,080)
Total other assets	40,945	54,210	81,694	816,940
	¥276,175	¥282,759	¥337,778	$3,377,780

See accompanying notes.

	Millions of yen			Thousands of U.S. dollars
	2006	2007	2008	2008
Liabilities and Net Assets				
Current liabilities:				
Current portion of long-term debt (Notes 6 and 7)	¥ 8,384	¥ 2,324	¥ 1,324	$ 13,240
Notes and accounts payable:				
Trade	23,407	26,216	36,385	363,850
Other	6,513	6,897	9,070	90,700
	29,920	33,113	45,455	454,550
Accrued expenses	5,089	5,302	2,524	25,240
Income and enterprise taxes payable	3,646	4,271	5,443	54,430
Consumption tax payable	274	395	1,575	15,750
Advances received	23,624	24,975	34,725	347,250
Provision for bonuses to employees (Note 2)	—	—	4,798	47,980
Provision for bonuses to directors and corporate auditors (Note 2)	59	72	135	1,350
Provision for loss of stores rebuilding (Note 2)	—	—	956	9,560
Provision for loss of Umeda main store rebuilding (Note 2)	111	—	—	—
Other current liabilities	2,745	3,080	3,180	31,800
Total current liabilities	73,852	73,532	100,115	1,001,150
Long-term debt (Note 6 and 7)	22,000	23,044	21,159	211,590
Long-term deferred tax liabilities (Note 14)	15,348	14,105	19,439	194,390
Long-term deferred tax liabilities related to land revaluation (Note 16)	344	348	348	3,480
Employees' severance and retirement benefits (Note 9)	11,826	12,843	17,975	179,750
Directors' severance and retirement benefits	376	462	541	5,410
Provision for loss of stores rebuilding (Note 2)	—	5,390	4,272	42,720
Provision for loss of Umeda Main Store rebuilding (Note 2)	4,296	—	—	—
Provision for redemption of gift certificates (Note 2)			1,685	16,850
Long-term payables accrued	773	75	47	470
Guarantee deposits	6,629	7,877	7,963	79,630
Deferred hedge gains	227	—	—	—
Other noncurrent liabilities	119	191	247	2,470
Contingent liabilities (Note 11)				
Total liabilities	135,790	137,867	173,791	1,737,910
Net assets (Note 15)				
Shareholders' equity:				
Common stock: Authorised - 300,000,000 shares Issued - 187,688,301 shares in 2006 and 2007 - 206,740,777 shares in 2008	17,797	17,797	17,797	177,970
Capital surplus	17,577	17,580	37,172	371,720
Retained earnings	80,340	86,091	92,388	923,880
Treasury stock - 321,437 shares in 2006 - 345,561 shares in 2007 - 183,302 shares in 2008	(252)	(288)	(192)	(1,920)
Total shareholders' equity	115,462	121,180	147,165	1,471,650
Accumulated gains from revaluation and translation:				
Net unrealised holding gains on securities	24,546	22,970	16,840	168,400
Deferred hedge gains	—	79	41	410
Land revaluation, net of tax (Note 16)	(1,112)	(797)	43	430
Foreign currency translation adjustments	(328)	(237)	(191)	(1,910)
Total accumulated gains from revaluation and translation	23,106	22,015	16,733	167,330
Minority interests in consolidated subsidiaries	1,817	1,697	89	890
	140,385	144,892	¥163,987	1,639,870
	¥276,175	282,759	337,778	$3,377,780

Consolidated Statements of Income

Years ended 31st March	Millions of yen 2006	Millions of yen 2007	Millions of yen 2008	Thousands of U.S. dollars (Note1) 2008
Net sales	¥381,285	¥395,950	¥471,617	$4,716,170
Cost of sales	268,044	279,365	334,688	3,346,880
Gross profit	113,241	116,585	136,929	1,369,290
Selling, general and administrative expenses	98,649	101,821	119,815	1,198,150
Operating income	14,592	14,764	17,114	171,140
Other income (expenses):				
Interest and dividend income	655	874	863	8,630
Equity in earnings (losses) of affiliated companies	22	99	(268)	(2,680)
Amortisation of negative goodwill	238	150	75	750
Gain on reversal of provision for loss of stores rebuilding	—	—	228	2,280
Gain on reversal of provision for loss of Umeda Main Store rebuilding	—	901	—	—
A bonus dividend	—	640	—	—
Gain on sales of investment in consolidated subsidiary	3,036	—	—	—
Compensation for moving	2,028	—	—	—
Gain on sales of property, plant and equipment (Note 19)	189	—	2,391	23,910
Gain on the revision of employees' severance and retirement benefits plans (Note 9)	—	—	—	—
Gain on donations of property, plant and equipment	—	—	200	2,000
Interest expense	(97)	(125)	(72)	(720)
Loss of stores rebuilding (Note 20)	—	(1,994)	(67)	(670)
Loss on disposal of property, plant, equipment and intangibles (Note 23)	(1,218)	(743)	(812)	(8,120)
Loss on restructuring of subsidiary business	(621)	(597)	—	—
Loss of Umeda main store rebuilding (Note 21)	(2,936)	—	—	—
Impairment losses (Note 22)	(2,664)	—	(867)	(8,670)
Outplacement expenses	(719)	—	(249)	(2,490)
Expenses for opening new store	—	—	(418)	(4,180)
Loss on provision for redemption ot gift certificates	—	—	(882)	(8,820)
Loss on provision for redemption of gift certificates for prior periods	—	—	(1,131)	(11,310)
Loss on depreciation of property, plant, equipment and intangibles	—	—	(354)	(3,540)
Loss on decrease in investment in affiliated company	—	—	(57)	(570)
Other, net	844	339	1,211	12,110
	(1,243)	(456)	(209)	(2,090)
Income before income taxes	13,349	14,308	16,905	169,050
Income taxes (Note 14)**:**				
Current	4,295	5,645	6,821	68,210
Deferred	1,002	653	628	6,280
	5,297	6,298	7,449	74,490
Minority interests (losses)	130	(90)	6	60
Net income	¥7,922	¥8,100	¥9,450	$94,500

	Yen 2006	Yen 2007	Yen 2008	U.S. dollars (Note 1) 2008
Net income per share - basic	¥42.28	¥43.23	¥50.07	$0.50
Net income per share - diluted	¥38.13	¥38.99	¥45.19	$0.45
Cash dividends	¥12.50	¥12.50	¥12.50	$0.13

See accompanying notes.

Consolidated Statements of Changes in Net Assets

Years ended 31st March	Thousands	Millions of yen								
	Number of shares of common stock	Common stock	Capital surplus	Retained earnings	Treasury stock	Net unrealised holding gains (losses) on securities	Deferred hedge gains	Land revaluation, net of tax (Note 16)	Foreign currency translation adjustments	Minority interests in consolidated subsidiaries
Balance at 31st March 2005	187,688	¥17,797	¥17,574	¥74,824	(¥213)	¥12,608	—	(¥429)	(¥326)	¥1,712
Cash dividends - ¥12.5 per share	—	—	—	(2,342)	—	—	—	—	—	—
Net income	—	—	—	7,922	—	—	—	—	—	—
Gain on treasury stock	—	—	3	—	(39)	—	—	—	—	—
Land revaluation, net of tax (Note 16)	—	—	—	—	—	—	—	(683)	—	—
Increase resulting from decrease in number of equity method affiliates	—	—	—	2	—	—	—	—	—	—
Increase in net unrealised holding gains on securities	—	—	—	—	—	11,938	—	—	—	—
Deferred hedge gains	—	—	—	—	—	—	—	—	—	—
Adjustments from translation of foreign currency financial statements	—	—	—	—	—	—	—	—	(2)	—
Bonuses to directors and corporate auditors	—	—	—	(66)	—	—	—	—	—	—
Minority interests in consolidated subsidiaries	—	—	—	—	—	—	—	—	—	105
Balance at 31st March 2006	187,688	¥17,797	¥17,577	¥80,340	(¥252)	¥24,546	—	(¥1,112)	(¥328)	¥1,817
Cash dividends - ¥12.5 per share	—	—	—	(2,342)	—	—	—	—	—	—
Net income	—	—	—	8,100	—	—	—	—	—	—
Gain on treasury stock	—	—	3	—	(36)	—	—	—	—	—
Land revaluation, net of tax (Note 16)	—	—	—	(7)	—	—	—	315	—	—
Decrease resulting from increase in number of consolidated subsidiaries	—	—	—	—	—	—	—	—	—	—
Decrease in net unrealised holding gains on securities	—	—	—	—	—	(1,576)	—	—	—	—
Deferred hedge gains	—	—	—	—	—	—	79	—	—	—
Adjustments from translation of foreign currency financial statements	—	—	—	—	—	—	—	—	91	—
Minority interests in consolidated subsidiaries	—	—	—	—	—	—	—	—	—	(120)
Balance at 31st March 2007	187,688	¥17,797	¥17,580	¥86,091	(¥288)	¥22,970	¥79	(¥797)	(¥237)	¥1,697
Cash dividends - ¥12.5 per share	—	—	—	(2,241)	—	—	—	—	—	—
Net income	—	—	—	9,450	—	—	—	—	—	—
Gain and loss on treasury stock	—	—	(16)	(29)	95	—	—	—	—	—
Stock exchange	19,052	—	19,608	—	1	—	—	—	—	—
Land revaluation, net of tax (Note 16)	—	—	—	(840)	—	—	—	840	—	—
Decrease resulting from increase in number of consolidated subsidiaries	—	—	—	(43)	—	—	—	—	—	—
Decrease in net unrealised holding gains on securities	—	—	—	—	—	(6,130)	—	—	—	—
Deferred hedge gains	—	—	—	—	—	—	(38)	—	—	—
Adjustments from translation of foreign currency financial statements	—	—	—	—	—	—	—	—	46	—
Minority interests in consolidated subsidiaries	—	—	—	—	—	—	—	—	—	(1,607)
Balance at 31st March 2008	206,740	¥17,797	¥37,172	¥92,388	(¥192)	¥16,840	¥41	¥43	(¥191)	¥90

	Thousands of U.S. dollars (Note 1)								
	Common stock	Capital surplus	Retained earnings	Treasury stock	Net unrealised holding gains (losses) on securities	Deferred hedge gains	Land revaluation, net of tax (Note 16)	Foreign currency translation adjustments	Minority interests in consolidated subsidiaries
Balance at 31st March 2007	$177,970	$175,800	$860,910	($2,880)	$229,700	$790	($7,970)	($2,370)	$16,970
Cash dividends - $0.11 per share	—	—	(22,410)	—	—	—	—	—	—
Net income	—	—	94,500	—	—	—	—	—	—
Gain and loss on treasury stock	—	(160)	(290)	950	—	—	—	—	—
Stock exchange	—	196,080	—	10	—	—	—	—	—
Land revaluation, net of tax (Note 16)	—	—	(8,400)	—	—	—	8,400	—	—
Decrease resulting from increase in number of consolidated subsidiaries	—	—	(430)	—	—	—	—	—	—
Decrease in net unrealised holding gains on securities	—	—	—	—	(61,300)	—	—	—	—
Deferred hedge gains	—	—	—	—	—	(380)	—	—	—
Adjustments from translation of foreign currency financial statements	—	—	—	—	—	—	—	460	—
Minority interests in consolidated subsidiaries	—	—	—	—	—	—	—	—	(16,070)
Balance at 31st March 2008	$177,970	$371,720	$923,880	($1,920)	$168,400	$410	$430	($1,910)	$900

See accompanying notes.

Consolidated Statements of Cash Flows

Years ended 31st March	Millions of yen 2006	Millions of yen 2007	Millions of yen 2008	Thousands of U.S. dollars (Note1) 2008
Cash flows from operating activities:				
Income before income taxes	¥13,349	¥14,308	¥16,905	$169,050
Depreciation and amortisation	6,726	7,038	7,731	77,310
Loss on disposal of property, plant, equipment and intangible assets	1,218	743	812	8,120
Impairment loss	2,664	—	867	8,670
Decrease in allowance for doubtful receivables	(164)	(118)	(146)	(1,460)
Increase in provision for bonuses to employees	—	—	2,516	25,160
Increase in provision for bonuses to directors and corporate auditors	—	—	46	460
Increase in provision for retirement benefits	236	880	146	1,460
Increase in provision for redemption of gift certificates	—	—	1,685	16,850
Interest and dividend income	(655)	(874)	(863)	(8,630)
Interest expense	97	125	72	720
Gain on sales of property, plant and equipment	(189)	—	(2,391)	(23,910)
Gain on sales of investment in consolidated subsidiary	(3,036)	—	—	—
Decrease (increase) in notes and accounts receivable	1,485	(1,136)	(2,861)	(28,610)
Decrease (increase) in inventories	(150)	310	582	5,820
Increase (decrease) in notes and accounts payable	(1,404)	497	1,540	15,400
Increase (decrease) in consumption tax payable	(235)	76	1,028	10,280
Bonuses payable to directors and corporate auditors	(67)	(60)	—	—
Other	2,310	1,299	(1,719)	(17,190)
	22,185	23,088	25,950	259,500
Interest and dividends received	663	920	875	8,750
Interest paid	(110)	(125)	(76)	(760)
Income tax paid	(7,775)	(5,050)	(6,642)	(66,420)
Net cash provided by operating activities	14,963	18,833	20,107	201,070
Cash flows from investing activities:				
Net decrease (increase) in time deposits	(5,000)	5,000	—	—
Additions to property, plant and equipment	(9,616)	(5,294)	(10,262)	(102,620)
Proceeds from disposal of property, plant and equipment	343	957	8,119	81,190
Additions to intangibles	(1,014)	(831)	(1,447)	(14,470)
Proceeds from disposal of intangibles	12	82	94	940
Investment in securities	(8,576)	(175)	(1,508)	(15,080)
Proceeds from sales of investment securities	8,503	11,992	658	6,580
Payments for the purchase of stock of subsidiary accompanied by a change in the scope of consolidation	—	(15,370)	21,336	213,360
Proceeds from the sale of stock of subsidiary accompanied by a change in the scope of consolidation	3,679	—	—	—
Payments for long-term loans receivable	—	—	—	—
Proceeds from collection of long-term loans receivable	4,332	562	562	5,620
Net cash used in investing activities	(7,337)	(3,077)	17,552	175,520
Cash flows from financing activities:				
Net decrease in short-term debt	(11)	(2,800)	—	—
Repayments of long-term debt	(6,441)	(3,175)	(2,885)	(28,850)
Payments for redemption of bonds	—	(5,817)	—	—
Dividends paid	(2,366)	(2,366)	(2,264)	(22,640)
Proceeds from sale of treasury stock	36	54	142	1,420
Additions to treasury stock	(72)	(87)	(18,609)	(186,090)
Net cash used in financing activities	(8,854)	(14,191)	(23,616)	(236,160)
Foreign exchange differences in cash and cash equivalents	(2)	92	46	460
Net increase (decrease) in cash and cash equivalents	(1,230)	1,657	14,089	140,890
Cash and cash equivalents at beginning of year	40,158	38,928	40,595	405,950
Cash and cash equivalents at beginning of year of newly consolidated subsidiaries	—	10	4	40
Cash and cash equivalents at end of year	¥38,928	¥40,595	¥54,688	$546,880
Reconciliation to balance sheet:				
Cash and cash equivalents:				
Cash on hand and in banks in the balance sheet	¥48,947	¥45,719	¥59,812	$598,120
Time deposits with maturities exceeding three months	(10,019)	(5,124)	(5,124)	(51,240)
Total	¥38,928	¥40,595	¥54,688	$546,880

See accompanying notes.

Notes to the Consolidated Financial Statements

H2O RETAILING CORPORATION and Consolidated Subsidiaries

1. Basis of Presenting Consolidated Financial Statements

The accompanying consolidated financial statements have been prepared in accordance with the provisions set forth in the Japanese Financial Instruments and Exchange Law which took effect on 30th September 2007, replacing the Japanese Securities and Exchange Law and its related accounting regulations and in conformity with accounting principles generally accepted in Japan, which are different in certain respects as to application and disclosure requirements from International Financial Reporting Standards. The accounts of overseas subsidiary are based on their accounting records maintained in conformity with generally accepted accounting principles and practices prevailing in the country of domicile.

H2O RETAILING CORPORATION (the "Company") and its consolidated domestic subsidiaries maintain their official accounting records in Japanese yen, and the accompanying consolidated financial statements have been restructured and translated into English, with some expanded descriptions, from the consolidated financial statements of the Company prepared in accordance with Japanese GAAP and filed with the appropriate Local Finance Bureau of the Ministry of Finance as required by the Financial Instruments and Exchange Law. Some supplementary information included in the statutory Japanese language consolidated financial statements, but not required for fair presentation, is not presented in the accompanying consolidated financial statements.

The translation of the Japanese yen amounts into U.S. dollar amounts is included solely for the convenience of readers outside Japan, using the prevailing exchange rate at 31st March 2008, which was ¥100 to U.S.$1.00. The translations should not be construed as representations that the Japanese yen amounts have been, could have been, or could in the future be converted into U.S. dollars at this or any other rate of exchange.

2. Summary of Significant Accounting Policies

Consolidation and investments in affiliates

The accompanying consolidated financial statements include the accounts of the Company and significant companies (together the "Companies") over which the Company has power of control through majority voting rights or the existence of certain other conditions evidencing control by the Company.

Investments in affiliates over which the Company has the ability to exercise significant influence over operating and financial policies are accounted for by the equity method.

The consolidated financial statements include the accounts of the Company and its 47 (38 in 2007 and 34 in 2006) significant majority owned subsidiaries. All significant inter-company transactions and accounts have been eliminated in consolidation.

In the year ended 31st March 2008, the Company made Hanshin Department Store, Ltd. a subsidiary by a stock-for-stock exchange.

In the year ended 31st March 2007, the Company purchased all the stock of Nissho, a supermarket business. The Company also set up Hanshoku and Hankyu Foods as new subsidiaries and took into account Mameda as a subsidiary.

In the year ended 31st March 2006, the Company sold the stock of Hankyu Kyoei Pharmacy Co., Ltd., a drugstore subsidiary, and recorded a gain of ¥3,036 million.

One of the consolidated subsidiaries has a financial year ending on 31st December. With respect to the period from the subsidiary's year-end to 31st March, necessary adjustments are made for significant transactions to reflect them appropriately in the consolidated financial statements.

In the elimination of investments in consolidated subsidiaries, the assets and liabilities of the subsidiaries, including the portion attributable to minority shareholders, are evaluated using the fair value at the time the Company acquired control of the respective subsidiary.

The difference between the cost of investments in consolidated subsidiaries and the equity in their net assets at dates of acquisition has been, with minor exceptions, amortised over five to twenty years.

The equity method has been applied to 7 (6 in 2006 and 2007) affiliates for the year ended 31st March 2008.

Investments in nonconsolidated subsidiaries and non-equity-method affiliates are accounted for at cost because of the immaterial effect on the consolidated financial statements. Income from these nonconsolidated subsidiaries and non-equity-method affiliates is recognised only when the Companies receive dividends.

Cash flow statements

In preparing the consolidated statements of cash flows, cash on hand, readily available deposits and short-term highly liquid investments with maturities not exceeding three months at the time of purchase are considered to be cash and cash equivalents.

Securities

Investment securities consist principally of marketable and non-marketable equity securities. The Companies categorise the securities as "available-for-sale." Available-for-sale securities with fair market values are stated at fair value. Unrealised holding gains and losses on these securities are reported, net of applicable income taxes, as a separate component of net assets. Realised gains and losses on sales of such securities are principally determined by the average cost method. Available-for-sale securities with no fair market value are stated at average cost.

If the fair market value of available-for-sale securities declines significantly, the securities are stated at fair market value, and the difference between fair market value and the carrying amount is recognised as loss in the period of decline. If the net asset value of available-for-sale securities with no available fair market value declines significantly, the securities are written down to the net asset value and charged to income. In these cases, the fair market value or the net asset value will be carried forward as book value to the next year.

Allowance for doubtful receivables

The allowance for doubtful receivables is provided in amounts management considers sufficient to cover possible losses on collection. With respect to normal trade accounts receivable, it is stated at an amount based on the actual rate of historical bad debts, and for certain doubtful receivables, the uncollectible amount is individually estimated.

Inventories

Inventories are stated at cost, which is determined principally by the retail cost method.

Property, plant and equipment

Property, plant and equipment are carried at cost. Depreciation is computed principally by the declining balance method at rates based on the estimated useful life of the assets. Expenditures for maintenance and repairs, including minor replacements and betterments, are charged to income as incurred.

Buildings acquired after 1st April 1998 (excluding peripheral facilities) are depreciated using the straight-line method.

The estimated useful life of the assets are as follows:

Buildings and structures: 3 to 50 years
Machinery and equipment: 3 to 20 years

Goodwill

The difference between the cost of investments in consolidated subsidiaries and the equity in their net assets at the date of acquisition are with minor exceptions, amortised over five to twenty years. The investments in the Hanshin Depertment Store, Ltd. and the Hankyu Nissho Store are amortised over twenty years.

Software

Software is amortised using the straight-line method over the estimated useful life of five years.

Bonuses to employees

The Companies accrue estimated amounts of employee bonuses based on the estimated amount to be paid in the subsequent period. Provision for bonuses to employees, which was included in “other current liabilities” until the year ended 31st March 2007, is presented separately from the year ended 31st March 2008. As of 31st March 2007, ¥3,978 million was included “other current liabilities” as provision for bonuses to employees.

Bonuses to directors and corporate auditors

Commencing with the year ended 31st March 2007, the Company accrues bonuses for directors and corporate auditors based on the estimated payments to be made after the end of the year. Previously, the Company treated bonuses for directors and corporate auditors as an appropriation of retained earnings at the time of approval by the shareholders. However, the Company now treats bonuses to directors and corporate auditors as an expense at the time of accrual, in compliance with the new accounting treatment of bonuses for directors and corporate auditors (Accounting Standards Board of Japan’s practical guidance report No. 13, 9th March 2004).

Retirement benefits

The Companies provide two types of post-employment benefit plans, unfunded lump-sum payment plans and funded contributory and noncontributory pension plans, under which all eligible employees are entitled to benefits based on the level of wages and salaries at the time of retirement or termination, length of service and certain other factors.

Hankyu Department Stores, Inc. has a retirement benefits plan which consists of unfunded lump-sum payment plans (50% of the whole plan), contributory pension plans (25% of the whole plan) and noncontributory pension plans (25% of the whole plan). Other subsidiaries also have unfunded lump-sum payment plans, contributory pension plans or noncontributory pension plans. The employees of the Company are all seconded from the consolidated subsidiaries and provided with the respective subsidiary's post-employment benefit plans.

The Companies provide for employees’ severance and retirement benefits based on the estimated amounts of projected benefit obligation and the fair value of plan assets.

Prior service costs are mainly recognised in expenses when incurred, and actuarial gains and losses are recognised in expenses in equal amounts within the average of the estimated remaining service years (mainly over 13 years) commencing with the following period.

With regard to retirement benefits for directors and corporate auditors of the Company and certain consolidated subsidiaries, the liability for lump-sum payments is stated at the amount which would be required to be paid if they retired as of the balance sheet date.

The Companies have executive officers' severance and retirement benefits. The amount of liability as of 31st March 2006, 2007 and 2008 was ¥105 million, ¥123 million, and ¥142 million ($1,420 thousand), respectively.

Derivative and hedge accounting
Derivative financial instruments are stated at fair value, and changes in fair value are recognised as gains or losses unless the derivative financial instruments are used for hedging purposes. All derivative financial instruments are used as hedges and meet certain hedging criteria. The Companies defer recognition of gains or losses resulting from changes in fair value of derivative financial instruments until the related losses or gains on the hedged items are recognised.

Translation of foreign currencies
Monetary assets and liabilities denominated in foreign currency are translated into Japanese yen at the rates prevailing at each balance sheet date, and the resulting translation gains or losses are charged to income.

In the translation of the financial statements of the overseas subsidiary, assets, liabilities, revenues and expenses are translated at the rates prevailing at the subsidiary's balance sheet date and shareholders' equity accounts are translated at historical rates. The resulting foreign currency translation adjustments are shown as a separate component of net assets.

Finance leases
Except for leases with covenants transferring ownership of the property to the lessee, the Companies do not capitalise finance leases.

Reclassifications
Certain amounts in prior years were reclassified to conform to the 2008 presentation. These changes had no impact on previously reported results of operations.

Provision for loss of stores rebuilding
The Companies made a provision to cover estimated losses arising from the rebuilding of the Umeda Main Store, Hankyu-Oi Building and Oi Development Building. The estimates of these losses were based on historical precedents, the book value of the stores' property at the time of demolition, and the estimated cost of the demolition work for the year ended 31st March 2008.

With the expansion of the rebuilding plans, the provision for loss of the Umeda Main Store rebuilding is included in the provision for loss of stores rebuilding from the year ended 31st March 2007.

Gain on reversal in provision for loss of stores rebuilding is due to the decrease in the book value of Umeda Main Store's property, accompanied by the extension of the rebuilding period.

Provision for loss of Umeda Main Store Rebuilding
The Companies made a provision to cover estimated losses arising from the rebuilding of the Umeda Main Store. The estimates of these losses were based on historical precedents, the book value of the store property at the time of demolition, and the estimated cost of the demolition work.

Provision for redemption of gift certificates
The Company records a liability for gift certificates upon the issuance of certificates to its customers. If gift certificates are not redeemed by customers within a certain time period, the Company reverses the liability and recognises a gain. A provision is recorded by the Company for the unredeemed gift certificates previously recognised as a gain based on the estimated future redemptions of those certificates.

(Change in accounting policies)
For gift certificates not redeemed by customers within a certain time period, the Company previously reversed the liability associated with unredeemed gift certificates and recognised a gain in other nonoperating income, in the same manner as that under Corporate Tax Law. Beginning with the current fiscal year, the Company records a provision for the unredeemed gift certificates based on the estimated future redemptions of those certificates.

The reason for this change in accounting policies is to more accurately present profits and losses for the period and to present a more sound financial position by recording the provision. This is reflective of the concept in the Japanese Institute of Certified Public Accountants Auditing and Assurance Practice Committee Report No. 42, April 13, 2007, "Audit Treatment of Reserves Under the Special Taxation Measures Law, Allowance and Reserves Under Special Laws, and Reserves for Officers' Retirement Benefits."

As of the beginning of the current fiscal year, the Company recognised an extraordinary loss of ¥1,130 million related to the provision and change in accounting policy. The Company additionally recorded ¥177 million of provision during the current year. As a result, ordinary income and income before income taxes for the current fiscal year were ¥177 million and ¥1,308 million less, respectively, than the amounts that would have been recorded with the previous accounting policy.

Accounting Standard for Presentation of Net Assets in the Balance Sheet
Effective from the year ended 31st March, 2007, the Company and its consolidated subsidiaries adopted the new accounting standard, "Accounting Standard for Presentation of Net Assets in the Balance Sheet" (Statement No. 5 issued by the Accounting Standards Board of Japan on 9th December 2005), and the "Implementation guidance for the accounting standard

and the "Implementation guidance for the accounting standard for presentation of net assets in the balance sheet" (the Financial Accounting Standard Implementation Guidance No. 8 issued by the Accounting Standards Board of Japan on 9th December 2005), (collectively, the "New Accounting Standards").

Under the New Accounting Standards, the balance sheet comprises three sections, which are the assets, liabilities and net assets sections. Previously, the balance sheet comprised the assets, liabilities, minority interests, as applicable, and the shareholders' equity sections.

Under the New Accounting Standards, the following items are presented differently compared to the previous presentation. The net assets section includes unrealised gains (losses) on hedging derivatives, net of taxes. Under the previous presentation rules, companies were required to present unrealised gains (losses) on hedging derivatives in the assets or liabilities section without consideration for the related income tax effects. Share subscription rights and minority interests are required to be included in the net assets section under the New Accounting Standards. Under the previous presentation rules, companies were required to present minority interests in consolidated subsidiaries between the noncurrent liabilities and shareholders' equity sections, respectively.

The adoption of the New Accounting Standards had no impact on the consolidated statement of income for the years ended 31st March 2006 and 2007. Also, if the New Accounting Standards had not been adopted at 31st March 2007, shareholders' equity amounting to ¥143,116 million would have been presented.

Accounting Standard for Statement of Changes in Net Assets

Effective from the year ended 31st March 2007, the Company and its consolidated subsidiaries adopted the new accounting standard, "Accounting Standard for Statement of Changes in Net Assets" (Statement No. 6 issued by the Accounting Standards Board of Japan on 27th December 2005), and the "Implementation guidance for the accounting standard for statement of changes in net assets" (the Financial Accounting Standard Implementation Guidance No. 9 issued by the Accounting Standards Board of Japan on 27th December 2005), (collectively, the "Additional New Accounting Standards").

Accordingly, the Company prepared the statement of changes in net assets for the year ended 31st March 2007 in accordance with the Additional New Accounting Standards. Also, the Company voluntarily prepared the consolidated statement of changes in net assets for 2005 and 2006 in accordance with the Additional New Accounting Standards. Previously, consolidated statements of shareholders' equity were prepared for the purpose of inclusion in the consolidated financial statements although not required under Japanese GAAP.

Bond issue expenses

Bond issue expenses are charged to expenses when incurred.

Net income per share

Computations of basic net income per share are based on the weighted average number of shares outstanding during each period. As for diluted net income per share for the years ended 31st March 2006, 2007 and 2008, see Note 25.

Consumption taxes

Consumption taxes are excluded from the revenue and expense accounts which are subject to such taxes.

3. Investment Securities

The following tables summarise acquisition costs and book values (fair values) of available-for-sale securities with available fair values as of 31st March 2006, 2007 and 2008.

Securities with book values exceeding acquisition costs:

	Millions of yen									Thousands of U.S. dollars		
	2006			2007			**2008**			**2008**		
	Acquisition cost	Book value	Difference	Acquisition cost	Book value	Difference	Acquisition cost	Book value	Difference	Acquisition cost	Book value	Difference
Equity securities	¥ 20,267	¥ 61,305	¥ 41,038	¥ 20,309	¥ 58,674	¥ 38,365	**¥ 19,693**	**¥ 48,016**	**¥ 28,323**	**$ 196,930**	**$ 480,160**	**$ 283,230**
Government bonds	701	702	1	-	-	-	**-**	**-**	**-**	**-**	**-**	**-**
Other	11,561	11,663	102	205	208	3	**5,690**	**5,773**	**83**	**56,900**	**57,730**	**830**
Total	¥ 32,529	¥ 73,670	¥ 41,141	¥ 20,514	¥ 58,882	¥ 38,368	**¥ 25,383**	**¥ 53,789**	**¥ 28,406**	**$ 253,830**	**$ 537,890**	**$ 284,060**

Other securities:

	Millions of yen									Thousands of U.S. dollars		
	2006			2007			**2008**			**2008**		
	Acquisition cost	Book value	Difference	Acquisition cost	Book value	Difference	Acquisition cost	Book value	Difference	Acquisition cost	Book value	Difference
Equity securities	¥ 184	¥ 142	(¥ 42)	¥ 367	¥ 262	(¥ 105)	**¥ 1,595**	**¥ 1,216**	**(¥ 379)**	**$ 15,950**	**$ 12,160**	**($ 3,790)**
Government bonds	10	10	-	10	10	-	**-**	**-**	**-**	**-**	**-**	**-**
Other	-	-	-	-	-	-	**1,145**	**1,091**	**(54)**	**11,450**	**10,910**	**(540)**
Total	¥ 194	¥ 152	(¥ 42)	¥ 377	¥ 272	(¥ 105)	**¥ 2,740**	**¥ 2,307**	**(¥ 433)**	**$ 27,400**	**$ 23,070**	**($ 4,330)**

The following table summarises book values of securities with no available fair values as of 31st March 2006, 2007 and 2008:

	Millions of yen			Thousands of U.S. dollars
	2006 Book value	2007 Book value	**2008** Book value	**2008** Book value
Non-listed equity securities	¥ 5,916	¥ 6,011	**¥ 5,566**	**$ 55,660**

The following table summarises maturities of available-for-sale securities that have maturities as of 31st March 2008:

	Millions of yen				Thousands of U.S. dollars			
	Within 1 year	Over 1 year but within 5 years	Over 5 years but within 10 years	Over 10 years	Within 1 year	Over 1 year but within 5 years	Over 5 years but within 10 years	Over 10 years
Government bonds	¥ 1,107	¥ 2,032	¥ 727	¥ 338	$ 11,070	$ 20,320	$ 7,270	$ 3,380

The following table summarises sales of available-for-sale securities for the years ended 31st March 2006, 2007 and 2008:

	Millions of yen									Thousands of U.S. dollars		
	2006			2007			**2008**			**2008**		
	Sales	Gains on sales	Losses on sales	Sales	Gains on sales	Losses on sales	Sales	Gains on sales	Losses on sales	Sales	Gains on sales	Losses on sales
Equity securities	¥ 1	-	-	¥ 5	5	-	**¥ 1**	**-**	**-**	**$ 10**	**-**	**-**

4. Inventories

Inventories at 31st March 2006, 2007 and 2008 consisted of the following:

	Millions of yen			Thousands of U.S. dollars
	2006	2007	**2008**	**2008**
Merchandise goods and finished goods	¥ 11,173	¥ 12,109	**¥ 15,001**	**$ 150,010**
Work in progress	842	135	**67**	**670**
Raw materials and supplies	340	806	**618**	**6,180**
	¥ 12,355	¥ 13,050	**¥ 15,686**	**$ 156,860**

5. Long-term Leasehold Deposits

In connection with its department store business, the Company has entered into long-term lease agreements for store sites and premises. Under such agreements, lessors in Japan generally require the lessee to make substantial deposits in addition to monthly rental payments. A large portion of such deposits is refundable, generally by 10 to 15 equal annual installments commencing in the eleventh year of the lease term, with the balance refundable only on termination of the lease. The deposits bear no interest or bear interest only at a nominal rate.

6. Short-term Bank Loans and Long-term Debt

There were no short-term bank loans as of 31st March 2006, 2007 and 2008.
Long-term debt at 31st March 2006, 2007 and 2008 consisted of the following:

	Millions of yen			Thousands of U.S. dollars
	2006	2007	**2008**	**2008**
1.34% to 3.17% loans from banks and others, due through 2008	¥ 4,500	¥ 5,368	**¥ 2,483**	**$ 24,830**
5.60% Euro dollar bonds, due 2006	5,884	-	**-**	**-**
Zero coupon convertible bonds, due 2011	20,000	20,000	**20,000**	**200,000**
	30,384	25,368	**22,483**	**224,830**
Less amounts due within one year	(8,384)	(2,324)	**(1,324)**	**(13,240)**
	¥ 22,000	¥ 23,044	**¥ 21,159**	**$ 211,590**

In the year ended 31st March 2005, the Company entered into debt assumption agreements with banks for ¥6,800 million ($57,627 thousand) 3.05% bonds due in 2009.

The Company remains contingently liable, however, on the amounts assumed by the banks.

The current conversion price of the zero coupon convertible bonds issued by the Company on 16th August 2004 is ¥982 ($8.30). The convertible bonds are convertible into 20,366,598 shares of common stock as of 31st March 2007.

Annual maturities of long-term debt at 31st March 2008 were as follows:

Year ending 31st March,	Millions of yen	Thousands of U.S. dollars
2009	**¥ 1,324**	**$ 13,240**
2010	**72**	**720**
2011	**-**	**-**
2012	**20,000**	**200,000**
2013 and thereafter	**1,087**	**10,870**
	¥ 22,483	**$ 224,830**

7. Pledged Assets

The following assets were pledged as collateral for the current portion of long-term debt of ¥324 million ($3,240 thousand) and long-term debt of ¥1,159 million ($11,590 thousand) at 31st March 2008:

	Millions of yen	Thousands of U.S. dollars
Time deposits	**¥ 5**	**$ 50**
Buildings	**1,953**	**19,530**
Land	**890**	**8,900**
	¥ 2,848	**$ 28,480**

8. Deposited Securities

Certain securities, included in investment securities, were deposited with the Ministry of Justice in accordance with the relevant laws regarding the following transactions:

	Millions of yen			Thousands of U.S. dollars
	2006	2007	**2008**	**2008**
Installment sales transactions	¥ 702	¥ -	**¥ 1,955**	**$ 19,550**
Real estate transactions	10	10	**-**	**-**
Law on gift certificates	-	-	**2,239**	**22,390**
	¥ 712	¥ 10	**¥ 4,194**	**$ 41,940**

9. Employees' Severance and Retirement Benefits

The liabilities for severance and retirement benefits included in the liability section of the consolidated balance sheets as of 31st March 2006, 2007 and 2008 consisted of the following:

	Millions of yen			Thousands of U.S. dollars
	2006	2007	**2008**	**2008**
Projected benefit obligation	¥ 28,726	¥ 31,423	**¥ 42,021**	**$ 420,210**
Unrecognised actuarial differences	204	(192)	**557**	**5,570**
Fair value of pension assets	(17,104)	(18,388)	**(24,603)**	**(246,030)**
Liability for severance and retirement benefits	¥ 11,826	¥ 12,843	**¥ 17,975**	**$ 179,750**

Included in the consolidated statements of income for the years ended 31st March 2006, 2007 and 2008 were severance and retirement benefit expenses that comprised the following:

	Millions of yen			Thousands of U.S. dollars
	2006	2007	**2008**	**2008**
Service costs - benefits earned during the year	¥ 1,058	¥ 1,008	**¥ 2,321**	**$ 23,210**
Interest cost on projected benefit obligation	577	612	**828**	**8,280**
Expected return on plan assets	(279)	(316)	**(468)**	**(4,680)**
Amortisation of actuarial differences	8	(69)	**59**	**590**
Severance and retirement benefit expenses	1,364	1,235	**2,740**	**27,400**
Other	1,515	367	**322**	**3,220**
Total	¥ 2,879	¥ 1,602	**¥ 3,062**	**$ 30,620**

Retirement benefit expenses of consolidated subsidiaries which have adopted the simplified method are included in service costs.

The discount rate and the rate of expected return on plan assets used by the Companies were mainly both 2.0% for the years ended 31st March 2006, 2007 and 2008. The estimated amount of all retirement benefits to be paid at future retirement dates is allocated equally to each service year using the estimated number of total service years. Past service costs are mainly recognised as expenses when incurred, and actuarial gains and losses are recognised in equal amounts mainly over 13 years.

10. Finance Leases

Information, as lessee, for non-capitalised finance leases at 31st March 2006, 2007 and 2008 was as follows:

	Millions of yen			Thousands of U.S. dollars
	2006	2007	**2008**	**2008**
Original lease obligations (including finance charges) for machinery and equipment	¥ 3,837	¥ 2,920	**¥ 1,749**	**$ 17,490**
Payments remaining:				
Payments due within one year	¥ 427	¥ 341	**¥ 281**	**$ 2,810**
Payments due after one year	710	465	**389**	**3,890**
Total	¥ 1,137	¥ 806	**¥ 670**	**$ 6,700**

Rental expenses under such non-capitalised finance leases for the years ended 31st March 2006, 2007 and 2008 were ¥393 million, ¥441 million and ¥456 million ($4,560 thousand), respectively.

11. Contingent Liabilities

Contingent liabilities as of 31st March 2006, 2007 and 2008 were as follows:

	Millions of yen			Thousands of U.S. dollars
	2006	2007	**2008**	**2008**
Dept assumption agreements	¥ 15,800	¥ 6,800	**¥ 6,800**	**$ 68,000**

12. Derivative Transactions

The Company enters into interest rate swap contracts to manage risk and reduce exposure to interest rate fluctuations and currency swap contracts to manage risk related to marketable securities denominated in foreign currencies. The Company does not use derivatives for leveraging or speculative purposes.

Derivative transactions involve credit risk and market risk. However, the Company is exposed to minimum credit risk from breach of contract because it deals only with highly rated financial institutions. In addition, the Company enters into interest rate and currency swaps to hedge against risks of market fluctuations in relation to interest rates and its assets and liabilities. Accordingly, although profits or losses are produced temporarily, no profit or loss will be incurred at the expiration of the contracts.

To maintain adequate risk management, the Board of Directors and other persons in management approve derivative transactions and review them as to purpose, content, counter-party and risk.

The Company evaluates hedge effectiveness semi-annually by comparing the cumulative changes in cash flows or the changes in fair value of the hedged items and the corresponding changes in the hedging derivative instruments, except in cases of obvious hedge effectiveness.

13. Business Segment Information

Business segment information for the years ended 31st March 2006, 2007 and 2008, required to be disclosed by the Financial Instruments and Exchange Law of Japan, was as follows:

	Millions of yen					
As of and for the year ended 31st March 2006	Department stores	Supermarkets	Property management	Other	Eliminations	Total
Net sales						
External customers	¥ 301,048	¥ 50,960	¥ 9,225	¥ 20,052	¥ -	¥ 381,285
Intersegment	1,623	5,390	761	14,789	(22,563)	-
Total net sales	302,671	56,350	9,986	34,841	(22,563)	381,285
Operating costs and expenses	291,013	55,063	8,456	34,709	(22,548)	366,693
Operating income	¥ 11,658	¥ 1,287	¥ 1,530	¥ 132	¥ (15)	¥ 14,592
Assets	¥ 227,620	¥ 22,026	¥ 21,955	¥ 41,984	¥ (37,410)	¥ 276,175
Depreciation and amortisation	4,626	1,062	622	416	-	6,726
Capital expenditure	9,226	1,413	314	435	-	11,388

	Millions of yen					
As of and for the year ended 31st March 2007	Department stores	Supermarkets	Property management	Other	Eliminations	Total
Net sales						
External customers	¥ 291,567	¥ 78,257	¥ 9,284	¥ 16,842	¥ -	¥ 395,950
Intersegment	1,584	4,570	792	14,677	(21,623)	-
Total net sales	293,151	82,827	10,076	31,519	(21,623)	395,950
Operating costs and expenses	281,351	81,827	8,462	31,181	(21,635)	381,186
Operating income	¥ 11,800	¥ 1,000	¥ 1,614	¥ 338	¥ 12	¥ 14,764
Assets	¥ 248,290	¥ 51,819	¥ 22,075	¥ 36,966	¥ (76,391)	¥ 282,759
Depreciation and amortisation	4,569	1,543	580	346	-	7,038
Capital expenditure	3,740	2,774	453	292	-	7,259

Prior year information for 2006 has been reclassified to conform to the 2007 presentation.

Changes in Business Segmentation

The Companies used to classify their businesses into four segments: department stores, foods, property management and other businesses. However, we changed this segmentation in accordance with the increasing importance of the supermarket business. In fiscal year 2007, Hankyu Nissho Store, a supermarket business company, joined the Companies. The Companies also established Hanshoku Co., Ltd. as the intermediate holding company of the supermarket and food manufacturing business subsidiaries to ensure prompt and effective decision-making and implementation of business strategy in the supermarket business. Hanshoku Co., Ltd. controls 3 functional groups of supermarket business subsidiaries.

These 3 groups consist of Hankyu Oasis, Inc., Hankyu Family Store Co., Ltd. and Hankyu Nissho Store as the retailing business group, Hankyu Bakery Co., Ltd., Hankyu Foods, Inc., Hankyu Delica, Inc. and Mameda, Inc. as the food manufacturing business group, and Hankyu Fresh Yell Co., Ltd. as the purchasing function group. These 3 functional groups operate as one group, increasing their scale to make the supermarket business more profitable. This is the reason why we reclassified these subsidiaries related to the supermarket business as 'Supermarket business.' Subsidiaries which used to be in 'Foods business' and are not related to the supermarket business have been reclassified into other businesses since these subsidiaries have no significant impact on sales and operating income.

As of and for the year ended 31st Martch 2008	Millions of yen					
	Department stores	Supermarkets	Property management	Other	Eliminations	Total
Net sales						
External customers	¥ 351,435	¥ 89,785	¥ 9,686	¥ 20,711	¥ -	¥471,617
Intersegment	988	3,770	773	17,257	(22,788)	-
Total net sales	352,423	93,555	10,459	37,968	(22,788)	471,617
Operating costs and expenses	338,836	92,130	8,712	36,937	(22,112)	454,503
Operating income	¥ 13,587	¥ 1,425	¥ 1,747	¥ 1,031	¥ (676)	¥ 17,114
Assets	¥ 154,970	¥ 42,136	¥ 24,031	¥268,606	¥(151,965)	¥337,778
Depreciation and amortisation	4,743	1,765	501	721	-	7,730
Impairment loss	-	867	-	-	-	867
Capital expenditure	9,431	1,928	525	1,241	-	13,125

As of and for the year ended 31st March 2008	Thousands of U.S. dollars					
	Department stores	Supermarkets	Property management	Other	Eliminations	Total
Net sales						
External customers	$ 3,514,350	$ 897,850	$ 96,860	$ 207,110	$ -	$4,716,170
Intersegment	9,880	37,700	7,730	172,570	(227,880)	-
Total net sales	3,524,230	935,550	104,590	379,680	(227,880)	4,716,170
Operating costs and expenses	3,388,360	921,300	87,120	369,370	(221,120)	4,545,030
Operating income	$ 135,870	$ 14,250	$ 17,470	$ 10,310	$ (6,760)	$ 171,140
Assets	$1,549,700	$ 421,360	$ 240,310	$2,686,060	$(1,519,650)	$3,377,780
Depreciation and amortisation	47,430	17,650	5,010	7,210	-	77,300
Impairment loss	-	8,670	-	-	-	8,670
Capital expenditure	94,310	19,280	5,250	12,410	-	131,250

Segment	Commodity and business lines
Department stores	Clothing, accessories, foods, Restaurants and coffee shops, general merchandise, services and others
Supermarkets	Supermarkets, food production, purchasing and other food related business
Property management	Rental management of commercial facilities and hotels
Other	Wholesaling, membership management, home delivery, transportation, interior facilities, restaurants, temporary staffing, information processing

Geographic segment information for the years ended 31st March 2006, 2007 and 2008 was not disclosed since the proportion of amounts attributable to domestic operations to the total amounts were more than 90% for both the total sales and assets.

Overseas sales segment information was not disclosed since overseas sales of the Companies were less than 10% of consolidated net sales.

14. Income Taxes

Income taxes consist of corporation, inhabitants and enterprise taxes.

Significant components of the Companies' deferred tax assets and liabilities as of 31st March 2006, 2007 and 2008 were as follows:

	Millions of yen			Thousands of U.S. dollars
	2006	2007	**2008**	**2008**
Deferred tax assets:				
Loss carryforwards	¥ 540	¥ 498	**¥ 818**	**$ 8,180**
Provison for redemption of gift certificates	-	-	**684**	**6,840**
Bonuses to employees	1,580	1,521	**1,923**	**19,230**
Retirement benefits	4,707	5,104	**7,224**	**72,240**
Investments in consolidated subsidiaries	-	3,038	**1,924**	**19,240**
Loss on disposal of fixed assets	598	549	**512**	**5,120**
Depreciation	1,218	145	**153**	**1,530**
Impairment of investment securities and others	-	142	**-**	**-**
Loss on revaluation of land	1,561	-	**-**	**-**
Impairment losses of fixed assets	1,861	1,517	**1,150**	**11,500**
Provision for loss of stores rebuilding	-	2,156	**2,115**	**21,150**
Provision for loss of Umeda Main Store rebuilding	1,763	-	**-**	**-**
Unpaid transitional contribution on definite contribution pension plan	609	301	**2**	**20**
Retirement benefit trust assets	1,134	769	**415**	**4,150**
Other	2,032	1,727	**3,649**	**36,490**
	17,603	17,467	**20,569**	**205,690**
Valuation allowance	(132)	(390)	**(166)**	**(1,660)**
Total deferred tax assets	17,471	17,077	**20,403**	**204,030**
Deferred tax liabilities:				
Deferred gains on real properties	(3,252)	(3,020)	**(2,941)**	**(29,410)**
Special appropriation to the deferred gains on real properties	-	-	**(664)**	**(6,640)**
Land revaluation of a consolidated subsidiary	(793)	(1,409)	**(1,957)**	**(19,570)**
Valuation gain on investment securities resulting from conversion of retirement benefit trust assets (equity securities)	(4,591)	(4,591)	**(4,591)**	**(45,910)**
Unrealised holding gains on securities	(16,551)	(15,347)	**(11,288)**	**(112,880)**
Deferred hedge gains	-	(52)	**-**	**-**
Other	-	-	**(204)**	**(2,040)**
Total deferred tax liabilities	(25,187)	(24,419)	**(21,645)**	**(216,450)**
Net deferred tax assets (liabilities)	¥ (7,716)	¥ (7,342)	**¥ (1,242)**	**$(12,420)**

Net deferred tax assets (liabilities) as of 31st March 2006, 2007 and 2008 were included in the consolidated balance sheets as follows:

	Millions of yen			Thousands of U.S. dollars
	2006	2007	**2008**	**2008**
Current assets	¥ 3,447	¥ 3,228	**¥ 4,113**	**$ 41,130**
Long-term assets	4,185	3,535	**14,084**	**140,840**
Long-term liabilities	(15,348)	(14,105)	**(19,439)**	**(194,390)**
Net deferred tax assets (liabilities)	¥ (7,716)	¥ (7,342)	**¥ (1,242)**	**$ 12,420**

Reconciliation of the differences between the statutory tax rate and the effective income tax rate was as follows:

	Millions of yen
	2006
Aggregate statutory income tax rate	42.0%
Increase (reduction) in taxes resulting from:	
Nondeductible expenses	1.6
Tax on inhabitants per capita	0.5
Net operating losses in subsidiaries	1.3
Permanent differences (including dividends)	(1.8)
Amortisation of consolidated goodwill	(0.6)
Valuation allowance	(1.1)
Others	(2.2)
Effective income tax rate	39.7%

Reconciliation of the differences between the statutory tax rate and the effective income tax rate for 2007 and 2008 is not disclosed since the difference between the statutory tax rate and the effective income tax rate was less than 5% of the aggregate statutory income tax rate.

15. Net Assets

The Japanese Corporate Law (the“ Law”) became effective on 1st May 2006, replacing the Japanese Commercial Code (the“ Code”). The Law is generally applicable to events and transactions occurring after 30th April 2006 and for fiscal years ending after that date.

Under Japanese laws and regulations, the entire amount paid for new shares is required to be designated as common stock. However, a company may, by a resolution of the Board of Directors, designate an amount not exceeding one-half of the price of the new shares as additional paid-in capital, which is included in capital surplus.

Under the Law, in cases where a dividend distribution of surplus is made, the smaller of an amount equal to 10% of the dividend or the excess, if any, of 25% of common stock over the total of additional paid-in capital and legal earnings reserve must be set aside as additional paid-in capital or legal earnings reserve. Legal earnings reserve is included in retained earnings in the accompanying consolidated balance sheets.

Under the Code, companies were required to set aside an amount equal to at least 10% of the aggregate amount of cash dividends and other cash appropriations as legal earnings reserve until the total of legal earnings reserve and additional paid-in capital equaled 25% of common stock.

Under the Code, legal earnings reserve and additional paid-in capital could be used to eliminate or reduce a deficit by a resolution of the shareholders' meeting or could be capitalised by a resolution of the Board of Directors. Under the Law, both of these appropriations generally require a resolution of the shareholders' meeting.

Additional paid-in capital and legal earnings reserve may not be distributed as dividends. Under the Code, however, on condition that the total amount of legal earnings reserve and additional paid-in capital remained equal to or exceeded 25% of common stock, they were available for distribution by resolution of the shareholders’ meeting. Under the Law, all additional paid-in capital and all legal earnings reserve may be transferred to other capital surplus and retained earnings, respectively, which are potentially available for dividends.

The maximum amount that the Company can distribute as dividends is calculated based on the nonconsolidated financial statements of the Company in accordance with the Law.

At the Board of Directors' meeting held on 13th May 2008, the Company resolved cash dividends amounting to ¥1,290 million ($12,900 thousand). These appropriations have not been accrued in the consolidated financial statements as of 31st March 2008. The appropriations were recognised on 3rd June 2008.

The dividend policy is one of the most important policies of the Company. The Company used to focus on maintaining the dividend amount, Now the Company considers the dividend amount based on the progress of GP10 plan ver.2.

During the period of rebuilding of Umeda Main Store, however, the Company is focused on maintaining a dividend of ¥12.5 per share even if sales decrease temporally.

Stock Information

Changes in number of shares issued and outstanding during the years ended 31st March 2006, 2007 and 2008 were as follows:

Common stock outstanding

	number of shares		
	2006	2007	**2008**
Balance at beginning of year	187,688,301	187,688,301	**187,688,301**
Increase due to stock exchange	-	-	**19,052,476**
Balance at end of year	187,688,301	187,688,301	**206,740,777**

Treasury stock outstanding

	number of shares		
	2006	2007	**2008**
Balance at beginning of year	286,314	321,437	**345,561**
Increase due to additions to treasury stock in preparation for stock exchage	-	-	**16,257,000**
Increase due to purchase of odd-lot shares	78,065	87,598	**90,507**
Increase due to treasury stock held by Hanshin Department Stores, Ltd.	-	-	**20,050**
Decrease due to stock exchange	-	-	**16,364,000**
Decrease due to sales of odd-lot shares	12,942	7,474	**39,816**
Decrease due to exercise of stock options	30,000	56,000	**126,000**
Balance at end of year	321,437	345,561	**183,302**

16. Land Revaluation

In accordance with the Law Concerning Revaluation of Land, land used for business owned by two consolidated subsidiaries was revaluated. The unrealised gains and losses, net of deferred taxes, were excluded from the statement of income and reported as "Land revaluation" in net assets, and the relevant deferred taxes were shown as "Long-term deferred tax liabilities related to land revaluation" in liabilities and "Long-term deferred tax assets related to land revaluation" in assets at 31st March 2006, 2007 and 2008.

Related information was as follows:

Date of revaluations	28th February 2002 and 31st March 2002
Book value of land after revaluation	¥2,386 million
Market value of land at 31st March 2008	¥1,764 million
Difference	¥622 million

17. Stock Purchase Rights

The details of zero coupon convertible bonds due 2011 were as follows:

Date of issue	16th August 2004
The number of stock purchase rights	4,000
Class and number of stock	20,366,598 shares of common stock
The exercise period of stock purchase rights	From 23rd August 2004 to 9th August 2011
The exercise price of stock purchase rights (convertible price)	¥982 per share
The stock issuing price and capitalising amount	¥982 per share ¥491 per share

The exercise price of stock purchase rights (convertible price) would be adjusted if the Company issued new shares at a price below the market price or in other circumstances.

18. Loan Commitments

For efficient procurement of working capital, the Company entered into loan commitment contracts with two financial institutions in 2007 (three in 2006), providing the Company with loan commitment facilities in the aggregate amount of ¥5,000 million as of 31st March 2007 and ¥10,000 million as of 31st March 2006.

19. Gain on Sales of Property, Plant and Equipment

The gain on sales of property, plant and equipment in the year ended 31st March 2006 was mainly due to the sale of an unused Hankyu Department Stores dormitory building and land in Takarazuka for ¥88 million and the sale of the former Ikeda Distribution Centre building and land for ¥99 million.

The gain on sales of property, plant and equipment in the year ended 31st March 2008 was mainly due to the sale of land, buildings and structures of Hankyu Oasis Shioe store for ¥170 million ($1,700 thousand), land, buildings and structures of Kawanishi Mosaic Box for ¥1,674 million ($16,740 thousand) and land of Hankyu Nissho Store, the former Ikeda store, for ¥547 million ($5,470 thousand).

20. Loss of Stores Rebuilding

Loss of stores rebuilding in the year ended 31st March 2007 consisted of a loss of ¥1,994 million for the provision for loss of stores rebuilding.

Loss of stores rebuilding in the year ended 31st March 2008 consisted of a loss of ¥67million ($670 thousand) for the provision for loss of stores rebuilding.

21. Loss of Umeda Main Store Rebuilding

Loss of Umeda Main Store rebuilding in the year ended 31st March 2006 consisted of a loss of ¥2,479 million for the provision for loss of Umeda Main Store rebuilding and a loss of ¥457 million on disposal of fixed assets etc.

22. Impairment Losses

The Company recorded impairment losses in the year ended 31st March 2006 as follows:

Location	Asset group	Use	Type of assets	Millions of yen
Chuo-ku, Kobe	Kobe Hankyu	Store	Buildings and structures	¥ 2,211
Kita-ku, Kobe	Rokko-Kita Sports Centre	Former recreation facility	Land	453

The Companies classify assets into groups under the accounting rules for impairment losses on fixed assets in the following way:

(1) Stores and other accounting units of a similar nature for which revenue and expenditure are continuously ascertained as a group; and
(2) An idle asset or an asset to be sold as a separate item

An impairment loss on Kobe Hankyu was recognised because a large adjacent supermarket closed at the end of November 2005. The closing caused a deterioration in the operating environment of the Kobe Harborland area, where the store is located, and this was expected to have a negative influence on the store's operating profit or loss.

Since the Rokko-kita Sports Centre, which was used as a recreational facility and grouped into common property, was closed in January 2006, it was reclassified as a separate asset and an impairment loss was recognised.

As a result, the book values of the two properties were reduced to net selling price or recoverable value, and the reduced amount, ¥2,664 million, was recorded as an impairment loss under special losses.

An appraisal value provided by a trust and banking company was used as the net selling price for Kobe Hankyu and an estimated selling price was used as the net selling price for the Rokko-kita Sports Centre.

The Companies recorded impairment losses in the year ended 31st March 2008 as follows:

Company	Asset Group	Use	Type of Assets	Millions of yen
Hankyu Oasis, Inc.	Kitasenri store	Store	Buildings and structures, machinery and equipment and other	¥ 50
Hankyu Nissho Store	Neyagawa store and other	Store	Buildings and structures, machinery and equipment and other	¥267
Hankyu Family Store Co., Ltd.	Shimpoin store and other	Store	Buildings and structures, machinery and equipment and other	¥264
Hankyu Foods, Inc.	Nishinomiya centre	Logistics centre	Buildings and structures, machinery and equipment	¥286

Hankyu Oasis Inc., Hankyu Nissho Store, and Hankyu Family Store Co., Ltd. recognised impairment losses on some of their stores because their operating environments became severe with the growing competition.

The recoverable amounts of the assets are based on the present values of expected cash flows from the on-going utilisation and subsequent disposal of the assets using a discount rate of 5%.

Hankyu Foods, Inc. classify the Nishinomiya Centre, which was used as a logistics centre, into a separate item and recognised impairment loss for it because it became an idle asset with the restructuring of their facilities. The recoverable amounut of the asset is its net realisable value based on the assessed asset value. As a result, ¥867 million ($8,670 thousand) was recorded as impairment losses in total.

23. Loss on Disposal of Property, Plant, Equipment and Intangibles

Loss on disposal of property, plant, equipment and intangibles in the year ended 31st March 2007 consisted of losses of ¥632 million ($5,356 thousand) on the disposal of buildings and structures, losses of ¥8 million ($68 thousand) on the disposal of machinery and vehicles and losses of ¥103 million ($873 thousand) on the disposal of other assets.

Loss on disposal of property, plant, equipment and intangibles in the year ended 31st March 2008 consisted of losses of ¥652 million ($6,520 thousand) on the disposal of buildings and structures, losses of ¥10 million ($100 thousand) on the disposal of machinery and vehicles, losses of ¥53 million ($530 thousand) on the disposal of intangibles and losses of ¥97 million ($970 thousand) on the disposal of other assets.

24. Consolidated Statements of Cash Flows

Assets and liabilities of the newly consolidated subsidiaries by acquisition of shares at the inception of their consolidation, 31 July 2006 and 1 October 2007, were as follows:

	Millions of yen			Thousands of U.S. dollars
	2006	2007	**2008**	**2008**
Current assets	¥ -	¥ 5,049	**¥ 22,634**	**$226,340**
Fixed assets	-	16,461	**22,625**	**226,250**
Total assets	¥ -	¥ 21,510	**¥ 45,259**	**$452,590**
Current liabilities	-	6,400	**16,862**	**168,620**
Long-term liabilities	-	6,503	**5,406**	**54,060**
Total liabilities	¥ -	¥ 12,903	**¥ 22,268**	**$226,680**

Assets and liabilities of the ex-consolidated subsidiary by sale of shares at the end of its consolidation, 30 September 2005, were as follows:

	Millions of yen		
	2006	2007	**2008**
Current assets	¥ 1,603	¥ -	¥ **-**
Fixed assets	787	-	**-**
Total assets	¥ 2,390	¥ -	¥ **-**
Current liabilities	1,565	-	**-**
Long-term liabilities	145	-	**-**
Total liabilities	¥ 1,710	¥ -	¥ **-**

25. Net Income Per Share

Reconciliation of the difference between basic and diluted net income per share ("EPS") for the years ended 31st March 2006, 2007 and 2008.

	Millions of yen			Thousands of U.S. dollars
	2006	2007	**2008**	**2008**
Basic net income per share calculation:				
Income (numerator):				
Net income	¥ 7,922	¥ 8,100	¥ **9,450**	**$ 94,500**
Amounts not belonging to common stock	-	-	**-**	**-**
Net income available to common stockholders	7,922	8,100	**9,450**	**94,500**
Shares, thousands (denominator):				
Weighted average number of shares	187,380	187,358	**188,738**	
Basic EPS (yen and U.S. dollars)	¥ 42.28	¥ 43.23	¥ **50.07**	**$ 0.50**
Diluted net income per share calculation:				
Income (numerator):				
Net income	¥ 7,922	¥ 8,100	¥ **9,450**	**$ 94,500**
Amounts not belonging to common stock	-	-	**-**	**-**
Net income available to common stockholders	7,922	8,100	**9,450**	**94,500**
Effect of dilutive securities-convertible bonds	-	-	**-**	**-**
Adjusted net income	7,922	8,100	**9,450**	**94,500**
Shares, thousands (denominator):				
Weighted average number of shares	187,380	187,358	**188,738**	
Assumed conversion of convertible bonds	20,366	20,366	**20,366**	
Assumed exercise of stock purchase rights	10	23	**-**	
Adjusted weighed average number of shares	207,756	207,747	**209,104**	
Diluted EPS (yen and U.S. dollars)	¥ 38.13	¥ 38.99	¥ **45.19**	**$ 0.45**

26. Business Combinations

(Change in accounting standard for business combinations, etc.)

Effective from the year ended 31st March 2007, the Company applied the "Accounting standard for business combinations" issued by the Business Accounting Council on 31st October 2003, Accounting Standard Board Statement No. 7, the "Accounting Standard for Business Divestitures" issued by the Accounting Standard Board of Japan on 27th December 2005 and the Accounting Standard Board Guidance No. 10, "Guidance for Accounting Standard for Business Combinations and the Accounting Standard for Business Divestitures" issued by the Accounting Standards Board of Japan on 22nd December 2006. The adoption of the New Accounting Standards had no impact on the consolidated statements of income for the year ended 31st March 2007.

In the year ended 31st March 2007

Purchase Method Application (Purchase of Nissho Corporation)

1. Corporate name and description of business of acquired company, main reason for business combination, date of business combination, legal form of business combination, corporate name after business combination and percentage of voting rights acquired

(1) Corporate name and business of the entity combined
Nissho Corporation - Supermarkets business
(2) Purpose of business combination
The Companies operate in the supermarkets business with originalities as department store group. By combining with Nissho Corporation, which has stores in Hokusetsu (the northern area of Osaka and south-eastern area of Hyogo), the Companies can enhance intra-group synergy through the combination of the strong points of each supermarkets subsidiaries and the complementary effects of the operating areas. The Companies can also enlarge the scale of the supermarkets business and implement the dominant strategy in the Kansai area.
(3) Date of business combination
31st July 2006
(4) Legal form of business combination
Purchase of shares of Nissho Corporation
(5) Corporate name after business combination
Hankyu Department Stores, Inc.
(6) Percentage of total shares outstanding
100%

2. The period of operations of the purchased company included in the consolidated statements of income
From 1st August 2006 to 31st March 2007

3. Acquisition cost
¥18,750 million

4. Amount of goodwill, reason for the generation of goodwill and the method and period of amortisation of goodwill
(1) Amount of goodwill
¥10,143 million
(2) Reason for the generation of goodwill
The goodwill arose from the expected future profitability generated by the increased scale of the supermarkets business.
(3) The method and period of amortisation of goodwill
Equal amortisation over 20 years

5. Assets and liabilities of the combined company as of the date of the combination

	Millions of yen
Current assets	¥ 5,049
Fixed assets	16,461
Total assets	¥ 21,510
Current liabilities	6,400
Long-term liabilities	6,503
Total liabilities	¥ 12,903

6. The estimated influence on the consolidated statement of income for the year ended 31st March 2007 if the business combination had been completed on 1st April 2006

Net sales	¥408,156 million
Operating income	¥14,647 million
Income before income taxes	¥14,203 million
Net income	¥7,969 million
Net income per share	¥42.53

The influence shown above is estimated by adding the sales and income of Nissho Corporation from 1st April 2006 to 31st July 2006 and the amortisation of goodwill for the same period.

In the year ended 31st March 2008

Purchase Method Application

(Management Combination with The Hanshin Department Store, Ltd. through share transfer)
The Company integrated its operations with The Hanshin Department Store, Ltd., a wholly owned subsidiary of the Company, through a share transfer effective 1st October 2007.

1. Corporate name and description of business of acquired company, primary reason for business combination, date of business combination, legal form of business combination, corporate name after business combination, percentage of voting rights acquired.
 (1) Corporate name and description of operations of acquired company
   The Hanshin Department Store, Ltd. - Department store operation
 (2) Primary reason for business combination of operations
   In addition to major changes in the operating environment such as the declining birthrate, the aging of the population, competition between different business formats, and a decline in the number of market participants triggered by industry reorganisation, the downtown of Osaka (“Kita”) is expected to become an area of unprecedented business concentration by 2011, creating an exceptionally competitive business environment. Accordingly, the companies, which are ranked as the number one and number two stores in the area, decided to merge in order to build a unified business foundation that can take full advantage of both brand and jointly utilise the business resources of both companies to construct a “super main store” that will give them a competitive advantage and, thereby, improve customer satisfaction and boost shareholder value.
 (3) Date of business combination
   1st October 2007
 (4) Legal form of business combination
   Share transfer whereby Hankyu Department Stores, Inc. becomes the 100% parent company and The Hanshin Department Store, Ltd. becomes the wholly-owned subsidiary (Note: The Hankyu Department Stores, Inc. changed its trade name to H2O RETAILING CORPORATION as of 1st October 2007.)
 (5) Corporate name after business combination
   H2O RETAILING CORPORATION
 (6) Percentage of voting rights acquired
   99.9%
   As a result of the above-mentioned acquisition, The Hanshin Department Store, Ltd. became a wholly-owned subsidiary of the Company.

2. Period of the business performance of the acquired company contained in the consolidated financial statements
   1st October 2007 to 31st March 2008

3. Acquisition cost
   ¥38,144 million ($381,440 thousand)

4. Share transfer ratio
   One common share of the Company was exchanged for one common share of The Hanshin Department Store, Ltd. However, this exchange was not applied to twenty thousand (20,000) shares of common stock in The Hanshin Department Store, Ltd. that were owned by the Company

5. Calculation method of share transfer ratio
   Daiwa Securities SMBC Co. Ltd. calculated the share transfer ratio on behalf of the Company, while Ernst & Young Transaction Advisory Services Co., Ltd. performed the calculation on behalf of The Hanshin Department Store, Ltd.
   Daiwa Securities SMBC performed a share value appraisal with respect to the Company based on the discounted cash flow method (DCF method) and another method used for a comparison of similar companies. It also performed a share value appraisal with respect to The Hanshin Department Store, Ltd. based on the same methods.

Ernst & Young made similar calculations with respect to the Company based on the market stock price method, DCF method, the other method used for the comparison of similar companies, and the net asset method. After comprehensively considering these results, the market stock price method and the DCF method were adopted to calculate the stock value per share. For valuation of The Hanshin Department Store, Ltd., Ernst & Young adopted the DCF method and calculated the stock value per share after comprehensively considering the calculation results based on the DCF method, the method used for the comparison of similar companies and the net asset method.

Based on the results of these calculations, and after considering the respective financial situations, business performance trends, and so on of both companies, and after extensive discussions between the two companies, it was finally agreed that the above-mentioned share transfer ratio was appropriate.

6. Number of shares delivered and appraised value
Number of shares delivered: 35,416,476 shares of common stock
Appraised value: ¥38,144 million ($381,440 thousand)
With respect to 16,364,000 shares of the adove-mentioned stock, shares in treasury stock were allocated for delivery.

7. Amount of goodwill, reason, method of amortization, and period for amortisation
(1) Amount of goodwill: ¥10,066 million ($100,660 thousand)
(2) Reason
Goodwill arose in connection with the anticipated future profitability resulting from improvements in the competitive predominance of the department store business as well as cost reductions achieved through integration of the business infrastructure.
(3) Method of amortisation and period for amortisation
Equal amounts over a twenty-year period

8. Amount of assets received and liabilities assumed on the date of business combination and breakdown thereof
(1) Amount of assets
Current assets: ¥22,634 million ($226,340 thousand)
Noncurrent assets: ¥22,624 million ($226,240 thousand)
(2) Amount of liabilities
Current liabilities: ¥16,862 million ($168,620 thousand)
Long-term liabilities: ¥5,405 million ($54,050 thousand)

9. Estimated effect on consolidated income statements for the reporting term assuming that the business combination is completed on the date of the commencement of the reporting period
Sales and profit and loss information
Net sales: ¥527,206 million ($5,272,060 thousand)
Operating income: ¥17,967 million ($179,670 thousand)
Income before income taxes: ¥18,110 million ($181,100 thousand)
Net income: ¥10,017 million ($100,170 thousand)
Net Income per Share: ¥48.85

(Calculation Method of Estimated Amounts and Important Prerequisites)
The sales and profits and losses of The Hanshin Department Store, Ltd. and five subsidiaries for the 2007 fiscal year were totaled and calculated after assuming the estimated amounts of eliminations for consolidation adjustment and goodwill amortization expenses.

Procedures and Other Relationships Under Common Control

(Changeover to holding company system through corporate split of department store business)
The department store business of the Company was taken over by the new company that was established by the corporate split on 1st October 2007. The Company itself was transformed into a holding company.

1. Name and description of target business, legal form of business combination, name of business after combination and summary of transactions, including purpose of transaction
   In order to change to a holding company system, the Company carried out a corporate split to establish a new company, which took the department store business (including the departments of the headquarters, such as personnel, general affairs, management, development, etc. related to the department store business, and internal companies) of the Company. The new company was named Hankyu Department Stores, Inc. Simultaneously, the Company changed its trade name to H_2O RETAILING CORPORATION.

2. Summary of accounting procedures performed
   As of 30th September 2007, the assets and liabilities of The Hankyu Department Stores, Inc. were divided into department store-related assets and liabilities and holding company-related assets and liabilities. Thereafter, the assets and liabilities related to the department store business were transferred to the newly established company through a corporate split in consideration for which the Company acquired shares of the new company.

(1) Amounts of transferred assets and liabilities and breakdown thereof
 1. Amount of assets
    Current assets: ¥41,099 million ($410,990 thousand)
    Noncurrent assets: ¥44,359 million ($443,590 thousand)
 2. Amount of liabilities
    Current liabilities: ¥34,609 million ($346,090 thousand)
    Long-term liabilities: ¥16,438 million ($164,380 thousand)

(2) Number of shares and calculation basis of the shares of the new company
 1. Number of shares: 100,000 shares
 2. Calculation basis
    We determined the number of shares to be issued by the new company to realise efficient management, taking into consideration the amount of its paid-in capital.
    In addition, notwithstanding the number of shares issued or allocated, the net assets of H_2O RETAILING CORPORATION remain unchanged.

(3) Paid-in capital and description of business of the new company
    Paid-in capital: ¥5 million ($50 thousand)
    Line of business: Department store operations

    The corporate split has no effect on the consolidated financial statements as the procedure comes under the category of common control.

(Establishment of intermediate holding company (development of Oi Development Co., Ltd.) through corporate split of property management business)
In order to achieve speedy and efficient expansion of the property management business, at the Board of Directors' meeting held on 1st October 2007, the Company resolved to establish Oi Development Co., Ltd. as an intermediate holding company to take over the property management business planning operations of the H_2O RETAILING Group through a corporate split, and established an intermediate holding company on 22nd October 2007.

1. Name and description of target business, legal form of business combination, name of business after business combination, and summary of procedures, including their purpose
   Oi Development Co., Ltd., as a holding company which controls the property management (PM) business of the H_2O RETAILING Group to optimize the Group's entire PM business, conducts strategic planning, primarily relating to the redevelopment of the JR Oimachi Station area (in Tokyo), and promotes the further acceleration of the growth strategy. For this purpose, the operations of the PM Business Planning Department of the Company (drafts the strategic planning for the PM Business segment) were taken over by Oi Development Co., Ltd., the newly established intermediate holding company.

2. Summary of accounting procedures performed
Among the assets and liabilities of H2O RETAILING CORPORATION as 22nd October 2007, the assets and liabilities related to the redevelopment of the JR Oimachi Station area were transferred to the newly established company, in consideration for which the shares of the newly established company were acquired by H2O RETAILING CORPORATION.

Amounts of transferred assets and liabilities and breakdown thereof
(1) Amount of assets
Current assets: ¥34 million ($340 thousand)
Noncurrent assets: ¥9,969 million ($99,690 thousand)
(2) Amount of liabilities
Long-term liabilities: ¥145 million ($1,450 thousand)

The corporate split has had no effect on the consolidated financial statements as the procedure comes under the category of common control.

In addition, Oi Development Co., Ltd. (the intermediate holding company of the PM Business) and Ours Inn Hankyu (its trade name was changed as of 22nd October 2007 from Oi Development Co., Ltd.), which operates a hotel near JR Oimachi Station, passed a resolution at the Board or Directors' meeting of both companies held on 25th October 2007 to approve the business transfer agreement, stating that the business related to the redevelopment of the JR Oimachi Station area would be transferred from Ours Inn Hankyu to Oi Development Co. Ltd. The transfer agreement was implemented on 1st December 2007.

27. Subsequent Events

(Inter-group merger of subsidiaries engaged in department store business)
The Hanshin Department Store, Ltd. and Hankyu Department Stores, Inc., both of which are wholly-owned subsidiaries of the Company, concluded a merger agreement on 12th May 2008.

1. Name and description of business of companies subject to business combination, legal form of business combination, name of company after combination and summary of procedures, including their purpose
(1) Corporate name of the business entities prior to combination and description of their business lines
Hankyu Department Stores, Inc. - department store business
The Hanshin Department Store, Ltd. - department store business
(2) Legal form of business combination
Absorption of Hanshin Department Stores by Hankyu Department Stores, Inc. as the surviving entity
(3) Name of entity after business combination
Hankyu Hanshin Department Stores, Inc.
(4) Summary of procedures, including purpose of business combination
In Phase I of the business integration, which has a target completion date of autumn 2008, Hankyu Department Stores, Inc. and The Hanshin Department Store, Ltd. has been proceeding with the integration of their business infrastructure, including system integration, joint use of facilities, and the joint purchase of fixtures. Phase II has been focusing on the reorganisation of the head office staff departments and standardization of business flows. In order to accelerate the integration process and maximize the benefits, both companies determined to merge because they believed this would be more effective for business integration.

2. Summary of accounting procedures to be performed
Pursuant to the “Accounting Standards for Business Combinations” and the “Application Guidance for Accounting Standards for Business Combinations and Accounting Standards for Business Divestitures,” accounting procedures will be conducted as a form of procedure under the category of common control.

The merger has had no effect on the consolidated financial statements as the procedure comes under the category of common control.

(Inter-group merger of subsidiaries engaged in supermarket business)
The five wholly-owned subsidiaries of the Company, Hanshoku Co., Ltd., Hankyu Oasis, Inc., Hankyu Nissho Store, Hankyu Family Store, Co., Ltd and Hankyu Fresh Yell Co., Ltd., concluded a merger agreement on 7th May 2008.

1. Names and descriptions of business of companies subject to business combination, legal form of business combination, name of company after combination and summary of transactions, including purpose of transactions

(1) Corporate names and businesses of the business combination entities
Hanshoku Co., Ltd. -Supervision of food business companies and management of business activities
Hankyu Oasis, Inc. -Management of food supermarkets
Hankyu Nissho Store -Management of food supermarkets
Hankyu Family Store, Co., Ltd. -Management of food supermarkets
Hankyu Fresh Yell Co., Ltd. -Procurement and wholesaling of food products

(2) Legal form of business combination
Absorption of four companies by Hanshoku Co., Ltd. as the surviving company

(3) Corporate name of company after business combination
Hanshoku Co., Ltd.

(4) Summary of procedures, including purpose of business combination
In our supermarket business, the scale of operations has expanded by aggressively opening new food supermarkets and making Hankyu Nissho Store a subsidiary in July 2006. In September 2006, Hanshoku Co., Ltd. was established as an intermediate holding company to upgrade the management infrastructure and enable the rapid large-scale expansion of business by centralising administrative and procurement functions, integrating computer systems, and recognising the manufacturing and sales operations. Recently, the benefits of this infrastructure upgrading have begun to work efficiently, and in order to achieve further improvements in the efficiency of overall supermarket business operations, it was decided to merge Hanshoku Co., Ltd., Hankyu Oasis, Inc., Hankyu Nissho Store and Hankyu Family Store, Co., Ltd., which operate food supermarkets and Hankyu Fresh Yell Co., Ltd., which procures products.

2. Summary of accounting procedures to be performed
Pursuant to the “Accounting Standards for Business Combinations,” the “Application Guidance for Accounting Standards and Accounting Standards for Business Combinations and the Accounting Standards for Business Divestitures,” accounting procedures will be conducted as a form of common control procedure.

The merger has had no effect on the consolidated financial statements as the procedure comes under the category of common control.

(Abolition of retirement allowance for directors and corporate auditors, and introduction of stock options for directors and executive officers)
At the Board of Directors' meeting held on 13th May 2008, the Company resolved to abolish the retirement allowance system for directors and corporate auditors and to introduce a stock options programme for directors (excluding external directors) and executive officers of the Company and for directors and executive officers of The Hankyu Department Stores, Inc., which is a subsidiary of the Company. In addition, at the 89th Annual General Meeting of Shareholders held on 24th June 2008, as a result of the above-mentioned abolishment, a resolution was passed to make a final payment of the retirement allowance at the time of retirement of each director and corporate auditor currently in office corresponding to number of years of their services, pursuant to the current internal regulations for retirement allowances to directors and corporate auditors.

In the same manner, at the Board of Directors' meeting held on 12th May 2008, The Hankyu Department Stores, Inc. resolved to abolish the retirement allowance system for directors and corporate auditors, and at the 1st Annual General Meeting of Shareholders held on 20th June 2008, resolved to make a final payment of the retirement allowances for retiring officers.

The details of the Company's stock options system are as follows;

Date of resolution at the Board of Directors' meeting	13th May 2008
The class and number of grantees	H2O RETAILING CORPORATION: Directors (except for an outside director) and executive officers Hankyu Department Stores, Inc.: Directors and executive officers ✻1
The class of stock	Common stock
The number of shares	✻1,2,3
The exercise price of stock purchase rights	¥1 per share
The exercise period of stock purchase rights	The Board of Directors of the Company decide the exercise period on condition that it is within 30 years from the day following the day when the stock options are granted.
The exercise conditions of stock purchase rights	✻1
Transfer of stock purchase rights	The approval by the resolution of the Boad of Directors' meeting of the Company is required, to be granted stock purchase rights by transfer.

✻1 The concrete number of grantees, the number of shares and the exercise conditions of stock purchase rights are to be determined at the Board of Directors' meeting to be held. As for the Directors (except for an outside director) of the Company, the maximum number of shares is 80,000 shares by the resolution at the 89th annual general shareholders' meeting of the Company held on 24th June 2008. As for the Directors of Hankyu Department Stores, Inc., the maximum number of shares is 80,000 shares by the resolution at the 1st annual general shareholders' meeting of Hankyu Department Stores, Inc. held on 20 June 2008.

✻2 The number of shares per stock purchase right is 1,000.

✻3 The number of shares above would be adjusted if the Company split common stock (including the issue of common stock for free) or unite common stock.

Independent Auditors' Report

To the Shareholders and Board of Directors of
H2O RETAILING CORPORATION:

We have audited the accompanying consolidated balance sheets of H2O RETAILING CORPORATION (formerly Hankyu Department Stores, Inc.) and consolidated subsidiaries as of 31st March 2006, 2007 and 2008, and the related consolidated statements of income, changes in net assets and cash flows for each of the three years in the period ended 31st March 2008, expressed in Japanese yen. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to independently express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of H2O RETAILING CORPORATION and subsidiaries as of 31st March 2006, 2007 and 2008, and the consolidated results of their operations and their cash flows for each of the three years in the period ended 31st March 2008, in conformity with accounting principles generally accepted in Japan.

Without qualifying our opinion, we draw attention to the following.

(1) As discussed in Note 13 to the consolidated financial statements, effective 1st April 2006, the Company and subsidiaries changed its segmentation.
(2) As discussed in Note 2 to the consolidated financial statements, effective 1st April 2007, the Company and subsidiaries changed the accounting policy of provision for redemption of gift certificates.
(3) As discussed in Note 27 to the consolidated financial statements, a merger agreement of subsidiaries in department store business and its in supermarket business were engaged respectively.

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended 31st March 2008 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 1 to the consolidated financial statements.

Osaka, Japan
24th June 2008

KPMG AZSA & Co.

Corporate Data

Board of Directors and Corporate Auditors

Chairman, Representative Director and CEO
Shunichi Sugioka
President and Representative Director
Jun Wakabayashi
Representative Director
Nobuaki Nitta
Directors
Yosaku Fuji, Kazuo Sumi, Hideo Nishikawa,
Kazutoshi Senno, Kohei Yanagisawa
Director, Senior Managing Executive Officer
Yoshio Honda
Director, Executive Officer
Tadatsugu Mori
Executive Officers
Junichi Ono, Masanori Hara, Takashi Nakamoto
Standing Corporate Auditor
Toshimitsu Konishi
Corporate Auditors
Hideyuki Takai, Takeshi Nakagawa, Toshihisa Takamura
(as of 24th June 2008)

Outline of the Company

Date of Establishment :	March 1947
Stated Capital :	¥17,797 million
Authorised Shares :	300,000,000
Issued and Outstanding Shares :	206,740,777
Shareholders :	16,904
Employees :	58

Principal Shareholders :

Hankyu Department Stores Kyoeikai
Hanshin Electric Railway Co., Ltd.
Hankyu Hanshin Holdings, Inc.
Japan Trustee Services Bank, Ltd. (Trust account)
The Master Trust Bank of Japan, Ltd. (Trust account)
The Bank of Tokyo-Mitsubishi UFJ, Ltd.
Japan Trustee Services Bank, Ltd. (Trust account 4)
Trust & Custody Services Bank, Ltd.(Investment trust account)
Sumitomo Mitsui Banking Corporation
Deutsche Bank AG London-PB Non-Treaty Clients 613

Principal Consolidated Subsidiaries

Company Name	Stated capital (Millions of yen)	Annual sales (Millions of yen)	Direct holding by the company (%)	Principal business
Hankyu Department Stores, Inc.	¥ 5,000	¥ 156,867	100.0	Operation of department stores
Hanshin Department Store, Ltd.	4,359	58,121	100.0	Operation of department stores
Hanshoku Co., Ltd.	100	698	100.0	Supervision of supermarket business
Hankyu Oasis, Inc.	100	40,745	100.0	Operation of supermarkets
Hankyu Nissho Store	100	34,363	100.0	Operation of supermarkets
Hankyu Family Store Co., Ltd.	100	12,340	100.0	Operation of supermarkets
Hankyu Kitchen Yell Co., Ltd.	50	5,598	100.0	Food delivery service
Hankyu Foods, Inc.	50	3,086	100.0	Manufacture and sales of food products
Hankyu Bakery Co., Ltd.	50	1,688	100.0	Manufacture and sales of food products
Oi Development	100	132	100.0	Supervision of property maneagement business
Hankyu Shopping Center Development Co., Ltd.	50	6,499	100,0	Developer
Ours Inn Hankyu	100	2,396	100.0	Hotel
Hankyu Seisakusho Co., Ltd.	20	5,471	100.0	Manufacture and sales of furniture and furnishings
Hankyu Design Systems Co., Ltd.	10	2,736	100.0	Sales of sales promotion materials and printings
Hankyu Department Stores Europe B.V.	EUR.220 thousand	EUR.438 thousand	100.0	Fund-raising and fund management related to overseas business
Hankyu Home Styling Co., Ltd.	10	716	100.0	Sales of furniture
Esaka Logistics Services Co., Ltd.	20	4,883	100.0	Transportation
Persona Co., Ltd.	20	672	100.0	Credit card business
Hankyu Maintenance Services Co., Ltd.	10	2,701	81.0	Operation of office maintenance service
With System, Inc.	100	2,444	100.0	Data processing and systems development
Hankyu Job Yell Co., Ltd.	40	2,106	100.0	Temporary employment agency
Hankyu Tomonokai Co., Ltd.	50	347	100.0	Membership organization for customer service

Memo

Memo

Memo

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