LAWSON

Evolving

Annual Report 2007

Year ended February 28, 2007

Consolidated Financial Highlights

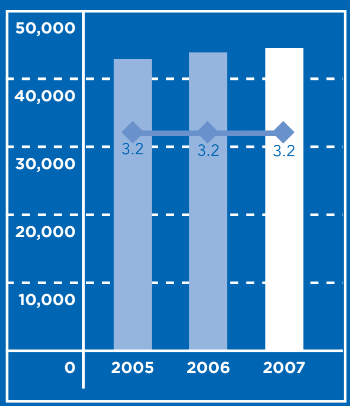
LAWSON, INC. and Subsidiaries
Years Ended February 28, 2007, 2006 and 2005

	Millions of Yen			Percent Change	Thousands of U.S. Dollars*
	2007	2006	2005	2007/2006	**2007**
For the Year:					
Net sales of all stores	**¥1,386,630**	¥1,361,731	¥1,329,077	1.8%	**$11,707,447**
Total operating revenues	**283,053**	268,058	254,395	5.6%	**2,389,843**
Operating income	**44,513**	43,867	42,941	1.5%	**375,827**
Income before income taxes and minority interests	**36,848**	38,723	36,040	–4.8%	**311,111**
Net income	**20,983**	22,025	20,435	–4.7%	**177,161**
Per Share Data (yen and dollars)**:**					
Net income	**¥ 202**	¥ 216	¥ 198	–6.5%	**$ 1.70**
Cash dividends	**100**	90	70	11.1%	**0.84**
At Year-end:					
Total assets	**¥ 398,258**	¥ 375,107	¥ 356,310	6.2%	**$ 3,362,530**
Total equity	**199,493**	175,184	160,282	13.9%	**1,684,339**
Financial Data:					
Return on equity (ROE)	**11.3%**	13.1%	13.0%	–1.8	
Payout ratio	**49.6%**	41.8%	35.3%	7.8	
Store Network:					
Total number of stores in Japan	**8,564**	8,366	8,077	2.4%	
Franchised stores	**8,093**	7,958	7,731	1.7%	
Company-owned stores	**471**	408	346	15.4%	

**The U.S. dollar amounts represent translations of Japanese yen at the approximate exchange rate at February 28, 2007, of ¥118.44=$1.*

Operating income and Operating income ratio

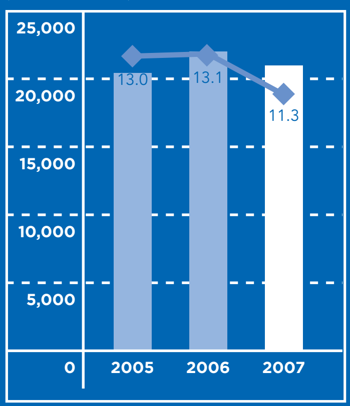
(Millions of Yen)



Operating income
Operating income ratio (%)
*Operating income ratio=Operating income/Net sales of all stores

Net income and ROE

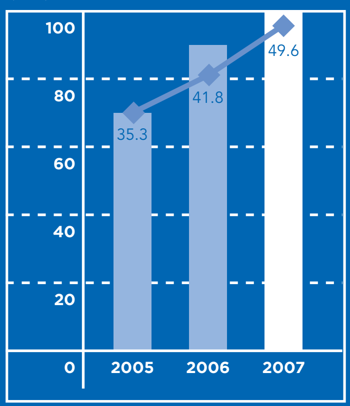
(Millions of Yen)



Net income
ROE (%)

Cash dividends per share and Payout ratio

(Yen)



Cash dividends per share
Payout ratio (%)

Forward-looking Statements

This annual report contains forward-looking statements about the future plans, strategies, beliefs and performance of LAWSON and its subsidiaries. These forward-looking statements are not historical facts. They are expectations, estimates, forecasts and projections based on information currently available to the company and are subject to a number of risks, uncertainties and assumptions, which, without limitation, include economic trends, competition in the Japanese convenience store industry, personal consumption, market demand, the tax system and other legislation. As such, actual results may differ materially from those projected.

Contents

A Message to LAWSON Stakeholders

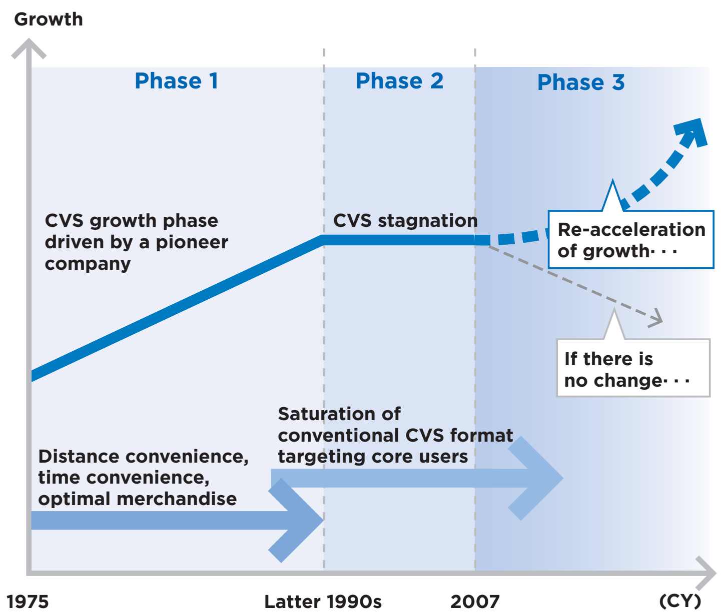
Evolving to Meet Changing

As President and CEO, I have continuously asked myself since my appointment what is necessary for LAWSON, INC. to achieve sustainable growth over the medium to long term. Broadly speaking, two elements are required—valuing and developing human resources, and constantly being conscious of coexistence with society.

The chain store industry in Japan has a history of growth by opening a large number of stores, driven by the strong leadership and charisma of founders based on a standardized model. At the same time, there has been a tendency to think of personnel expenses only as costs and thus to neglect employee development, leading to a dearth of successors. Also, business expansion hasn't always taken as much notice of the cost of capital as perhaps it should have. I think that these issues and the market saturation caused by mass openings of conventional convenience stores (CVS) of the same type probably led to the slump in existing store sales at CVS chains and slower corporate growth in recent years.

In this annual report, we intend to clarify the issues and strategies that LAWSON must tackle and execute by reflecting on the nearly 30-year history of the Japanese CVS industry, from its growth phase to the present day. In other words, we will look at the past and present as the basis for where the industry must head in the future.

CVS Chronicle —Overview—



Looking Back Over the 30 Years of Japan's CVS Industry

Phase 1

The period of approximately 20 years from 1975 to the second half of the 1990s was the dawning of the CVS industry and, at that same time, a phase of strong growth. At that time, consumers had few options available to them, with retail stores rarely close to their neighborhoods. Naturally, they welcomed the convenience offered by stores that operated 24 hours a day and the convenience in terms of being within walking distance of their homes. Men in their 20s to 30s, in particular, embraced the convenience store concept because 24-hour trading matched an era when young people were more active at night. These men became the core customers of today's CVS.

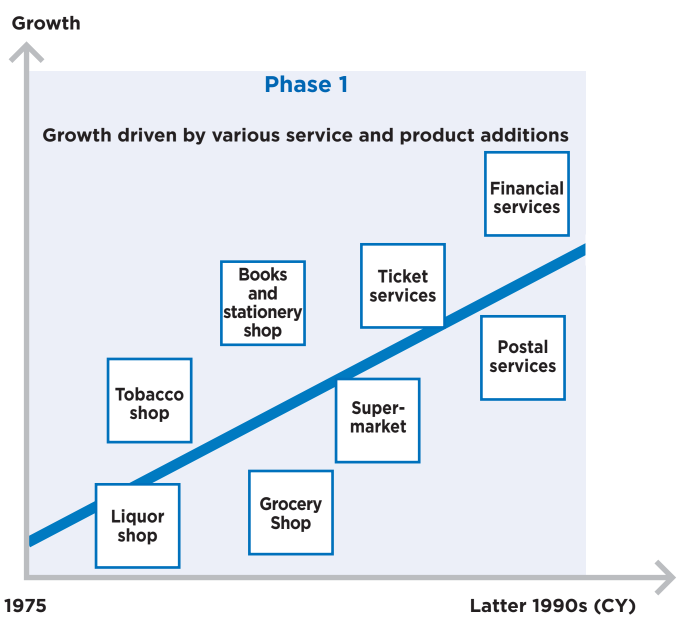
The number of stores increased rapidly as customer convenience was enhanced. Convenience stores differentiated their merchandise assortments from other formats by functioning also as manufacturers. For example, they created integrated manufacturing and sales systems that enabled them to develop and sell private brand boxed lunches, rice balls and other products. Furthermore, besides functioning as general stores and mini-supermarkets, convenience stores aggressively introduced ticket sales and other services, including financial services such as bill settlement and ATMs.

The existence of a standardized model used nationwide was a major factor behind the ability to rapidly open chain stores. At the same time, the franchise system, whereby store management was outsourced, also drove the rapid pace of convenience store openings.

In addition to this business framework, a large number of highly motivated franchised store owners also supported the growth of the CVS industry. These shopkeepers established the foundations for stores closely linked to the needs of local communities by operating stores 24 hours a day in all areas of the country.

Needs

CVS Industry Life Cycle in the Past Growth Stage

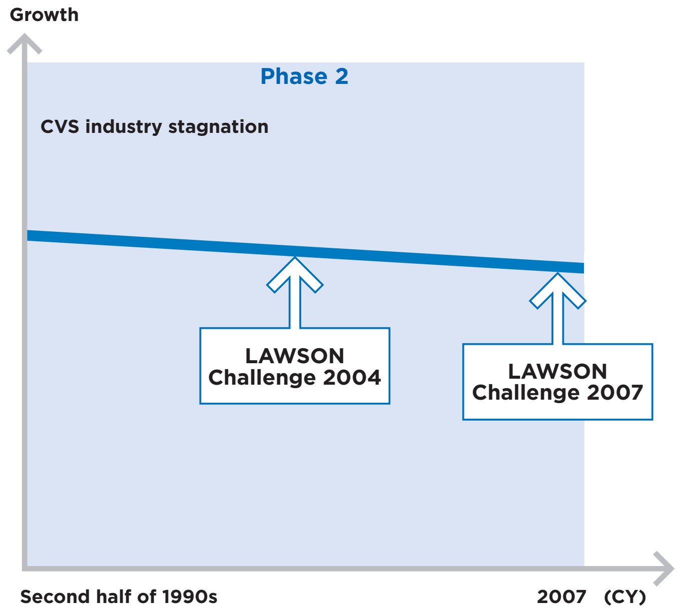


Phase 2

Phase 2, the 10 years from the second half of the 1990s to the present, was a period of slow growth.

The CVS industry, which had grown dramatically for the past two decades, witnessed competition to open stores in a drive to expand sales, as CVS operators became preoccupied with trying to reap economies of scale. This resulted in an excess of same-type stores with little differentiation whose core target was men in their 20s and 30s. With the middle-aged, elderly and women viewing the atmosphere and merchandise assortments of such stores as unattractive, convenience stores found their customer bases became lopsided. In addition, as CVS operators over-concentrated on the scale of their operations, they focused little effort on innovation in terms of adding value to their businesses through product development and the introduction of new services. Yet this was a decade when they really had to work hard to enhance and promote the attractiveness of the convenience store format itself.

CVS Industry Life Cycle in the Phase of Industry Stagnation



The competition fanned by mass store openings led to slower growth in existing store sales, and consequently increased the risk of poorer earnings at existing franchised stores. The continuous cycle of opening and closing large numbers of stores also resulted in poorer capital efficiency among the major CVS operators.

Trends in No. of Domestic Stores and Store Openings and Closures at Top Four CVS Chains*

Fiscal years ended February 28 and 29 (stores)

LAWSON	2003	2004	2005	2006	2007
No. of stores	7,625	7,821	8,077	8,366	**8,564**
Store openings	502	625	711	717	**700**
Store closures	611	429	455	428	**502**

Seven-Eleven Japan	2003	2004	2005	2006	2007
No. of stores	9,690	10,303	10,826	11,310	**11,735**
Store openings	930	904	904	891	**832**
Store closures	300	291	381	407	**407**

FamilyMart	2003	2004	2005	2006	2007
No. of stores	5,593	5,770	5,994	6,284	**6,501**
Store openings	501	456	532	606	**586**
Store closures	359	279	308	316	**369**

Circle K	2003	2004	2005	2006	2007
No. of stores	2,710	2,651	2,855	2,891	**2,898**
Store openings	230	200	193	196	**187**
Store closures	103	259	143	160	**180**

Sunkus	2003	2004	2005	2006	2007
No. of stores	2,257	2,200	2,273	2,263	**2,205**
Store openings	188	160	153	139	**119**
Store closures	69	217	80	149	**177**

**Source: Data released by each company*

Given the declining birthrate and aging society in Japan, it has become increasingly important for the CVS industry to expand its customer base by providing products and services aimed at the middle-aged, elderly and women, who have not traditionally been core customers. We realize that it is not possible to acquire new customer bases with homogenized, nationally uniform merchandise assortments resulting from standardization, as they will not fulfill customer needs any more. Moreover, it appears that the middle-aged, elderly and women have a greater need to shop within walking distance rather than by car compared to young men. Given this, we would expect convenience stores to be able to display the strength inherent in their handy locations to attract such customers.

Amid the changing industry environment, we have responded to these structural changes among consumers. We have striven to increase the number of customers through the expansion of our customer base by creating store formats and conducting merchandising matched to individual locations. Guiding these efforts have been two medium-term management plans: LAWSON Challenge 2004 (fiscal 2002 to 2004) and LAWSON Challenge 2007 (fiscal 2005 to 2007). We have executed strategy in line with these plans.

Under LAWSON Challenge 2004, we dealt with negative legacies by closing unprofitable stores that were the result of the dramatic expansion in the scale of operations in the past and taking other actions. In parallel, we took steps to strengthen human resources by opening training centers, for example. In addition, we have focused our efforts on the basics, such as the **Three Challenge Practices** for store management guidance, as we worked to build a platform for the creation of stores suited to the individual needs of customers in each location.

The Three Challenge Practices are points that franchised store owners, employees, and store crew (part-time workers) must pay particular attention to in running LAWSON stores. They are (1) ensuring merchandise assortments are matched to individual store locations, (2) serving customers courteously, and (3) keeping stores and surrounding areas clean.

Under LAWSON Challenge 2007, which began in fiscal 2005, we have promoted improved merchandise assortments through the use of **"store charts"** and the **"Mystery Shopper"** program. To increase the number of customers through the expansion of our customer base and respond to diverse customer needs, we are developing three formats—regular LAWSON stores, NATURAL LAWSON, and LAWSON STORE100. Furthermore, we have positioned growth in gross profit at existing stores, net increase in the number of stores, the improvement of earnings at affiliated companies, M&As, and the buyback and cancellation of treasury stock as earnings drivers. We also established the consolidated management targets of an average of 10% EPS growth over the 3 years of the plan and ROE of 15% in fiscal 2007, the final year of the plan, and endeavored to achieve these targets.

An important tool for franchised store owners to make decisions, "store charts" include analysis of marketing and management on an individual store basis. Through the use of these "store charts," each store is able to promote merchandise assortments and ordering that is matched to the individual characteristics of each store location.

The "Mystery Shopper" program is a system where an undercover researcher who is a company employee with a thorough knowledge of convenience store operations and merchandise assortments, objectively and quantitatively evaluates LAWSON stores from a customer's perspective. The results are fed back to LAWSON's Head Office and franchise owners. In fiscal 2004, LAWSON established subsidiary BestPractice Inc. and commissioned it to carry out these surveys.

Nevertheless, the impact of structural factors, namely, competition among similar convenience stores of the major CVS operators and intensifying competition across sectors such as with supermarkets and other sectors, has been far greater than we envisaged. Moreover, growth in existing store gross profit, which we had expected to drive earnings, has fallen short of our targets. Amid the continued aging of society, mainly in regional areas, the importance of merchandise assortments and services that attract middle-aged and elderly customers has increased. However, it has taken time to carry out research and development regarding stores that can cater to these needs (LAWSON PLUS, described later). Furthermore, upfront investment to cope with the dramatic changes in the operating environment, such as the "Mystery Shopper" program, **training centers**, new formats (NATURAL LAWSON and LAWSON STORE100), and sales promotion activities aimed at expanding customer bases, were higher than anticipated.

Training centers train crews and franchised store owners. This training is wide-ranging and includes training for leader crew candidates and franchise owners according to their years of experience. They are linked to the introduction of the Mystery Shopper program and were established at all regional headquarters in fiscal 2004.

As a result of the above factors, when announcing our business results for the fiscal year ended February 28, 2007, we revised the earnings targets for the final fiscal year of LAWSON Challenge 2007 and lowered the management targets for the plan, as shown on page 07.

LAWSON Challenge 2007 (FY2005 to FY2007) Mid-term Report

Management targets: EPS growth of 10% on average over 3 years and ROE of 15%

Overview of FY2005 and FY2006: Deterioration in operating environment exceeded expectations
→Increased medium-term business development, personnel development and franchise owner support

1 <Sluggish growth in existing store markups>

- Large number of store openings by major CVS chains
- Stiffer competition across business models, e.g., from supermarkets

2 <Subsidiaries taking longer than expected to contribute to earnings>

- Impact of upfront investments needed to quickly launch subsidiaries operating new formats
- Impact of so-called "grey zone interest rates" on LAWSON CS Card due to strict application of the Interest Limitation Law stemming from a change in government consumer finance policy

3 <Investments with medium-term outlook>

- Nationwide development of perishable foods and daily delivered products system
- Increased investment in personnel development

4 <FC owner support>

- Strengthened sales promotions
- Owner support system

Revised targets

FY2007 forecasts: 2.3% average EPS growth over 3 years and ROE of 11.1%

Nevertheless, I firmly believe that our upfront investments during this period to drive an increase in the number of customers through the expansion of our customer base were vital for Phase 3 (discussed in the next section)—that is, sustainable growth over the medium to long term.

In the section entitled "LAWSON's Store Format Strategy" from page 10, we discuss in detail the development of new formats that LAWSON has promoted as part of its strategy under LAWSON Challenge 2007.

Phase 3

In Phase 2, we implemented management policies based on the two medium-term management plans: LAWSON Challenge 2004 and LAWSON Challenge 2007. However, looking back now, I firmly believe the following points.

First, the reason for the stagnant growth in the CVS industry in recent times is certainly not a reflection of a dwindling need for the convenience store model itself. Rather, it has resulted from too many stores of the same type. And, if anything, the degree of importance placed on convenience in terms of location is increasing the value of irreplaceable CVS networks in an aging society.

Second, the major CVS operators, including LAWSON, are still cash rich and have strong balance sheets. Therefore, as long as they endeavor to improve their capital efficiency, they will probably have sufficient management resources needed to return to a growth phase.

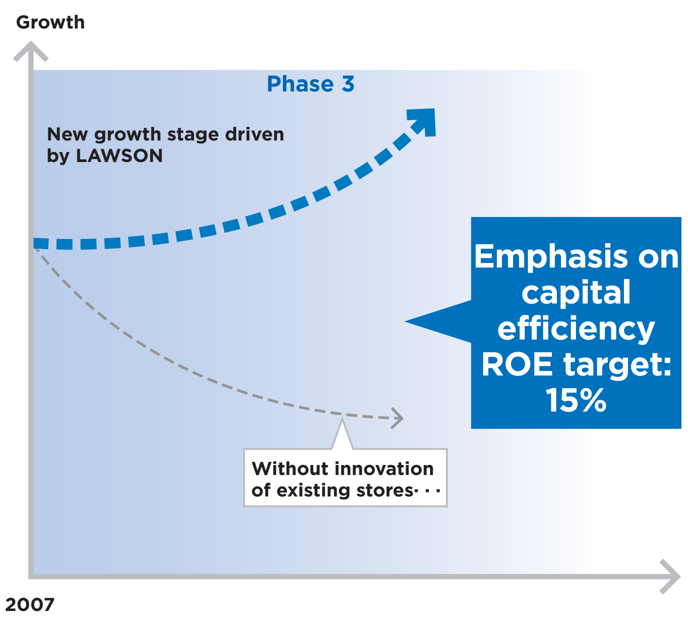
Third, whether CVS operators are able to return to a growth phase will certainly hinge on how well they use their management resources while emphasizing capital efficiency and whether they are able to promote innovation in their operations.

In other words, I believe that Phase 3 will be an era when the quality of the medium- to long-term growth strategies of each company will be increasingly called into question.

Accordingly, in Phase 3, LAWSON will further strengthen and promote the measures implemented in Phase 2.

In Phase 2, we made upfront investments to develop new formats and in other areas in a bid to expand our customer base. I believe that these measures, which stole a march on other major CVS operators, will surely differentiate LAWSON and put us back on a growth trajectory. As the industry number 2 CVS chain operator, it is unlikely that we would prevail if we adopted the same strategies and methods as that of the industry leader. Instead, our greatest theme will be innovation. By trying various new approaches in a way that makes the best utilization of the convenience of location, which is the

CVS Merchandise Cycle in the New Growth Stage



greatest strength of convenience stores, and collaborating with other sectors, we will increase corporate value and build an unshakeable position in the CVS industry.

Furthermore, based on an awareness of capital cost, we will continue to emphasize ROE and focus on capital efficiency in all aspects of strategic management execution. To that end, we aim to improve the earnings of existing franchised stores by implementing measures to revitalize existing stores that are centered on increasing the number of customers through the expansion of our customer base.

More specifically, we will pursue the following strategies.

First, we will strengthen the capabilities of individual stores to respond to customer needs and in the process expand our customer base of women, the middle-aged and elderly. We will achieve this by offering more fresh products, daily delivered foods, and locally targeted products, that is, merchandise utilizing ingredients that suit the preferences of local customers, and products in tune with local needs. These products will be developed based on an analysis of "store charts."

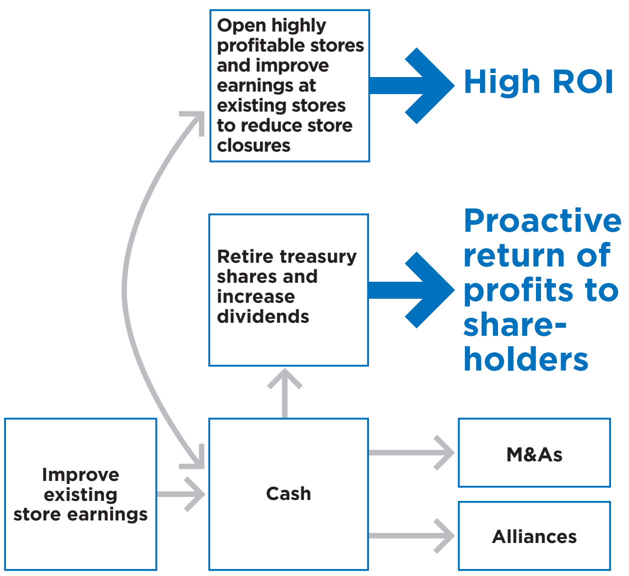
Second, in addition to utilizing "store charts," we aim to create merchandise assortments that are even more closely matched to local needs by leveraging our expertise, accumulated in our operations of the NATURAL LAWSON and LAWSON STORE100 formats, for our regular LAWSON stores.

Third, as a means of enhancing recognition among women, the middle-aged and elderly customers, we will convert regular LAWSON stores into the LAWSON PLUS format.

Fourth, we aim to increase our card users by increasing the membership base of LAWSON PASS, our point card with a credit function, and the point card MY LAWSON POINT as well as strengthening our sales promotion to make more effective use of these cards. These measures will realize customer relationship management* and ultimately help us to better match merchandise assortments to the individual characteristics of each location.

Finally, to reinforce the use of individual "store charts," we will actively develop human resources and recruit employees to strengthen our management support capabilities for franchise owners.

Improving Capital Efficiency



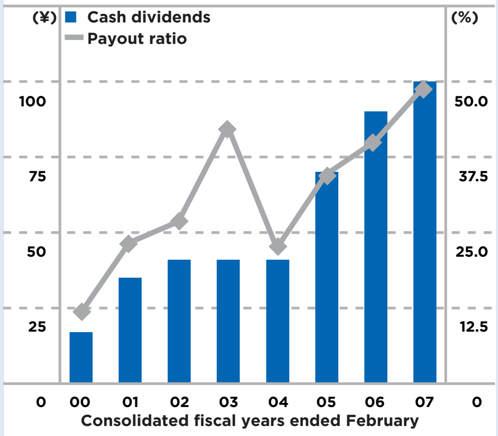
Thus, by promoting measures that emphasize the reinforcement of existing stores rather than new store openings, I intend to break the negative spiral of opening and closing stores in large numbers to improve capital efficiency so as to fulfill the expectations of shareholders. Our numerical goal in this context is to create a company that can deliver ROE of 15% in the future.

*Customer Relationship Management: Providing services tailored to individual needs by compiling and analyzing data concerning a customer's purchasing behavior, gender, age, and other characteristics.

Conclusion

I believe it is vital as a business executive to have a global management philosophy that emphasizes capital efficiency. It is equally important to practice a Japanese-style management philosophy that strives for coexistence with society and that focuses on employee satisfaction. The entrepreneur Eiichi Shibusawa, who is known as the "father of Japanese capitalism," summed this up effectively in his book "Confucius Analects and Abacus." As he said, I think that management which skillfully balances a Japanese-style corporate culture with global economic rationalism is the source of stable, long-term growth.

Annual Cash Dividends and Payout Ratio



As CEO of LAWSON, I will strive to create a balance between the achievement of short-term earnings targets and the realization of sustained medium- to long-term growth. In regards to investments in businesses, I will focus on ROE and by implementing management that is committed to generating return exceeding the cost of capital, I aim to achieve earnings over a three- to five-year time frame. On the other hand, I also intend to realize long-term growth through the promotion of our core businesses while constantly remaining aware of the need for coexistence with society.

In addition, we will use our cash reserves to make upfront investments with a medium- to long-term focus that will enable us to deliver high ROE in the future. At the same time, we will actively return profits to shareholders through the retirement of treasury shares and higher dividends, balancing this with the need to invest in our future.

With a core focus on increasing shareholder value, we will emphasize frank communication with the securities market and make efforts to deepen understanding regarding our management vision and strategies, as well as their current status and issues. I look forward to your continued support in these endeavors.

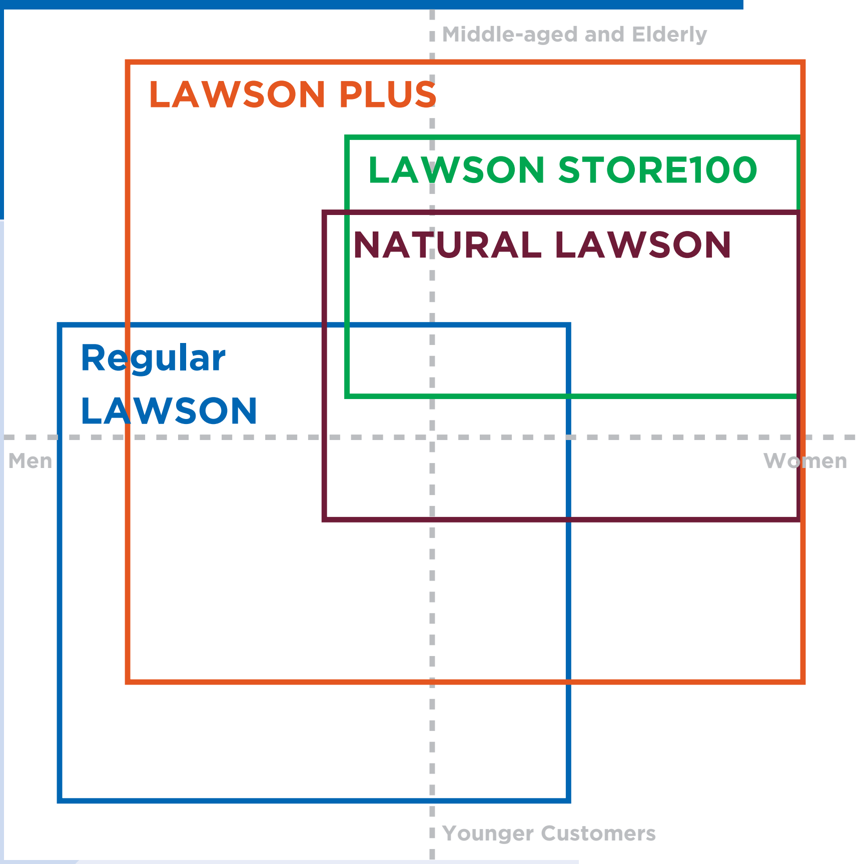
August 2007

Takeshi Niinami
President and Chief Executive Officer

LAWSON's Store Format Strategy

Format Strategy

LAWSON is striving to provide merchandise and services that customers require in individual locations by developing store formats that match merchandise and layout to customers' ages and needs and utilize existing infrastructure.



As of February 28, 2007, LAWSON had three store formats—regular LAWSON, NATURAL LAWSON, and LAWSON STORE100. In addition, as a remodeled format of regular LAWSON stores, we added LAWSON PLUS from the fiscal year ended February 28, 2007. In this section, we provide an overview of LAWSON's store formats.

The basis of LAWSON's strategy is to open the optimal format for the location—that is, to match the needs of local customers. We analyze customer needs based on factors such as age and gender composition, regional characteristics, and differences in living environments in each area and then open stores using the format best suited to the location.

LAWSON bases its decision on which format to use on individual "store charts" (analysis of individual store information). In other words, when we open a new store, we decide which format is suitable, and if existing-store earnings decline, we change the format (e.g., from a regular LAWSON store to the NATURAL LAWSON format). Alternatively, we may remodel it into the LAWSON PLUS format, or try to improve the results of an existing store without changing the format by enhancing quality (Q), service (S), and cleanliness (C) and reinforcing merchandise assortments suited to local customers. When we previously only had a single store format, the regular LAWSON, we either had to close or relocate stores when store earnings were weak. However, our multiple format strategy enables us to continue providing products and services to customers in pre-existing locations.

Specifically, while promoting the creation and maintenance of individual "store charts," franchise owners and LAWSON supervisors (management guidance staff) work together to analyze the customer base and regional characteristics of store locations. In addition, by using the information obtained from "store charts," they decide whether merchandise assortments will be able to fulfill local customer needs.

In terms of the profitability of each format, we believe that the format that best matches the needs of local customers as well as the surrounding commercial area of each unique store will be the most profitable one for the franchise owner and LAWSON.

LAWSON's new format strategy thus involves opening formats that suit the individual characteristics of each location, providing maximum convenience to customers in that particular location.

Regular LAWSON Stores

Regular LAWSON Stores

What Is the Regular LAWSON Format?

Since our establishment in 1975, the regular LAWSON format has been positioned as our mainstay store format. As a rule, the store concept color, including the signboard and the logo, has a blue tone. Operating hours are 24 hours a day, in principle, apart from locations where there are time restrictions such as some office buildings.

The main customer target is men in their 20s and 30s. By responding to needs generated by changes in lifestyle patterns of mainly young men (increasingly working and going out late at night), this format has grown for about 30 years since its conception.

The strength of this format lies in the existence of a dense store network in the vicinity of areas where people live, work or are otherwise active. The convenience in terms of time and distance in a small commercial area have become the strength of the convenience store format. Furthermore, this format is differentiated from other retail formats by the convenience of merchandise assortments carefully selected from a wide range of product categories and types so as to meet the varying needs of customers, ranging from daily necessities to emergency-use items, even in a limited retail space.

Through TV commercials and other media, LAWSON has created a familiar brand image in the form of "the 'hot' station in the neighborhood." Furthermore, LAWSON's network is broad; LAWSON became the first national chain in the CVS industry to have stores in all 47 prefectures in Japan in 1997. Other strengths include innovative measures, evident in the *Onigiriya* series of rice balls brand and the *Gohantei* boxed lunch brand.

Happy Child-Raising Project
Miffy-themed campaign gifts

Challenges Faced by the Regular LAWSON Format

The regular LAWSON format has driven LAWSON's growth for three decades. But existing store sales have continued to struggle due to such factors as competition with like stores in the CVS industry and changing lifestyles. LAWSON recognizes three challenges facing this format.

1] The market is saturated with conventional CVS due to major chains opening large numbers of stores.

2] This format has a strong image among young men, but less appealing to women, the middle-aged and elderly.

3] Roadside convenience stores in particular are suffering from competition from supermarkets, drug stores and other business models.

Future Measures for the Regular LAWSON Format

To overcome these issues, we are giving top priority to increasing the number of customers to improve the trend in existing store sales. We will do this by maintaining the support of our core customers, while working to attract other customers to our stores. Six specific measures will be implemented.

1] We will develop merchandise assortments matched to the individual characteristics of each location by strengthening franchise owners' store management capabilities and enhancing utilization of "store charts."

2] As regards head office management policy, we will delegate authority to LAWSON's seven regional headquarters (Hokkaido, Tohoku, Kanto, Chubu, Kinki, Chugoku and Shikoku, and Kyushu). Spearheaded by these headquarters, we will endeavor to provide a detailed response to regional needs in terms of merchandise, management and product development, and to improve the ability of store supervisors to offer management guidance to franchise owners.

3] We will introduce and reinforce products that match local preferences and needs, health-oriented products, and perishable and daily delivered foods for housewives, middle-aged and elderly customers.

4] We will strengthen alliances with corporations as we continue to open stores in special locations where high earnings are projected due to captive markets. These locations include hospitals, stations, and post offices.

5] To encourage the use of "store charts" and promote improvements in merchandise assortments matched to local areas, we will reinforce the development of store supervisors and other personnel.

6] We will promote the use of LAWSON PASS and MY LAWSON POINT. Aiming to have six million members by February 29, 2008, we will continue to work to acquire new cardholders while creating loyal existing cardholders through sales promotions, including the provision of attractive points programs and privileges. Moreover, by promoting customer relationship management (CRM) based on card data, we will strengthen merchandise assortments matched to regions and individual stores.

As of February 28, 2007

Launch of business format	April 1975
Core customer target	Men in their 20s and 30s
Female customer ratio (estimated)	Approx. 30%
Store-opening area	Nationwide
Number of items handled	Approx. 2,800
Private brand product ratio	Approx. 30%
Sales area per store	Approx. 35 *tsubo**

*A Japanese measurement equivalent to 3.306 square meters per *tsubo*

Total number of stores in Japan	8,384
Franchise ratio	96.4%

NATURAL LAWSON Stores

NATURAL LAWSON Stores

What Is the NATURAL LAWSON Format?

Aiming to acquire more women customers, we opened the first NATURAL LAWSON store in July 2001. These value-added-type outlets are based on the key words "beauty," "health," and "convenience." NATURAL LAWSON stores broke the conventional convenience store image. Our intention was to create stores that encourage more women to enjoy shopping at our stores. For example, the concept color of stores and the logo is burgundy red while store interiors and merchandise assortments are also intentionally different from regular LAWSON stores. There are three specific points of differentiation.

1] A stronger range of health-oriented products, including boxed lunches featuring ingredients such as black rice and brown rice.

2] The majority of stores provide a lineup of fresh bread baked on the premises.

3] The stores actively promote NATURAL LAWSON brands and alliances with other business formats that have a close affinity. Examples include naturalBeat (sales of healthy sandwiches), Vinos Yamazaki (specialty wine stores), Ef Agri Systems (sale of fruit and vegetables), and Motoya Express (mobile coffee shops).

Future Measures for the NATURAL LAWSON Format

We have adopted the stance that NATURAL LAWSON should be developed as an entirely new format. To achieve this, we have promoted innovations in product development and store concept, without being constrained by past successes. And these stores have been operated by a company that is a wholly owned LAWSON subsidiary. Five years after the format was launched and 100 stores later, we believe that the NATURAL LAWSON brand has become firmly established in terms of distinctive merchandise and the store concept. Going forward, we are determined to capture more synergies by making better use of the LAWSON Group's infrastructure.

We intend to strengthen the management capabilities of existing stores through collaboration with LAWSON regional headquarters. And by further strengthening cooperation with LAWSON's head office development division, we will open stores with a strong focus on store earnings. Moreover, we will step up the development of products that rigorously comply with the NATURAL LAWSON image—that is, they appeal to health-conscious customers and the preferences of women. Through these measures, we will raise the profitability of existing stores and promote the franchising of directly operated stores.

naturalBeat stores provide products such as bread, muffins, and soups that are healthy. They do not use additives such as synthetic seasonings, preservatives, and colorings or genetically modified ingredients. As of March 31, 2007, naturalBeat had 10 stores operating in the Tokyo metropolitan area. The company was established in 2004.

As of February 28, 2007

Launch of business format	July 2001
Core customer target	Working women in their 20s and 30s and health-conscious customers
Female customer ratio (estimated)	Approx. 45%
Store-opening area	Office and residential districts
Number of items handled	Approx. 2,500
Ratio of common products with regular LAWSON	Approx. 60%
Total number of stores	100
Franchise ratio	5%

LAWSON STORE100 Stores

LAWSON STORE100 Stores

What Is the LAWSON STORE100 Format?

We developed the LAWSON STORE100 format to build up expertise within the LAWSON Group in response to growing needs for fresh foods in small commercial areas stemming from changes in the structure of families in recent years, including the trend toward the nuclear family and the aging of society. The first LAWSON STORE100 was opened in May 2005. This format weds the CVS and mini-supermarket formats, based on the theme of "supporting savings of living expenses, simplicity, and convenience in everyday life," and features perishable foods. Whereas general merchandizing stores (GMS) and food supermarkets are used by large families to buy groceries in bulk on the weekend, LAWSON STORE100 stores are used by housewives busy with child-rearing and elderly people who tend to buy only what they need each day. Consequently, LAWSON STORE100's merchandising is distinguished by sales of perishable foods and daily delivered foods in small quantities and conveniently sized packages. The pricing strategy is based on simplicity, with a single price of ¥105 (including consumption tax) for most products—this is particularly reassuring for elderly people. We have also developed a private brand called *Value Line*. The number of items in this series has grown and some are now also being sold at regular LAWSON stores.

Future Measures for the LAWSON STORE100 Format

In the two years since the launch of this format in 2005, a total of 80 LAWSON STORE100 stores have been opened. By building purchasing channels for perishable foods and accumulating expertise regarding methods of handling such merchandise within the Group, we established a nationwide distribution channel for perishable foods in February 2007.

The same month, LAWSON formed an equity-based business alliance with Ninety-nine Plus Inc., a pioneer in fresh food convenience stores that operates the SHOP99 chain. As a result, both companies are sharing their expertise in the fresh food CVS business, and we will initiate measures with a view to integrate both businesses in the future as well. Actual customer data shows that SHOP99 has stronger support from housewives, the middle-aged and elderly than general CVS chains, and its strengths lie in expertise in the development and sale of perishable foods and daily delivered foods.

As of February 28, 2007

Launch of business format	May 2005
Core customer target	Housewives, the middle-aged and elderly
Female customer ratio (estimated)	Approx. 40%
Store-opening area	Residential districts and near stations
Number of items handled	Approx. 4,500
Number of *Value Line* SKUs	320
Ratio of common products with regular LAWSON	Approx. 10%
Total number of stores	80
Franchise ratio	0%

LAWSON PLUS Stores

LAWSON PLUS Stores

What Is the LAWSON PLUS Format?

The LAWSON PLUS format is based on the remodeling of existing LAWSON stores, mainly in terms of signage, interior décor, fixtures and fittings, and merchandise assortments. This format is designed to attract business from new customer bases, namely, the middle-aged, elderly and women, while maintaining the core customer base of men aged in their 20s and 30s.

There are certain conditions for remodeling existing stores. Based on an analysis of "store charts," we select stores with a high percentage of women, middle-aged and elderly customers in the surrounding commercial area. These stores must also have a "Mystery Shopper" rank of B+ or higher. LAWSON PLUS stores are increasing their handling of perishable and daily delivered foods, frozen foods, and delicatessen items, in addition to products handled by regular LAWSON stores.

The LAWSON PLUS format was established in fiscal 2006 based on the results of several trials, including that of senior-friendly LAWSON stores and introducing perishable foods at stores in urban areas. The number of LAWSON PLUS stores in a broad sense, including all of these, was 77 as of February 28, 2007.

The sunrise color symbolizes a new start, as if the sun were rising above the horizon (the LAWSON signboard in this case).

Strengths of the LAWSON PLUS Format

We aim to differentiate the LAWSON PLUS format from conventional CVS by making use of the expertise we have built up through NATURAL LAWSON in products such as freshly baked bread and healthy foods and also through LAWSON STORE100 in perishable and daily delivered foods.

The central strategies of LAWSON PLUS are to develop products that are appealing to new customers, including the middle-aged and elderly and women, based on an analysis of "store charts," and to conduct merchandising that enables an assortment of products suited to the preferences of customers in the area concerned.

To enhance the effectiveness of these strategies, we are changing the signboard, interior décor, fixtures and fittings, and other items from the conventional LAWSON format. In particular, the color of the signboard has been changed from the conventional "blue" to a color with a warm tone that is called "sunrise color*." This color symbolizes the new rise of our traditional blue regular LAWSON store through its evolution into a store that is more appreciated among not only the traditional customer groups, namely men in their 20s and 30s, but also the new customer groups mainly the middle-aged, elderly and women.

Challenges for Fiscal 2007

We are aiming for a 15% to 20% improvement in sales as a result of LAWSON PLUS conversions. In fiscal 2007, our target is to remodel 700 to 800 stores. At present, we believe that about 30% of all stores can improve sales by being converted to the LAWSON PLUS format. Fiscal 2007 will be the first year of full-fledged LAWSON PLUS remodeling, and we therefore position it as an important year that holds the key to the future success of the LAWSON PLUS store format.

Launch of business format	**Trial started in 2005, full-scale development from fiscal 2007 (first store with sunrise color sign opened in January 2007)**
Core customer target	**Centered on conventional mainstay customer base (men in their 20s and 30s) and extending to all customers in general in the area concerned, including housewives, the middle-aged and elderly**
Store-opening area	**Large cities as well as urban and residential districts in regional areas**

Corporate Governance

Basic Policy on Corporate Governance

In order to be recognized as a company that has meaning for each of our stakeholders, namely, customers, franchise owners, store crew (part-time workers), business partners, employees, shareholders and society, we engage in business activities to maximize our corporate value. For this, not to mention promoting directors' and employees' compliance with laws, regulations, the Articles of Incorporation and the like, we believe that it is essential to strengthen corporate governance by enhancing the soundness and transparency of our management processes, through acting with consideration for others, based on our "Corporate Philosophy" and "the Lawson Code of Ethics", as well as the active disclosure of information.

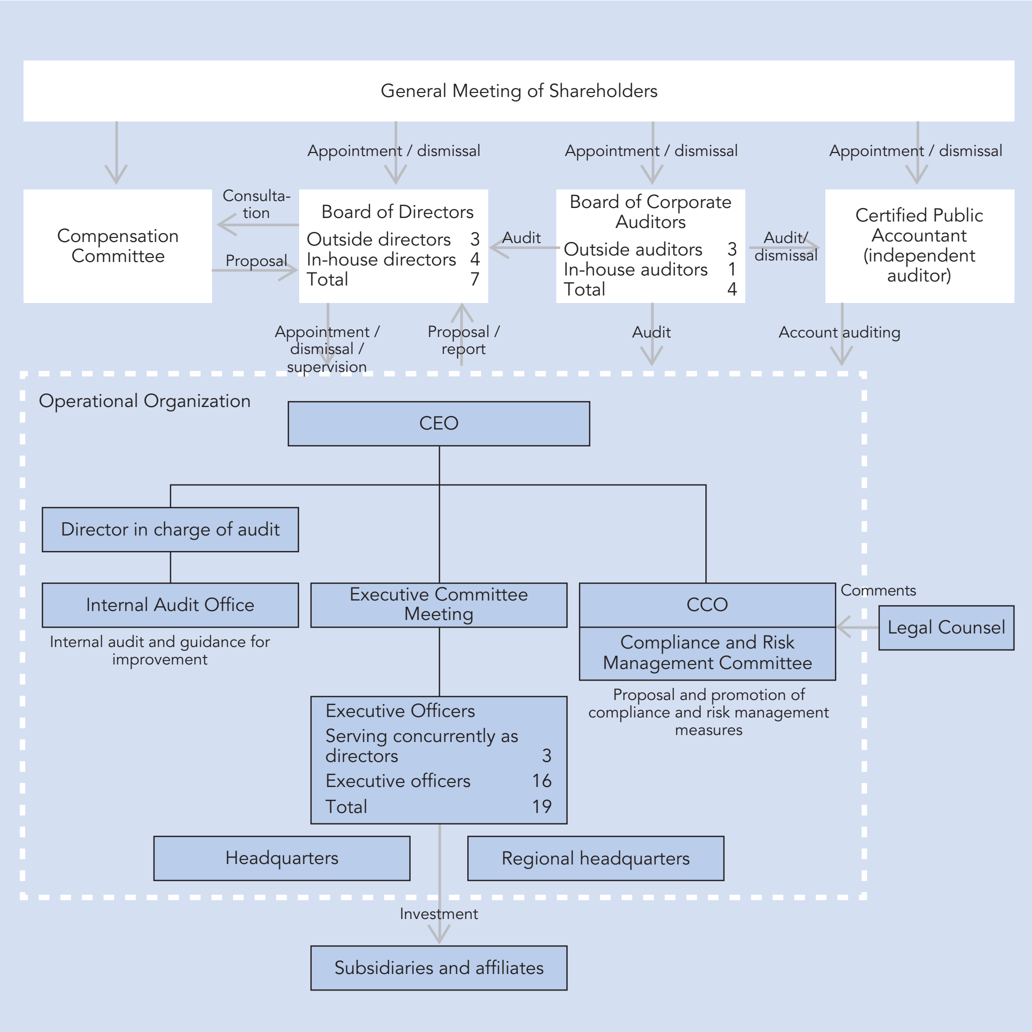
A diagram of our operational organization, management supervision systems and internal control system are presented on page 17.

Corporate Governance System (As of May 25, 2007)

ITEM	DESCRIPTION
Corporate organization:	Company with a Board of Corporate Auditors
Chairman of the Board of Directors:	Outside director
Number of Directors:	7 (including 3 Outside Directors)
Number of Board of Directors meetings in FY06:	15 (including 3 extraordinary meetings)
Outside Directors' attendance rate at Board of Directors' meetings in FY06:	78% (including extraordinary meetings)
Number of Corporate Auditors:	4 (including 3 Outside Corporate Auditors)
Outside Corporate Auditors' attendance rate at Board of Directors' meetings in FY06:	93% (including extraordinary meetings)
Major committee meetings attended by Corporate Auditors:	Board of Directors meetings, Executive Committee meetings, Compliance and Risk Management Committee meetings, Asset Management Committee meetings and Enforcement Evaluation Committee meetings
Number of Board of Corporate Auditors meetings in FY06:	14 (including 2 extraordinary meetings)
Attendance rate at Board of Corporate Auditors meetings in FY06:	97% (including extraordinary meetings)
Average age of Directors and Corporate Auditors:	54
Independent Auditor:	Deloitte Touche Tohmatsu
Internal Audit Division:	Internal Audit Office
Overview of the internal control system:	■ We focus on the following five areas, in accordance with the Fiscal 2007 Basic Policy on Development and Operation of Internal Control System, as revised in February 2007: **1]** Corporate governance supervised by the Board of Directors and Board of Corporate Auditors, including outside members **2]** Development of compliance and risk management-related regulations, and education and training in these issues **3]** Internal audits by the Internal Audit Office **4]** Establishment of internal control systems for the Group **5]** Enhancing the effectiveness of audits by Corporate Auditors through a system of reporting to Corporate Auditors and other means
Compliance system:	■ Appointment of an executive responsible for compliance and risk management (Chief Compliance Officer (CCO)) ■ Appointment of compliance officers at all headquarters departments and seven regional headquarters ■ Monthly meeting of Compliance and Risk Management Committee, chaired by the CCO, to identify compliance issues and assess risk exposure and to deliberate on ways to prevent illegal or improper actions
Support system provided for Outside Directors and Corporate Auditors:	■ As a rule, the secretariat of the Board of Directors distributes the agenda one week in advance of Board meetings, and is also responsible for other measures, such as sharing information on risk and other important matters.

Compensation for directors:	■ The Compensation Committee, which is made up entirely of outside directors and outside corporate auditors, determines compensation for directors and presents its recommendations to the Board of Directors for final approval. ■ Approximately 30% of annual compensation is linked to business results. ■ Compensation paid to all directors is reported in the Annual Report filed pursuant to the Securities and Exchange Law of Japan and Business Report. ■ Other compensation includes stock-compensation-type stock options that can be exercised (exercise price: ¥1) after a director retires, and conventional stock options with an exercise price set, in principle, at the market price of the Company's stock on the day of allocation.
Special factors with an important bearing on corporate governance:	■ Mitsubishi Corporation holds 31.0% of the Company's voting rights, including indirectly held rights. LAWSON is treated as an equity-method affiliate by Mitsubishi Corporation. ■ Our consolidated subsidiary LAWSON TICKET INC. is listed on the JASDAQ market. LAWSON respects its independence as a publicly listed company.
Disclosure policy:	■ Basic Principles for Information Disclosure are presented on our IR site: http://www.lawson.co.jp/company/e/corporate/disclose.html ■ The Company discloses material information, including presentation materials used in meetings to announce business results, in both Japanese and English, on the IR site, without delay.

Corporate Governance System (As of May 25, 2007)



Directors and Corporate Auditors

TAKESHI NIINAMI
President and CEO

Takeshi Niinami became President of LAWSON in May 2002, subsequent to Mitsubishi Corporation's February 2000 acquisition of an equity stake in the Company. Before coming to LAWSON, Mr. Niinami worked in Mitsubishi Corporation's restaurant business and has been a representative director of SODEX CORPORATION (currently LEOC Japan Co., Ltd.), a company specializing in the foodservice business, and an outside director of Kentucky Fried Chicken Japan Ltd.

TORU MORIYAMA
Member of the Board and Senior Executive Vice President

Toru Moriyama was appointed General Manager, Merchandizing & Logistics Division, Senior Executive Vice President and Member of the Board in May 2006. In this capacity he is the executive in charge of merchandising and logistics, core operations of the Company. Prior to joining LAWSON, Mr. Moriyama had a long career at Mitsubishi Corporation, mainly in the marine products business. His posts included those of Manager, Tuna Unit, Foods (Products) Division and Manager, Chubu Block, Living Essentials.

YOSHIYUKI YAHAGI
Member of the Board, Executive Vice President, Chief Financial Officer (CFO)

After a long stint at Mitsubishi Corporation, where he worked mainly in business administration, investments and loans management and risk management, Mr. Yahagi was appointed team leader of the No. 1 Investment and Loans Team, Controller Office. He also served as Asst. Manager, Internal Audit Dept. He was appointed a Member of the Board, Executive Vice President and Chief Financial Officer (CFO), as well as put in charge of the Corporate Planning Office and Human Resources Office at LAWSON in May 2007. As CFO, he is responsible for LAWSON's capital and financial policy. He is also in charge of management planning, business administration and human resources.

MANABU ASANO
Member of the Board, Senior Vice President, Chief Compliance Officer (CCO)

After joining LAWSON, he worked as General Manager, Store Development Department; General Manager, Chubu LAWSON Branch; and as assistant Chief Risk Management Officer (CRO). He was subsequently appointed a Member of the Board, Senior Vice President and Chief Compliance Officer (CCO) in May 2006, and is also in charge of General Affairs and Internal Audit. As the executive responsible for compliance and risk management and for audit operations, Mr. Asano supervises the Company's internal control systems.

1. HIROSHI TASAKA
Member of the Board

2. REIKO OKUTANI
Member of the Board

3. TAKEHIKO KAKIUCHI
Member of the Board

OUTSIDE DIRECTORS

LAWSON's outside directors include experts from academia and business managers. They advise the Company and provide opinions on a range of issues, from overall business strategy development, M&As and capital strategy, including the distribution of profit to shareholders, as well as other important management issues. Their advice, provided from an independent, external perspective, is derived from their experience, insights and knowledge.

The three current outside directors are Professor Hiroshi Tasaka of the Graduate School of Tama University and Representative of Sophia Bank, a think-tank; Reiko Okutani, President, The R Co., Ltd.; and Takehiko Kakiuchi, General Manager, Living Essentials Group CEO Office, Mitsubishi Corporation.

4. MUNEHIKO NAKANO
Standing Corporate Auditor

5. KENJI YAMAKAWA
Standing Corporate Auditor

6. TETSUO OZAWA
Corporate Auditor

7. HIROSHI KUWATA
Corporate Auditor

CORPORATE AUDITORS

Three of the four corporate auditors are outside auditors. The corporate auditors conduct audits with an emphasis on the Internal Control System Basic Policy, in order to assure that LAWSON lives up to the trust society has placed in us, and to assure sound and steady growth.

Our outside corporate auditors are Munehiko Nakano (standing corporate auditor), a former Mitsubishi Corporation executive; Tetsuo Ozawa, a lawyer; and Hiroshi Kuwata, General Manager, Risk Management Dept., Mitsubishi Corporation.

(As of May 25, 2007)

LAWSON's Corporate Philosophy and Code of Conduct

LAWSON assures that all corporate activities conform to its corporate philosophy, and that the Company's management and employees work together as a team for the realization of the goals defined in it. In seeking to live up to our corporate philosophy, we ensure that all of our actions are grounded in our shared values, no matter what changes may take place in the operating environment. Our code of conduct requires employees to accept responsibility for reflecting our values and standards through their actions.

CORPORATE PHILOSOPHY

Happiness and Harmony in Our Community

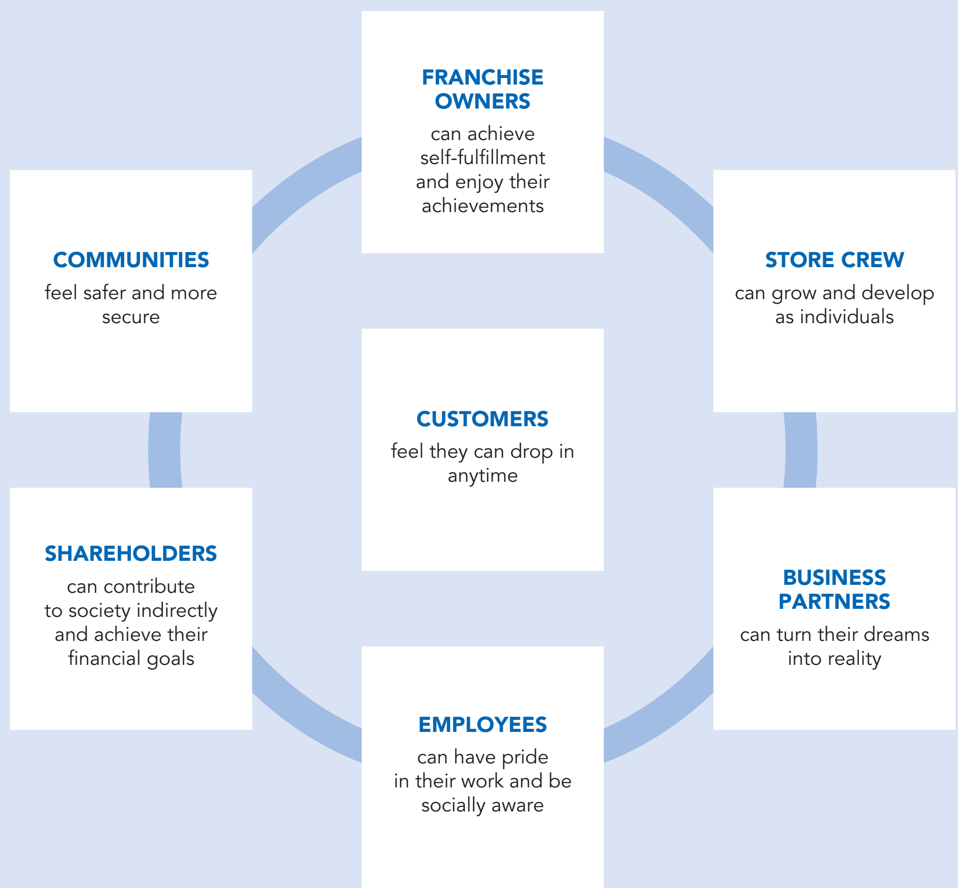
CODE OF CONDUCT

Acting with utmost consideration for others

Challenging with innovative ideas and actions

Having a strong will to attain the objectives

We promise to make LAWSON a place where:



LAWSON believes that honoring these commitments to its stakeholders will translate into higher corporate value.

Corporate Social Responsibility

LAWSON firmly believes that proactively addressing and resolving issues from the standpoint of social responsibility to live up to our corporate philosophy of realizing "Happiness and Harmony in Our Community," will raise our corporate value and, accordingly, shareholder value. This will bring benefits to all stakeholders and contribute to protection of the Earth's environment.

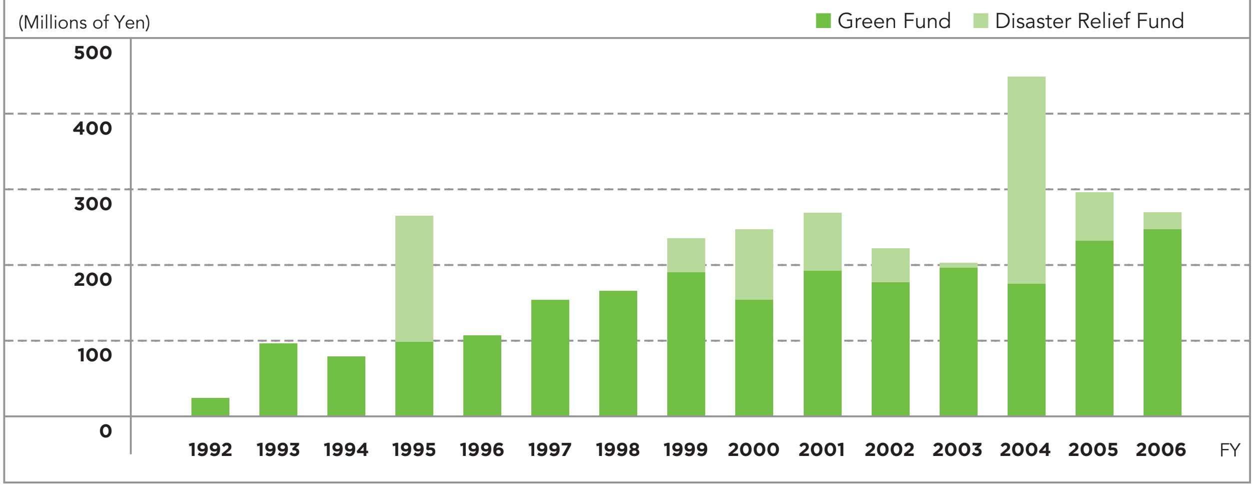
Major Initiatives in FY2006

Greenification Activities

LAWSON Green Fund activities were instigated in 1992. Donations to the LAWSON Green Fund, including contributions from LAWSON headquarters, totaled ¥2.29 billion as of the end of February 2007. Funds donated at stores throughout Japan are provided to the National Land Afforestation Promotion Organization, which promotes tree planting, thinning, undergrowth clearance and other forestry activities. In fiscal 2006, franchise owners, store managers, crews and LAWSON headquarter staff participated in over 80 events. Our afforestation activities (planting and arboriculture) in 1,528 locations in Japan, covering 4,510 hectares, have benefited more than 11.27 million trees*.

**The figures for the area covered and number of trees are estimates based on the amount of donations received by the Green Fund and the history of fund activities.*

Green Fund Donations



Food Waste Recycling Measures (Using Waste Oil, Making Animal Feed and Fertilizer)

LAWSON is working to improve the precision of its merchandise ordering system in order to minimize food waste, in addition to implementing the following three initiatives.

1. LAWSON started recycling waste oil (edible oil) in January 2006, and we have now built a national waste oil collection system. As of the end of March 2007, 86% of LAWSON stores were recycling waste oil.
2. 900 stores in metropolitan Tokyo, Nagoya and elsewhere in Japan recycle food waste by converting it into animal feed and fertilizer.
3. Organic waste is dewatered and dried using a processor to reduce volumes at some stores. In fiscal 2006, approximately 60 stores were using organic waste processors.

The combined effect of these three methods helped LAWSON to achieve a food waste recycling level of 25% on an all-store basis as of March 31, 2007.

Japan's Food Recycling Law requires that food product recycling levels must reach at least 20% by fiscal 2006. In the year to March 2007, LAWSON achieved an average recycling level of 36% at Company-operated stores. The recycling level for all stores, including franchised stores, was 18%.

Customer Input

In 2005, as part of the program to commemorate our 30th anniversary, we invited customers to share their ideas on the theme of "The Convenience Store of the Future" and selected the top prize on November 12 of that year. This award was handed to an entry titled "Convenience stores that support raising kids." In March 2006, we set up an in-house project team and in July 2007, via our web site, we started soliciting people's suggestions on how convenience stores could provide support for families raising children.

Based on the input received, in December 2006 we opened the first Happy LAWSON store on a 6-month trial basis in Nihonbashi, Tokyo. The merchandise, service information and know-how gained through the operation of this store will be used to develop stores that meet the requirements of families raising children. On two occasions during fiscal 2006, we ran the "Happy Child-Rearing Project." LAWSON donated one yen for every Miffy-themed picture plate customers received. The donations were used to provide picture books and daily-use articles to ZENBOKYOU, a social welfare organization that supports single mothers and their children.

01

02

01 Fertilizer made from food waste
02 Happy LAWSON, Nihonbashi store*

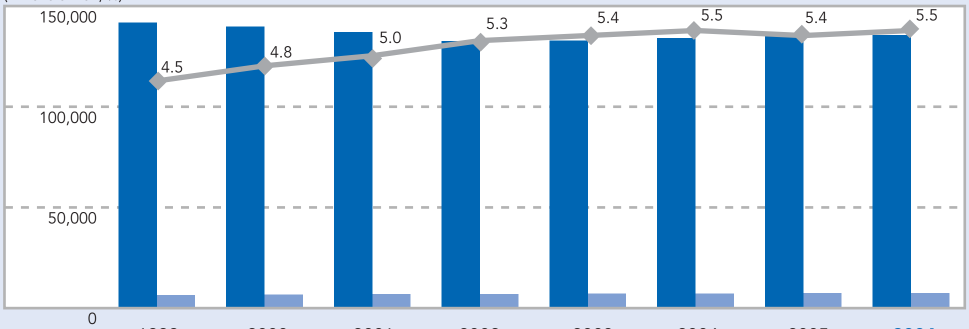
**The Nihonbashi store closed in June 2007 and a new store (Yamashita Koen Store, Yokohama) opened in July.*

Financial Section

Overview of the CVS Sector and Selected Financial Data

CVS Share of the Total Retail Market

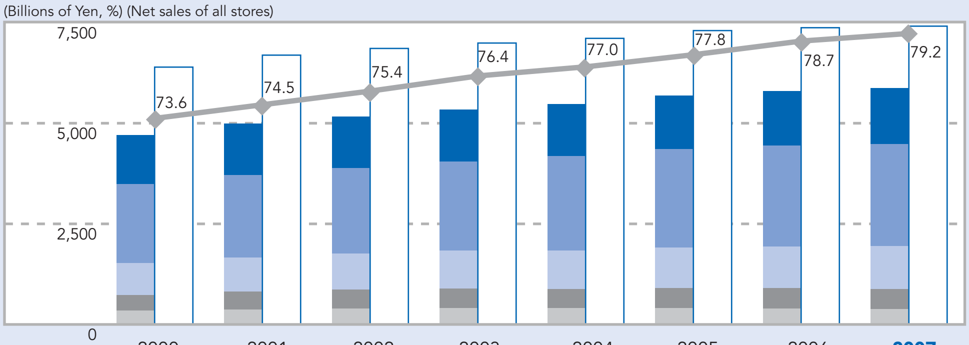
(Billions of Yen, %)



Years ended December 31	1999	2000	2001	2002	2003	2004	2005	**2006**
■ Total retail industry annual sales	¥141,528	¥139,435	¥136,808	¥132,280	¥132,446	¥133,712	¥135,055	**¥135,257**
■ CVS sector annual sales	6,383	6,680	6,846	6,980	7,096	7,289	7,360	**7,399**
— CVS share (%)	4.5%	4.8%	5.0%	5.3%	5.4%	5.5%	5.4%	**5.5%**

Share of CVS Market Held by Top Four Chains (Sales)

(Billions of Yen, %) (Net sales of all stores)

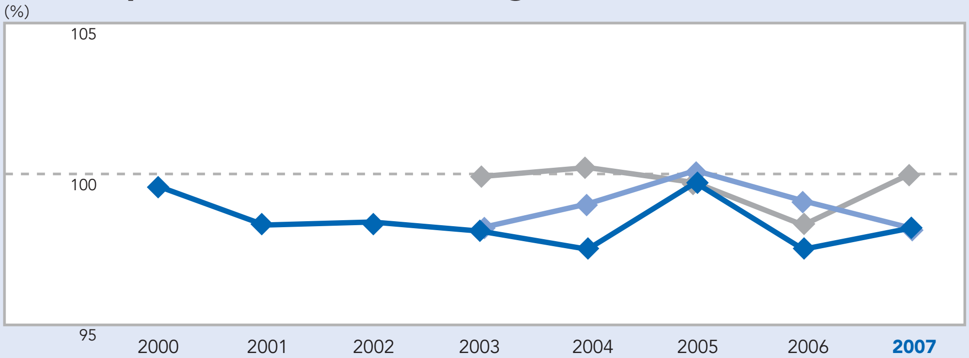


February 28 and 29	2000	2001	2002	2003	2004	2005	2006	**2007**
■ LAWSON	¥1,221	¥1,275	¥1,286	¥1,294	¥1,288	¥1,329	¥1,362	**¥1,387**
■ Seven-Eleven Japan	1,964	2,047	2,114	2,213	2,343	2,441	2,499	**2,534**
■ FamilyMart	783	843	899	932	954	998	1,032	**1,069**
■ Circle K	391	447	467	485	480	503	505	**497**
■ Sunkus	342	366	393	406	403	403	394	**376**
Total	4,701	4,978	5,159	5,330	5,468	5,674	5,792	**5,863**
— (Share) (%)	73.6%	74.5%	75.4%	76.4%	77.0%	77.8%	78.7%	**79.2%**
□ CVS industry	¥6,383	¥6,680	¥6,846	¥6,980	¥7,096	¥7,289	¥7,360	**¥7,399**

CVS industry figures are for previous calendar years ended December 31.

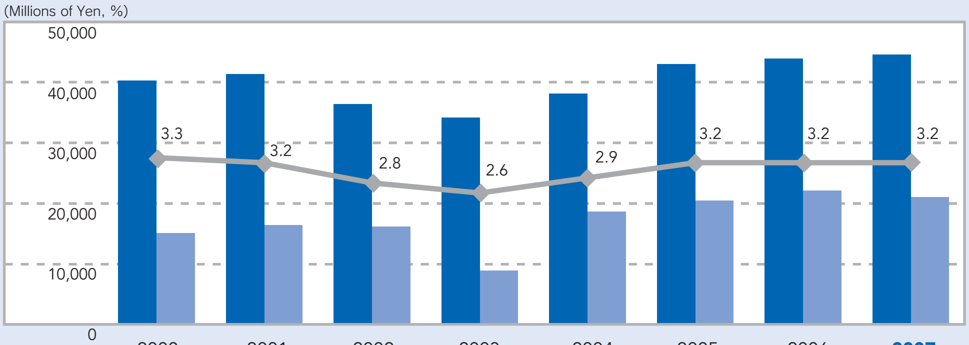
YoY Rate on Existing Store Sales, Average Number of Customers and Average Purchase Value per Customer in Existing Stores

(%)



	2000	2001	2002	2003	2004	2005	2006	**2007**
— YoY rate on existing store sales	99.6	98.3	98.4	98.1	97.5	99.7	97.5	**98.2**
Average number of customers and average purchase value per customer in existing stores								
— Number of customers	–	–	–	98.2	99.0	100.1	99.1	**98.2**
— Average purchase value per customer	–	–	–	99.9	100.2	99.7	98.3	**100.0**

Operating Income, Operating Income Ratio and Net Income

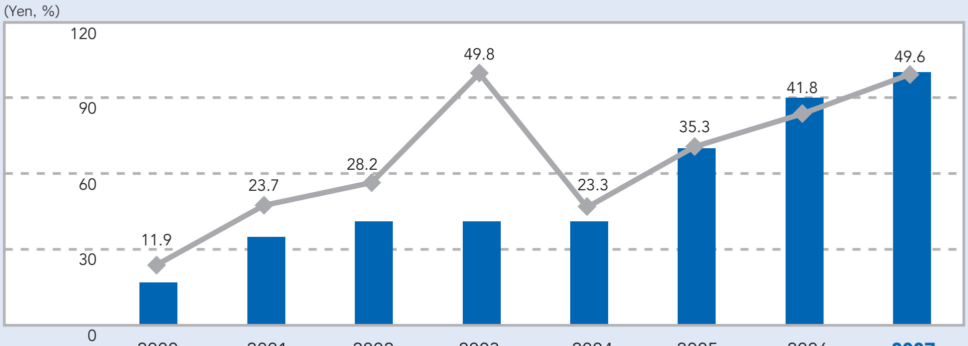


	2000	2001	2002	2003	2004	2005	2006	**2007**
Operating Income	¥40,185	¥41,279	¥36,363	¥34,107	¥38,087	¥42,941	¥43,867	**¥44,513**
Operating Income Ratio	3.3%	3.2%	2.8%	2.6%	2.9%	3.2%	3.2%	**3.2%**
Net Income	¥15,011	¥16,368	¥16,123	¥ 8,861	¥18,571	¥20,435	¥22,025	**¥20,983**

Net Income per Share and ROE

	2000	2001	2002	2003	2004	2005	2006	**2007**
Net Income per Share	¥143	¥148	¥146	¥82	¥176	¥198	¥216	**¥202**
ROE	16.8%	11.9%	9.8%	5.9%	12.1%	13.0%	13.1%	**11.3%**

Cash Dividends per Share and Payout Ratio



	2000	2001	2002	2003	2004	2005	2006	**2007**
Cash Dividends per Share	¥17	¥35	¥41	¥41	¥41	¥70	¥90	**¥100**
Payout Ratio	11.9%	23.7%	28.2%	49.8%	23.3%	35.3%	41.8%	**49.6%**

Consolidated Eight-Year Summary

LAWSON, INC. and Consolidated Subsidiaries
Years Ended February 28 and 29

	2007	2006	2005
For the year:			
Operating revenues			
Franchise commission from franchised stores	**¥174,325**	¥170,785	¥162,963
Net sales from Company-operated stores	**75,151**	66,027	63,802
Other	**33,577**	31,246	27,630
Total operating revenues	**283,053**	268,058	254,395
Operating income	**44,513**	43,867	42,941
Net income	**20,983**	22,025	20,435
Cash flows from operating activities	**47,596**	46,933	47,329
Cash flows from investing activities	**(31,754)**	(55,282)	(33,297)
Cash flows from financing activities	**(736)**	(7,795)	(13,836)
Capital expenditure[2]	**49,822**	54,417	46,873
Depreciation and amortization[3]	**21,352**	20,896	19,641
At year-end:			
Total assets	**¥398,258**	¥375,107	¥356,310
Total equity	**199,493**	175,184	160,282
Equity ratio	**49.0%**	46.7%	45.0%
Interest-bearing debt	**–**	–	–
Ratio of interest-bearing debt	**–**	–	–
Cash and cash equivalents	**75,547**	60,441	76,585
Total number of stores[4]	**8,564**	8,366	8,077
Number of employees (full-time)	**3,614**	3,585	3,391

Per share data:			
Net income	**¥ 202**	¥ 216	¥ 198
Cash dividends	**100**	90	70
Payout ratio	**49.6%**	41.8%	35.3%
Financial data:			
ROE	**11.3%**	13.1%	13.0%
ROA	**5.4%**	6.0%	5.7%
Net sales of all stores:			
Net sales by store category			
Franchised stores[5]	**¥1,311,479**	¥1,295,704	¥1,265,275
Company-operated stores	**75,151**	66,027	63,802
Net sales by product category[5]			
Processed foods	**¥ 705,155**	¥ 682,006	¥ 665,687
Fast foods	**324,993**	312,289	297,369
Daily delivered foods	**155,575**	150,917	148,134
Non-food products	**200,907**	216,519	217,887
Net sales of all stores	**¥1,386,630**	¥1,361,731	¥1,329,077

Notes: 1. The U.S. dollar amounts represent translations of Japanese yen at the approximate exchange rate at February 28, 2007, of ¥118.44=$1.
2. Effective from annual report 2006, the composition of capital expenditure has changed to also include leases, investments and advances, and construction assistance guarantees. Please refer to page 39 for details.
3. Including depreciation and amortization of intangible fixed assets.
4. Shanghai stores are not included because SHANGHAI HUALIAN LAWSON CO., LTD. was excluded from the scope of consolidation from April 2005.
5. These figures, as reported by franchised stores, are unaudited.

				Millions of Yen	Thousands of U.S. Dollars[1]
2004	2003	2002	2001	2000	**2007**
¥153,910	¥149,032	¥141,621	¥135,237	¥124,587	**$1,471,842**
67,479	80,954	101,353	132,921	149,458	**634,507**
24,212	20,348	13,142	12,061	17,808	**283,494**
245,601	250,334	256,116	280,218	291,853	**2,389,843**
38,087	34,107	36,363	41,279	40,185	**375,827**
18,571	8,861	16,123	16,368	15,011	**177,161**
37,424	33,860	44,804	52,793	67,790	**401,857**
(40,621)	(3,787)	(44,031)	(54,696)	121,758	**(268,102)**
(14,364)	(7,247)	(58,236)	18,707	(92,521)	**(6,214)**
48,303	75,828	59,810	32,651	30,703	**420,652**
18,499	16,071	16,328	16,021	15,017	**180,277**
¥354,831	¥342,599	¥342,934	¥387,236	¥339,413	**$3,362,530**
154,317	151,864	149,827	178,448	95,932	**1,684,339**
43.5%	44.3%	43.7%	46.1%	28.3%	
–	–	3,140	23,530	71,817	
–	–	0.9%	6.1%	21.1%	
76,389	93,994	71,269	128,655	111,753	**637,850**
7,967	7,721	7,824	7,749	7,432	
3,402	3,462	3,817	4,170	4,234	
				Yen	U.S. Dollars[1]
¥ 176	¥ 82	¥ 146	¥ 148	¥ 143	**$ 1.70**
41	41	41	35	17	**0.84**
23.3%	49.8%	28.2%	23.7%	11.9%	
12.1%	5.9%	9.8%	11.9%	16.8%	
5.3%	2.6%	4.4%	4.5%	4.0%	
¥1,220,819	¥1,213,088	¥1,184,204	¥1,144,717	¥1,073,422	**$11,072,940**
67,479	80,954	101,353	132,921	149,458	**634,507**
¥ 625,031	¥ 600,508	¥ 583,712	¥ 562,777	¥ 528,188	**$ 5,953,690**
302,568	303,098	297,030	362,979	350,702	**2,743,946**
139,506	138,353	150,862	90,569	89,248	**1,313,534**
221,192	252,083	253,953	261,313	254,742	**1,696,277**
¥1,288,297	¥1,294,042	¥1,285,557	¥1,277,638	¥1,222,880	**$11,707,447**

Management's Discussion and Analysis

■ Industry Overview

In the Japanese retail industry, the 2000 abolition of the Large-Scale Retail Store Law and enforcement of the Large-Scale Retail Store Location Law, made it easier for companies to set up large-scale retail stores in suburban areas, triggering a rush to construct large-scale shopping centers. Meanwhile, with regard to small and medium-sized retail stores, a large number of convenience stores (CVS), specialty stores and restaurant and ready-made meal outlets continue to be opened, with the number of chain stores increasing, particularly in residential and suburban areas. On the other hand, small and medium-sized retailers, which congregate around train stations and central city areas, are finding it increasingly difficult to generate profits. As a result, in regional cities in particular, increasing concerns have been expressed about the emptying of central city areas as consumers flock to large-scale shopping centers and major general merchandizing stores (GMS) in suburban areas.

Because of this, the Diet passed and enacted revisions to the Three New Acts about Harmonization of City Planning and Commercial Policy (City Planning Law, Central City Revitalization Law and Large-store Establishment Law) in May 2006, signaling a move to curb the excessive opening of major retail properties in suburban areas.

Looking ahead, major GMS chains and specialty stores, which have relied on large-scale outlets in the suburbs, are expected to intensify competition for securing locations near train stations and in central city areas. An example of this has already been seen with the acquisition of a ready-made meal supplier by a major GMS chain. Under these circumstances, the value of the networks of small outlets already established by CVS operators is expected to increase.

In the CVS sector, major chains continue to open stores in large numbers. This is increasing the saturation of conventional CVS formats targeting men in their 20s and 30s as core customers. Among the major CVS chains, some chains have seen daily sales at new stores slip year on year. This suggests that, if conventional stores continue to be opened in large numbers, the number of low-profit stores will also increase. LAWSON's view is that such a situation increases the risk of a decline in the earnings of franchised store owners as well as capital efficiency, leading to lower ROE.

Retail Industry Market Size and CVS Share

(Billions of Yen)

Years ended December 31	**2006**	2005	2004	2003	2002
Total retail industry annual sales	**¥135,257**	¥135,055	¥133,712	¥132,446	¥132,280
CVS sector annual sales	**7,399**	7,360	7,289	7,096	6,980
CVS share	**5.5%**	5.4%	5.5%	5.4%	5.3%

Source: "Survey of Commerce," Ministry of Economy, Trade and Industry

Share of CVS Market Held by Top Five Chains (Sales)

(Billions of Yen)

February 28 and 29	**2007**	2006	2005	2004	2003
LAWSON	**¥ 1,387**	¥ 1,362	¥ 1,329	¥ 1,288	¥ 1,294
Seven-Eleven Japan	**2,534**	2,499	2,441	2,343	2,213
FamilyMart	**1,069**	1,032	998	954	932
Circle K	**497**	505	503	480	485
Sunkus	**376**	394	403	403	406
Total	**5,863**	5,792	5,674	5,468	5,330
(Share)	**79.2%**	78.7%	77.8%	77.0%	76.4%

Note: Total figures are for the years ended February 28 and 29.

■ Management Measures in Fiscal 2006

LAWSON's major goal in fiscal 2006 was to increase the number of customers through expansion of its customer base. To this end, LAWSON implemented the following management initiatives.

(1) We continued to emphasize the Three Challenge Practices*—promoting the enhancement of quality (Q), service (S), and cleanliness (C)—aiming to raise the level of customer satisfaction.

(2) We made greater use of "store charts"** (analysis of individual store information) that have been introduced nationwide with the aim of assembling merchandise assortments and creating store displays matched to regional preferences of customers of individual stores.

(3) We targeted product development at new customers, namely women and middle-aged and elderly customers, making progress in developing "health-oriented products," "products in appropriately sized small quantities," and "perishable foods and daily delivered foods."***

(4) We strengthened sales promotion activities aimed at expanding the customer base by running such events as the LAWSON Fair and a campaign allowing customers to exchange shopping points for Miffy-themed picture plates. The ultimate goal of these actions was to increase the number of customers.

(5) We also promoted initiatives centered on point cards, which have won strong support from female customers. In order to strengthen merchandise assortments of individual stores through customer relationship management, we worked to sign up more members to the LAWSON PASS credit card, which is also used as a shopping point card. Furthermore, for those customers who dislike owning credit cards, in January 2007 we rolled out the MY LAWSON POINT point card nationwide.

(6) To expand the customer base, we opened stores using the format—"LAWSON," "NATURAL LAWSON" or "LAWSON STORE100"—we thought best suited the location. And in order to expand the customer base still further, on February 28, 2007 we entered into an equity-based business alliance with Ninety-nine Plus Inc., which saw us subscribe to a private placement of shares to acquire approximately 20% of the company's total issued shares.

(7) As an initiative to strengthen existing stores, we developed LAWSON PLUS, stores that carry perishable foods as a main product line to respond to specific local demand. We have started converting existing LAWSON stores into LAWSON PLUS stores.

The Three Challenge Practices are points that franchised store owners, employees, and store crew (part-time workers) must pay particular attention to in running LAWSON stores. They are (1) ensuring merchandise assortments are matched to individual locations, (2) serving customers courteously, and (3) keeping stores and surrounding areas clean.

** *An important tool for franchised store owners to make decisions, store charts include analysis of marketing and management on an individual store basis.*

*** *Includes tofu, natto (fermented soy beans) and other side dishes and delicatessen items as well as cooked noodles and other food products with a relatively short sales period after manufacture. Basically, these products are ordered and delivered every day.*

■ Product Overview

Sales by Product Category (consolidated, total net sales)

During the fiscal year under review, strong growth in sales of processed and fast foods compensated for lower sales of non-food products. In the processed foods category, net sales increased 3.4% year on year to ¥705,155 million. Cigarette sales rose 7.4% year on year on an all-store basis, inflated by higher tax from July 2006; existing store sales rose 4.3% due to this tax hike. Other main contributors to the higher sales in the processed foods category were new products belonging to national brands, and rice snacks and baked goods, as LAWSON offered a fuller lineup of products matched to regional preferences for seniors. In the fast foods category, sales rose 4.1% to ¥324,993 million. Rice dishes struggled, as strong *sushi* sales failed to counter sharply lower sales of boxed lunches and rice balls. However, overall category sales were bolstered by robust sales of delicatessen items due to the launch of health-conscious products such as salads, and of *Karaage-kun* crispy Japanese-style fried chicken and other counter products, as we actively launched new products. In the daily delivered foods category, sales rose 3.1% to ¥155,575 million, lifted by buoyant sales of desserts and bakery items thanks to the success of new product launches and shopping point campaigns. The non-food products category, however, saw sales drop 7.2% to ¥200,907 million despite firm sales of energy drinks, health care products, books and certain other products. This overall decline was primarily attributable to the fact that Highway Card sales were recorded in the previous fiscal year until they were terminated in September 2005, a decrease in sanitary goods following strong sales in fiscal 2005 of products for countering hay fever, and lackluster magazine sales.

Net Sales by Product Segment (consolidated, total net sales)

(Millions of Yen)

Years ended February 28 and 29	2007*	2006	2005	2004	2003
Fast foods	**¥ 324,993**	¥ 312,289	¥ 297,369	¥ 302,568	¥ 303,098
Daily delivered foods	**155,575**	150,917	148,134	139,506	138,353
Processed foods**	**705,155**	682,006	665,687	625,031	600,508
Total food sales	**1,185,724**	1,145,212	1,111,190	1,067,105	1,041,959
Non-food products	**200,907**	216,519	217,887	221,192	252,083
Net sales of all stores	**¥1,386,630**	¥1,361,731	¥1,329,077	¥1,288,297	¥1,294,042

* *Figures in the above table are for the fiscal year ended February in each year.*
** *Processed foods includes cigarettes.*

Breakdown of Net Sales by Product Segment (consolidated, total net sales)

(%)

Years ended February 28 and 29	2007*	2006	2005	2004	2003
Fast foods	**23.4%**	22.9%	22.4%	23.5%	23.4%
Daily delivered foods	**11.2**	11.1	11.1	10.8	10.7
Processed foods**	**50.9**	50.1	50.1	48.5	46.4
Total food sales	**85.5**	84.1	83.6	82.8	80.5
Non-food products	**14.5**	15.9	16.4	17.2	19.5

* *Figures in the above table are for the fiscal year ended February in each year.*
** *Processed foods includes cigarettes.*

Gross Profit Margin by Product Segment (parent company)

The overall gross profit margin improved by about 0.1 of a percentage point, roughly in line with our target. The loss of a half year's sales of low-margin Highway Cards, which were terminated in mid-September 2005, elevated the gross profit margin by about 0.2 of a percentage point on a fiscal year basis. On the other hand, higher sales of low-margin cigarettes ahead of a tax hike had an approximate 0.1 of a percentage point negative impact on the gross profit margin. In the non-food products category, there was a marked improvement in the markup from the previous fiscal year. This was due to a lower share of sales of low markup products such as books and magazines in the sales mix; increasing markups of daily necessities; and an increasing share in the non-food products category of commission income from bill settlement services.

Gross Profit Margin by Product Segment (parent company)

(%)

Years ended February 28 and 29	2007*	2006	2005	2004	2003
Fast foods	**36.5%**	36.8%	36.4%	35.6%	35.7%
Daily delivered foods	**33.8**	33.6	33.3	32.5	32.5
Processed foods**	**26.4**	26.7	26.7	26.9	27.3
Non-food products***	**38.0**	35.8	34.0	33.4	29.9
Gross profit margin	**31.3**	31.2	30.8	30.7	30.3

* *Figures in the above table are for the fiscal year ended February in each year.*
** *The processed foods category includes cigarettes.*
*** *Calculation of the gross profit margin for non-food products includes bill settlement and other commission income.*

Bill Settlement Services (parent company)

Years ended February 28 and 29	2007*	2006	2005	2004	2003
Bill settlements (millions of yen)	**¥1,204,004**	1,165,255	1,035,936	919,205	817,656
No. of transactions (millions)	**140.9**	130.6	118.9	108.4	100.0
No. of companies handled	**396**	349	309	283	245
Commission income (millions of yen)	**8,141**	7,507	6,768	6,368	5,990

**Figures in the above table are for the fiscal year ended February in each year.*

Merchandising Strategy

In the area of merchandising strategy, LAWSON made progress developing products aimed at middle-aged, senior and women customers. The goal was to expand the customer base by targeting these less-traditional customer segments.

In the case of the *Gohantei* series, a rice dish brand launched in 2004 based on the concepts of "surprise" and "innovation," in April 2006 we began selling *Yasai to Isshoni*, a new offering of small portions of vegetables and rice aimed at women and health-conscious customers. In the same vein, the following May, we developed *Kurogome iri Onigiri* (rice ball with black rice and black beans), the first NATURAL LAWSON brand dish offered at LAWSON stores. Subsequently, in September the same year, we leveraged know-how from product development for NATURAL LAWSON to augment the *Gohantei* series with the launch of *Gokoku Hayashi to Guriru Yasai* (stew with grilled vegetables and 5-grain rice).

In sushi, which is popular with middle-aged, senior and health-conscious customers, we actively developed a range of new products, including hand-rolled sushi, sushi in small boxes and sushi rice balls.

We also continued to offer products for the health-conscious, with the launch of the *Neba-neba Menu* featuring cold noodles, salads and other offerings based on food ingredients with a *neba-neba*, or sticky, quality such as *okra*, *tororo* potato, glutinous yam, *natto* and *mekabu* seaweed. All these ingredients have high nutritional values.

In June 2006, we ran the LAWSON Fair, a major sales promotion campaign that had as its central planks limited-time products and on-the-spot prize draws for coupons when customers purchased products. Similarly, on two occasions—from July through August 2006 and then from November 2006 through January 2007—we ran a shopping point collection campaign allowing customers to exchange their points for Miffy-themed picture plates. This campaign tied in with the launch of the Happy Child-Raising Project* and was designed to attract more customers to our stores during the key summer and winter sales periods.

**The Happy Child-Raising Project was launched in July 2006 and was inspired by the winning entry in an essay competition staged to mark LAWSON's 30th anniversary. Through this project, LAWSON has taken up the challenge presented in the essay of helping families to raise children.*

■ Store Development

During the past fiscal year, LAWSON worked to develop stores that it expects to generate high income by rigorously adhering to its proprietary store opening standards, centered on return on investment (ROI), when opening stores mainly in large city areas in the Kanto, Kinki, and Chubu regions. Furthermore, we worked to secure quality franchised store owners and focused on gathering information on prime locations for new stores by fostering closer cooperation between store operation and development divisions and by working with leading companies in candidate areas.

When opening stores, we focused on picking the right format for the needs of the area from our three main formats: "LAWSON," "NATURAL LAWSON" and "LAWSON STORE100." In candidate locations where use of the conventional LAWSON format was highly likely to expose us to stiff competition from other major convenience store chains, we opted to open "NATURAL LAWSON" and "LAWSON STORE100" stores to differentiate ourselves from other chains and to match customer needs in the area.

The pursuit of store formats best suited to each location was a key theme in the past fiscal year. In this vein, LAWSON initiated trials of Senior-friendly LAWSON, a format designed to cater to the needs of elderly customers in regions with a growing number of senior citizens. These stores feature special merchandise assortments, shopping carts, relaxation spaces and other features geared to the needs of the elderly. In urban areas, LAWSON also began converting existing stores to an enhanced format to expand the customer base. This hybrid format features perishable foods based on know-how garnered from the "LAWSON STORE100" stores. Following these trials during fiscal 2006, LAWSON named this format "LAWSON PLUS," positioning it as a format focused on sales spaces and product mixes, centered on products for seniors and women. To ensure that customers recognized these new stores as different to conventional LAWSON stores, we changed the outside and inside appearance, including the color of sign boards. Together with a stronger merchandise assortment for middle-aged, senior and women customers, these efforts were aimed at expanding the customer base.

Part of LAWSON's strategy is to open stores in diverse locations. In August 2006, we opened LAWSON + toks, a new type of convenience store for train stations. This format was developed in conjunction with Tokyu Corporation under a business alliance inked in the fiscal year ended February 28, 2006. By combining the functions of a train station store with the unique features of the convenience store format, we found new possibilities for convenience stores.

Along the same lines, LAWSON has opened stores in special captive commercial spaces, namely hospitals. During the past fiscal year, LAWSON opened another 14 Hospital LAWSON stores, bringing the number of these stores to 33 at the end of the fiscal year. We intend to expand this business model as a format that we expect to grow in an aging society in Japan.

We also made steady progress preparing to capitalize on business opportunities likely to occur after post office privatization with respect to Postal LAWSON stores, based on our alliance with Japan Post. As of February 28, 2007, there were five of these stores inside post offices in Japan. In a new initiative, in October 2006 we began trialing joint delivery in Kochi Prefecture, thereby raising the possibility of opening stores in areas where we had given up on due to poor distribution efficiency.

We believe that one of LAWSON's defining strengths lies in a flexible and dynamic store development system that makes possible alliances with diverse partners. Moving forward, based on mold-breaking concepts, we will rise to the challenge of opening stores in diverse locations as we pursue the potential of new business opportunities.

As a result of the aforementioned measures, domestic store openings in fiscal 2006 numbered 700 while store closures reached 502, including relocated stores. At February 28, 2007, LAWSON's domestic network comprised 8,564 stores, including 100 NATURAL LAWSON and 80 LAWSON STORE100 stores, a net increase of 198 from a year earlier.

The network of SHANGHAI HUALIAN LAWSON CO., LTD., an affiliate in the People's Republic of China accounted for under the equity method, reached 291 stores, an increase of 8 stores, as of December 31, 2006.

Number of Stores in the LAWSON Network

Years ended February 28 and 29	2007	2006	2005	2004	2003
Number of stores	**8,564**	8,366	8,077	7,821	7,625
Openings	**700**	717	711	625	502
Closings	**502**	428	455	429	611
Net increase (decrease)	**198**	289	256	196	(109)

Number of Stores by FC Contract Type

February 28 and 29	2007	2006	2005	2004	2003
B	**1,512**	1,674	1,836	1,992	2,200
Share (%)	**17.7**	20.0	22.7	25.4	28.8
G	**2,209**	2,272	2,335	2,415	2,446
Share (%)	**25.8**	27.2	28.9	30.9	32.1
C*	**4,372**	4,012	3,560	3,065	2,645
Share (%)	**51.0**	48.0	44.1	39.2	34.7
Franchised stores	**8,093**	7,958	7,731	7,472	7,291
Share (%)	**94.5**	95.1	95.7	95.5	95.6
Company-operated stores	**471**	408	346	349	334
Share (%)	**5.5**	4.9	4.3	4.5	4.4
Total	**8,564**	8,366	8,077	7,821	7,625
Share (%)	**100.0**	100.0	100.0	100.0	100.0

** Includes NATURAL LAWSON franchised stores.*

Outline of Store Contracts

Contract type		C	G	B
Contract term		10 years from store opening day		
Owner conditions		At least 20 years old, 2 full-time store workers		
Land and buildings		Prepared by LAWSON		Prepared by franchisee
Investment in store construction and interior decoration expenses		Borne by LAWSON		Borne by franchisee
Signage and business fixtures		Prepared by LAWSON		
Payment by franchisee at time of contract*	Franchise fee	¥1.5 million (Contract fee, training expenses, and store opening preparation commission, each ¥500,000)		
	Investment	¥1.5 million (Including payment for some merchandise purchased on behalf of the store)		
Guarantee deposit provided by franchisee		Not required	Average monthly sales x 2 months	Not required
Head Office income**		Gross profit x 50%	Gross profit x 45%	Gross profit x 34%
Burden of utility expenses		Franchisee		
Minimum guarantee (annual)** (thousands of yen)		21,000	22,200	22,200

* *The above amount is paid by franchisee to Head Office at the time of the franchising contract. In addition, the franchisee needs to separately prepare a total of ¥500,000, including float at time of store opening.*

** *Head Office income and minimum guarantee are in the case of stores operating on a 24-hour basis.*

■ Scope of Consolidation

The consolidated results for fiscal 2006 include the performances of nine members of the LAWSON Group—six consolidated subsidiaries and three affiliates accounted for under the equity method—and the parent company. These subsidiaries and affiliates are broadly involved in five categories of business: CVS operations, financial services, other services, overseas services and restaurant services. The business operations and fiscal results of companies included within the scope of consolidation are presented below.

CVS Operations

The LAWSON Group is developing four CVS formats: LAWSON, INC. is developing the "LAWSON" and "LAWSON PLUS" formats, while NATURAL LAWSON, Inc. and VALUE LAWSON, Inc are developing the "NATURAL LAWSON" and "LAWSON STORE100" formats, respectively.

NATURAL LAWSON, Inc. (Consolidated Subsidiary)

NATURAL LAWSON is a CVS format targeting mainly working women and particularly health-conscious customers, based on the key words "beauty," "health" and "convenience." The first store was opened in July 2001. In April 2004, one business division within the Head Office was spun off as NATURAL LAWSON, Inc., a wholly owned subsidiary of LAWSON. NATURAL LAWSON, Inc. undertakes store management guidance for NATURAL LAWSON and product planning and development under contract for LAWSON. In the fiscal year ended February 28, 2007, the company endeavored to achieve further differentiation from the conventional CVS business model by strengthening merchandising aimed at health-conscious and women customers. In addition, it promoted operations based on the introduction of individual store information analysis. In a new development, it began trialing the franchising of stores and as a result there were five franchised stores at the end of the fiscal year under review. In the fiscal year ending February 29, 2008, in addition to improving existing stores through enhanced product development and stronger store management guidance, the company will continue to franchise directly operated stores as it seeks to move back into the black on a single fiscal year basis.

At present, LAWSON, INC. owns the "NATURAL LAWSON" stores, leaving NATURAL LAWSON, Inc. to focus on store management guidance and product development.

(Millions of Yen)

	2007	2006	2005	2004	2003
Operating income (loss)	**¥(874)**	¥(690)	¥19	–	–
Net income (loss)	**(891)**	(723)	18	–	–
No. of stores	**100**	51	28	14	13

VALUE LAWSON, Inc (Consolidated Subsidiary)

This consolidated subsidiary operates "LAWSON STORE100" perishable food convenience stores. "LAWSON STORE100" stores target women and seniors with a concept of "supporting time saving, simplicity, and convenience in everyday life." These stores provide a wide range of products spanning processed foods and daily necessities at a uniform price of ¥100 (excluding consumption tax). The main products comprise fresh fruit and vegetables, handy boxed lunches and side dishes. VALUE LAWSON Inc. was founded in April 2005 as a wholly owned subsidiary to establish the "LAWSON STORE100" business format, which weds the CVS and mini-supermarket formats, as well as to perform product planning and development for these stores. The company opened its first store in May 2005. To differentiate the format from peer companies, the company is actively developing a private brand called *Value Line*. As of February 28, 2007, there were approximately 320 stock keeping units (SKUs) of *Value Line*, an increase of 180 over the past year.

(Millions of Yen)

	2007	2006	2005	2004	2003
Operating income (loss)	**¥ (980)**	¥(623)	–	–	–
Net income (loss)	**(1,311)**	(709)	–	–	–
No. of stores	**80**	35	–	–	–

Financial Services

LAWSON ATM Networks, Inc. (Consolidated Subsidiary)

This consolidated subsidiary was established in May 2001 with investments by LAWSON, Mitsubishi Corporation and several banks to run ATM-operations for LAWSON stores. The company began installing ATMs and started ATM services at some LAWSON stores from October 2001. The company's ATM business installs jointly operated ATMs on a leased basis in LAWSON stores in regions where agreement has been reached with partner banks. It has formed alliances with the major city bank groups and regional banks; partner banks currently number 21.

The company's main source of revenue is ATM commissions from banks. Its main expenses are operating center outsourcing fees, ATM line charges and ATM leasing charges.

As of February 28, 2007, the number of ATMs installed stood at 4,245 and the number of prefectures where ATMs are installed was 27. LAWSON held a 58.0% stake in this company as of February 28, 2007.

(Millions of Yen)

	2007	2006	2005	2004	2003
Operating revenues	**¥11,907**	¥11,311	¥10,003	¥8,352	¥6,718
Operating income (loss)	**866**	654	144	(348)	(529)
Net income (loss)	**509**	675	266	(350)	(529)

Number of ATMs Installed

	2007	2006	2005	2004	2003
Number of ATMs Installed	**4,245**	3,812	3,570	3,127	2,712

LAWSON CS Card, INC. (Equity-method affiliate)

This equity-method affiliate was established in February 2002 by Credit Saison Co., Ltd. (30% shareholding), Mitsubishi Corporation (20% shareholding), and LAWSON (50% shareholding). It issues the LAWSON PASS credit card, which is also used as a shopping point card by LAWSON customers and provides services through Loppi multimedia terminals and other channels. As of February 28, 2007, LAWSON PASS, for which services began in August 2002, had a cardholder base exceeding 2.7 million members. The company has been profitable since the fiscal year ended February 28, 2006, in line with growth in the cardholder base.

Credit Saison undertakes card issuance and credit screening for LAWSON PASS on behalf of LAWSON CS Card.

The company's main revenues come from commissions from the use of shopping and cash advance services, while the main expenses are outsourcing expenses related to operation of the card.

(Millions of Yen)

	2007	2006	2005	2004	2003
Operating revenues	**¥8,250**	¥7,157	¥ 4,261	¥ 2,551	¥ 858
Operating income (loss)	**189**	270	(1,230)	(2,255)	(3,935)
Net income (loss)	**200**	568	(1,218)	(2,256)	(3,936)

Other Services

LAWSON TICKET INC. (Consolidated Subsidiary)

This consolidated subsidiary sells tickets to concerts, movies, sporting events and other attractions, primarily through Loppi multimedia terminals at LAWSON stores. It was established as a ticket sales company in 1992 and became a subsidiary of LAWSON in 1997. In October 2004, LAWSON TICKET listed on the JASDAQ market (stock code: 2416).

In January 2004, LAWSON TICKET formed a business alliance with Rakuten, Inc., accepting capital participation from the latter. However, with the agreement of both companies, the business alliance was terminated in March 2007 because Rakuten Group website "Rakuten Auction" had included tickets to events as an auction item.

LAWSON TICKET ranks second in sales in the ticket sales industry behind PIA Corp. and is particularly strong in sales of tickets for J-POP (Japanese popular music generally popular among the relatively younger generation), sporting events and theater. In fiscal 2006, LAWSON TICKET posted record earnings, with operating income growing 1.8% year on year.

LAWSON used the opportunity presented by the termination of the business alliance between LAWSON TICKET and Rakuten to increase its equity interest in LAWSON TICKET. Between May and June 2007, LAWSON conducted a tender offer for the shares of LAWSON TICKET to acquire Rakuten's shares in the company with the view to strengthening the LAWSON Group's entertainment business. As a result of this tender offer, LAWSON raised its shareholding in LAWSON TICKET from 50.8% to 75.1%.

(Millions of Yen)

	2007	2006	2005	2004	2003
Operating revenues	¥6,533	¥6,259	¥6,288	¥6,218	¥5,425
Operating income	836	821	719	644	788
Net income	507	487	412	387	387

i-Convenience, Inc. (Consolidated Subsidiary)

This consolidated subsidiary was established in October 2000 with the aim of expanding business in the e-commerce sector, based on joint investment by LAWSON (51% shareholding), Mitsubishi Corporation (18%), Matsushita Electric Industrial Co., Ltd. (18%), and NTT DoCoMo, Inc. (13%). It operates the official "LAWSON Mobile" Internet site for mobile phones, and in addition to online merchandise sales and provision of related services and information, it manages the LAWSON website. During the fiscal year ended February 28, 2007, Mitsubishi Corporation purchased the shareholdings of Matsushita Electric Industrial and NTT DoCoMo, bringing its stake in i-Convenience to 49%.

(Millions of Yen)

	2007	2006	2005	2004	2003
Operating revenues	¥686	¥ 427	¥ 308	¥ 333	¥ 213
Operating income (loss)	46	(64)	(114)	(241)	(383)
Net income (loss)	43	(137)	(155)	(663)	(489)

BestPractice Inc. (Consolidated Subsidiary)

This company was established in March 2004 as a wholly owned subsidiary. BestPractice implements "Mystery Shopper" on-site inspections of convenience stores to determine the status of operations and offers advice and proposals to improve LAWSON stores at the operational level. Through this program, an undercover researcher who is an employee of BestPractice and has a thorough knowledge of convenience store operations and merchandise assortments, objectively and quantitatively evaluates LAWSON stores from a customer's perspective. The results are fed back to LAWSON's Head Office and franchise owners.

(Millions of Yen)

	2007	2006	2005	2004	2003
Operating revenues	¥885	¥892	¥628	–	–
Operating income (loss)	82	62	(2)	–	–
Net income (loss)	45	34	(2)	–	–

Overseas Business

SHANGHAI HUALIAN LAWSON CO., LTD. (Equity-method Affiliate)

This company has been developing a chain of LAWSON stores in Shanghai, the People's Republic of China, since July 1996. In May 2004, LAWSON relinquished 21.0% of its 70.0% equity interest in the company to partner Hualian Group Corporation, leaving LAWSON with a stake of 49.0% (current), to foster expansion through operation by local partners. At the end of December 2006, there were 291 stores in operation, of which 216 were franchised stores.

(Millions of Yen)

	2006	2005	2004	2003	2002
Operating income (loss)	¥ 20	¥ (7)	¥ (13)	¥ (81)	¥(191)
Net income (loss)	8	3	0	(71)	(190)
No. of stores	291	283	210	146	96

**SHANGHAI HUALIAN LAWSON CO., LTD. closes its accounts in December. It also changed from a consolidated subsidiary to an equity-method affiliate in fiscal 2004.*

Restaurant Business

naturalBeat Co., Ltd. (Equity-method affiliate)

This company was established in March 2004 by the Lotte Group and other companies. It is developing a chain of stores that provide so-called slow food based on a concept also of quickly serving customers. These include sandwiches, salads and other foods that are individually and carefully handmade from ingredients with an emphasis on natural taste and without using artificial additives where possible. naturalBeat had a chain of 10 stores as of March 31, 2007. LAWSON has had business relations with naturalBeat, such as selling its products in NATURAL LAWSON stores. However, with the view to leveraging each other's corporate brands, customer bases and expertise more in the future, LAWSON formed an equity-based business alliance with naturalBeat in February 2007. LAWSON paid approximately ¥0.35 billion to acquire a 33.4% equity interest in naturalBeat.

■ Overview of Earnings Figures

Consolidated Total Net Sales

Aggregate net sales of LAWSON stores in fiscal 2006, ended February 28, 2007, rose 1.8% to ¥1,386,630 million. In the first half of fiscal 2006, the September 2005 termination of Highway Card sales pushed down sales growth by about 1 percentage point. In addition, unseasonable weather conditions with few fine days and a delayed end to the rainy season, hurt sales. While a recovery was evident from August 2006 as weather conditions finally improved to seasonal levels and due to the success of a Miffy-themed shopping point campaign, this failed to compensate for sluggish customer numbers through July 2006. The recovery trend continued in the second half of the fiscal year, backed by the success of a second Miffy campaign run in November and an on-the-spot prize campaign in February 2007*. However, we did not achieve the sales we expected, as we were unable to overcome the effects of structural factors in the CVS industry.

Please refer to page 30 for details of sales by product category.

**A campaign where lucky customers were given vouchers that they could exchange for products free of charge. We ran the campaign twice during fiscal 2006, in June 2006 and February 2007.*

Existing Store Sales

Existing store sales in fiscal 2006 fell for the ninth consecutive year, marking a steady downward trend since fiscal 1998. While there was a recovery in consumer sentiment in Japan as a whole, the lack of a firm economic recovery in regions outside the main metropolitan areas of Tokyo, Osaka and Nagoya, had a slight impact on a company like LAWSON with a nationwide chain. Existing store sales struggled for the following reasons. One was the ongoing effect of competition with peer companies due to the opening of large numbers of conventional convenience stores. Another factor was that we are still in the process of creating new store formats and sales areas matched to local customers based on store charts due to a slow response to demographic changes in terms of products and store formats. Furthermore, sales were depressed by about 0.5% on an annual basis by the termination of Highway Card sales.

(%)

	2007	2006	2005	2004	2003
Existing store sales (year on year)	**98.2**	97.5	99.7	97.5	98.1
No. of customers and amount spent per customer (year on year)					
No. of customers	**98.2**	99.1	100.1	99.0	98.2
Amount spent per customer	**100.0**	98.3	99.7	100.2	99.9

Income and Expenses (Consolidated)

Total Operating Revenues

Total operating revenues comprise net sales from Company-operated stores, franchise commission from franchised stores, and other operating revenues.

Total operating revenues increased ¥14,995 million, or 5.6%, to ¥283,053 million. This result mainly reflected higher franchise commission from franchised stores, arising from a 198 net increase in the number of stores; higher sales due to an increase in the number of Company-operated NATURAL LAWSON and LAWSON STORE100 stores; and higher ATM fee income at consolidated subsidiary LAWSON ATM Networks. Additionally, the rate of total operating revenue growth was higher than total net sales growth. This was because franchise commission from franchised stores has risen at a faster pace than growth in the number of stores, as the weighting of Company-operated stores, except new formats, has declined every year and the share of C-type stores (prepared by LAWSON), which pay a high rate of franchise commissions, has become approximately 90%.

Selling, General and Administrative Expenses (SG&A) Expenses

SG&A expenses rose ¥7,274 million, or 4.1%, to ¥183,168 million. This increase was mainly attributable to a ¥4,082 million, or 8.0%, rise in store rents associated with an increase in the opening of mainly C-type franchised stores, and a ¥2,438 million, or 6.9%, increase in personnel expenses stemming from an increase in full-time and temporary employees associated with more store openings by NATURAL LAWSON, Inc. and VALUE LAWSON, Inc. However, taking into consideration the effect of a change in the classification of expenses for temporary employees, the increase was effectively only 4.7%. Advertising and promotion expenses increased ¥516 million, or 5.6%, as LAWSON conducted aggressive sales initiatives, including the Miffy-themed campaigns.

Breakdown of Main SG&A Expenses

(Millions of Yen)

	2007	2006	2005	2004	2003
Personnel expenses*	**¥ 37,888**	¥ 35,450	¥ 34,114	¥ 33,803	¥ 36,885
Advertising and promotional expenses	**9,693**	9,177	9,704	11,188	12,505
Store rents	**55,318**	51,236	46,785	42,679	40,035
Equipment leasing charges	**17,475**	16,734	16,263	15,726	14,316
Depreciation expenses	**16,185**	15,859	15,059	18,499	16,071
Amortization expenses	**5,163**	5,034	4,574	4,287	2,936
Other	**41,446**	42,402	38,136	31,274	33,590
Total	**¥183,169**	¥175,894	¥164,635	¥157,456	¥156,338

**Effective from the fiscal year ended February 28, 2007, expenses for temporary employees have been included in "Personnel expenses," whereas they were previously recorded under "Other." Expenses for temporary employees included in "Personnel expenses" in fiscal 2006 were ¥1,375 million, while expenses for temporary employees included in "Other" in fiscal 2005 were ¥750 million.*

Composition of SG&A Expenses

(%)

	2007	2006	2005	2004	2003
Personnel expenses	**20.7%**	20.2%	20.7%	21.5%	23.6%
Advertising and promotional expenses	**5.3**	5.2	5.9	7.1	8.0
Store rents	**30.2**	29.1	28.4	27.1	25.6
Equipment leasing charges	**9.5**	9.5	9.9	10.0	9.2
Depreciation expenses	**8.8**	9.0	9.1	11.7	10.3
Amortization expenses	**2.8**	2.9	2.8	2.7	1.9
Other	**22.6**	24.1	23.2	19.9	21.4
Total	**100.0%**	100.0%	100.0%	100.0%	100.0%

Operating Income

Operating income rose ¥646 million, or 1.5%, to ¥44,513 million. Existing store growth and franchise commission from franchised stores, which accounts for the majority of total operating revenues, were below target, meaning that total operating revenues fell short of target. SG&A expenses were held slightly below target due to curbs on IT-related costs and sales promotion costs, but this wasn't enough to make up for the lower-than-planned sales. As a result, operating income was about ¥787 million under target.

Income Before Income Taxes and Minority Interests

Income before income taxes and minority interests declined ¥1,875 million, or 4.8%, to ¥36,848 million. One reason for this decline was a ¥183 million decrease in equity in gains of associated companies, the result of a year-on-year decline in earnings at equity-method affiliate LAWSON CS Card, Inc. owing to higher issuance expenses in line with cardholder growth of LAWSON PASS and higher bad debt expenses associated with moves to eliminate "grey-zone" interest rates in Japan. Another reason was a loss of ¥2,202 million on the changeover to a next-generation IT system.

Net Income

Net income was ¥20,983 million, a decrease of ¥1,042 million, or 4.7%. Net income per share decreased 6.5% to ¥201.50.

■ Financial Position (Consolidated)

Current Assets

Total current assets increased ¥19,180 million, or 14.8%, to ¥149,022 million. This mainly reflected a ¥15,106 million increase in cash and cash equivalents due to the sale of treasury stock to NTT DoCoMo in March 2006.

Property and Store Equipment, Investments and Other Assets

Net property and store equipment rose ¥4,983 million, or 5.0%, year on year to ¥104,255 million, the result of a rise of ¥14,310 million in buildings, owing to an increase in the opening of C-type stores prepared by LAWSON among newly opened franchise stores.

Intangible fixed assets declined ¥1,382 million, or 8.0%, to ¥15,890 million. Investments and other assets decreased ¥1,012 million, or 0.7%, to ¥144,981 million. While there was an increase in long-term loans receivable, mainly to help with construction, lease deposits declined ¥2,024 million and software declined ¥1,021 million due to the start of amortization.

Current Liabilities

Total current liabilities increased ¥2,273 million, or 1.6%, to ¥143,514 million. While income taxes payable declined, there was a ¥4,140 million increase in money held as agent such as in bill settlement services.

Long-term Liabilities

Total long-term liabilities increased ¥392 million, or 0.7%, to ¥55,251 million. There was a ¥710 million increase in liability for employees' retirement benefits. On the other hand, guarantee deposits received from franchised stores declined ¥2,015 million due to a decrease in the number of franchised stores operating under franchise agreements requiring the payment of a guarantee deposit.

Total Equity

In accordance with enforcement of the Corporate Law in May 2006, shareholders' equity as presented in the past is now shown as a component of equity, along with minority interests and stock acquisition rights. Total equity, including minority interests, amounted to ¥199,493 million at the end of February 2007. Retained earnings were ¥95,344 million, reflecting net income of ¥20,983 million and cash dividends paid of ¥9,822 million. The equity ratio increased 2.3 points to 49.0%.

■ Special Account Items on the Balance Sheet

The following items are special features of LAWSON's financial statements.

Due From Franchised Stores

LAWSON makes bulk purchases of products ordered by all franchised stores and calculates and pays amounts payable for such to the vendors on the stores' behalf. LAWSON records the cost of the merchandise in the "Accounts receivable—Due from franchised stores" account since such costs are recovered from franchised stores. "Due from franchised stores" represents mainly the obligations of franchised stores to Head Office for these amounts at the balance sheet date. As of February 28, 2007, this asset account was ¥11,710 million, ¥948 million higher than a year ago. There was thus no substantial change in this account.

Accounts Receivable—Other

Other accounts receivable such as income due from vendors is included in "Other" in "Accounts receivable" on the balance sheet. The constituent elements of this item stood at ¥26,002 million at February 28, 2007, an increase of ¥4,424 million.

Long-Term Loans Receivable

This account mainly represents money paid to landlords (owners of land and buildings for stores) to help with construction and investments and finance from Head Office to franchised stores. As of February 28, 2007, this account was ¥3,749 million higher than a year ago at ¥24,380 million, due to an increase in money paid to landlords to help with construction for store openings.

Lease Deposits

This account represents leasehold deposits paid to landlords equivalent to several months' rent under lease agreements at LAWSON. As of February 28, 2007, this account was ¥87,904 million, a decrease of ¥2,024 million.

Due to Franchised Stores

This account represents Head Office obligations to franchised stores. All franchised stores make remittances of cash proceeds from daily sales to the Head Office. If franchised store remittances of cash proceeds from daily sales to the Company exceed the balance of "Accounts receivable—Due from franchised stores," the excess will be shown on the balance sheet as "Accounts payable—Due to franchised stores." As of February 28, 2007, this account was ¥2,757 million, down ¥660 million from a year ago.

Money Held as Agent

This account mainly comprises money held on behalf of third-party companies for which LAWSON provides bill settlement services, including public utility charges. There was an increase in money held as agent due to a rise in the number of transactions and the number of companies for which settlement services were provided. As a reflection of this, the balance of payments to third-party companies increased, leading to a rise of ¥4,140 million to ¥48,755 million in this account at February 28, 2007.

Guarantee Deposits Received From Franchised Stores

This represents guarantee deposits received by LAWSON from store owners operating under FC-G-type contracts. As of February 28, 2007, this account was ¥48,451 million, ¥2,015 million less than a year ago due to a decline in the number of FC-G-type contract stores.

■ Capital Expenditure

In fiscal 2006, capital expenditure totaled ¥49,822 million, a decrease of ¥4,595 million. Investments in new stores declined ¥2,603 million to ¥23,444 million due to constraints on store openings compared to the previous fiscal year and an increase in cash proceeds such as from the recovery of key money accompanying the closure of stores that were leased. Systems-related investments decreased ¥4,422 million to ¥4,662 million due to a decrease in IT investments for management accounting systems recorded in the previous year. Leases increased ¥4,382 million to ¥14,211 million as LAWSON made greater use of lease contracts for sign boards and other improvements. A breakdown of capital expenditure is as follows:

Capital Expenditure (Millions of Yen)

	2007	2006	2005	2004	2003
New store investments	**¥23,444**	¥26,047	¥21,695	¥19,614	¥14,663
Existing store investments	**5,887**	6,592	8,175	10,432	12,028
Systems-related investments	**4,662**	9,084	2,765	2,191	9,133
Other	**(1,395)**	1,615	4,186	377	1,149
Investments and advances	**3,013**	1,250	(1,000)	6,250	3,550
Leases*	**14,211**	9,829	11,052	9,439	35,305
Total	**¥49,822**	¥54,417	¥46,873	¥48,303	¥75,828

**The amount equivalent to the acquisition cost of leased property acquired during each fiscal year.*

■ Cash Flows

Operating activities provided net cash of ¥47,596 million, ¥664 million more than in the previous fiscal year. While there was a decline in income before income taxes and minority interests from the previous fiscal year, this result was attributable mainly to increases in other accounts payable and accounts payable, the add back of a loss on replacement of computer system and a decrease in income taxes paid.

Investing activities used net cash of ¥31,754 million, ¥23,528 million less than in the previous fiscal year. In addition to a decrease in payments for the purchase of intangible fixed assets such as systems, the increase in cash from the redemption of marketable securities outweighed the increase in cash for the purchase of marketable securities (maturity date of more than three months) for the purpose of short-term funds investment.

As a result of changes in cash flows from operating and investing activities, free cash flow—the difference between the two figures—increased ¥24,192 million year on year to ¥15,842 million.

Financing activities used net cash of ¥736 million, ¥7,058 million less than one year earlier. This reflected ¥9,021 million in proceeds from sales of treasury stock, although ¥1,635 million more was used for the payment of cash dividends.

As a result, cash and cash equivalents at the end of the fiscal year totaled ¥75,547 million, ¥15,107 million higher than a year earlier.

■ Capital Policy: Dividends and Purchase of Treasury Stock

LAWSON regards returning profits to shareholders as one of its most important management policies and properly acknowledges that the level of capital cost reflects the profit expectations of investors toward the Company. To select and develop businesses that achieve earnings above the cost of capital, LAWSON uses capital efficiency, such as ROE, as its most important management indicator. Accordingly, we pursue optimal capital efficiency by looking at the appropriate balance between the distribution of profits through dividends and the purchase and cancellation of treasury stock to maintain high profitability and secure our financial soundness, by securing the necessary level of internal reserves for investment aimed at achieving sustained corporate growth over the medium and long terms.

In the past, during the four-year period from fiscal 2001 to fiscal 2004, LAWSON cancelled approximately ¥43.0 billion of treasury stock. As regards cash dividends, in fiscal 2004, we increased the annual cash dividend per share by ¥29 to ¥70, and in fiscal 2005 we raised it by ¥20 to ¥90. In fiscal 2006, the dividend was increased by a further ¥10 to ¥100 per share, as we actively returned profits to shareholders. In fiscal 2007, we plan to raise the dividend by another ¥10 to ¥110 per share. We are aiming for a dividend payout ratio of around 40%, a level which takes into account the global standard, as we continue to strive to return profits to shareholders.

■ Business Cooperation and Alliances

The main business cooperation and alliances are as follows.

Mitsubishi Corporation

LAWSON formed a comprehensive tie-up, including a capital alliance, with Mitsubishi Corporation in February 2000. Mitsubishi Corporation is LAWSON's leading shareholder with an equity interest of 30.7%. The two firms have built a cooperative relationship in the areas of personnel resources, store development, new businesses, product development and other areas.

NTT DoCoMo, Inc.

In March 2006, LAWSON signed a business alliance agreement, including a capital alliance, with NTT DoCoMo, Inc. The main elements of the alliance are as follows.

Capital Alliance

In March 2006, LAWSON sold treasury stock of 2,092,000 common stock, representing 2.0% of total issued shares, to NTT DoCoMo for about ¥9.0 billion.

Business Alliance

(1) The introduction of settlement services based on *iD™** at all LAWSON stores

**iD™ is a mobile phone-based credit card payment service enabling shopping, etc., via NTT DoCoMo's* Osaifu-Keitai® *wallet services.*

(2) Information services utilizing *ToruCa®** at all LAWSON stores

**ToruCa® is a system for capturing information such as coupons just by holding NTT DoCoMo's* Osaifu-Keitai® *mobile phones over reader/writers at stores.*

(3) Going forward, the two companies will hold regular meetings to continue discussions regarding future fields of collaboration.

**ID™, ToruCa® and Osaifu-Keitai® are trademarks or registered trademarks of NTT DoCoMo.*

naturalBeat Co., Ltd.

LAWSON formed an equity-based business alliance with naturalBeat Co., Ltd. in February 2007. Please refer to page 36 for an overview of this company. The details of the alliance are as follows.

(1) Develop products for NATURAL LAWSON stores utilizing naturalBeat's expertise in making sandwiches, soups, gelato, muffins and other foods that emphasize the natural taste of the ingredients.
(2) Provide more attractive freshly baked bread products inside NATURAL LAWSON stores by using the products and technical expertise of Wholesome Co., Ltd., a naturalBeat subsidiary that offers bakery items based on the concept of providing healthy food.
(3) Expand sales of naturalBeat original products such as Rooibos tea in NATURAL LAWSON stores.
(4) Develop collaborative stores that tap the strengths of both NATURAL LAWSON and naturalBeat.

Ninety-nine Plus Inc.

In February 2007, LAWSON announced an equity-based alliance with Ninety-nine Plus Inc., which operates the "SHOP99" chain of convenience stores known for their fresh foods. Ninety-nine Plus was established in October 2000 and since then has grown rapidly as a pioneer in Japan of a new perishable foods store format that provides everything from daily food items, including perishable foods, to sundry goods at a single price—it created the concept of an everyday low price of 99 yen (excluding tax). As of March 31, 2007, the company had a network of 780 stores. SHOP99 stores have won strong acceptance from housewives and older shoppers for a strategy of strengthening the merchandise assortment of perishable and daily delivered foods at stores in residential areas. This is highlighted by a higher weighting of housewives and seniors in its customer mix than at conventional convenience stores.

Through this alliance with Ninety-nine Plus, LAWSON believes that it can improve the quality of perishable and daily delivered foods sold in suitably sized small portions, by complementing each other's know-how and strengths, including in the area of perishable foods. By doing so, LAWSON believes that it can broaden its customer base of housewives and seniors and attract more customers. Based on the agreement between the two companies, Ninety-nine Plus allotted 31,500 shares of common stock to LAWSON in March 2007 through an increase in capital by way of a private placement of shares. LAWSON held 20% of all Ninety-nine Plus shares with voting rights following the increase in capital via private placement.

Details of the alliance are as follows.

(1) Jointly develop and purchase products
  a) Between LAWSON STORE100 and SHOP99
  b) Extend to LAWSON PLUS and other stores

(2) Rationalize distribution
Leverage LAWSON's distribution infrastructure and know-how to rationalize distribution at Ninety-nine Plus.

(3) Full-scale franchising
Ninety-nine Plus will leverage LAWSON's franchise-related know-how and systems to begin franchise development trials at SHOP99 stores. Existing LAWSON franchise owners will be given first option to take up franchise agreements.

(4) Strengthen perishable foods lineups
Utilize SHOP99's knowledge of perishable and daily delivered foods and jointly developed private brand products, including frozen foods, in LAWSON PLUS and LAWSON STORE100 stores.

(5) Cooperation in opening stores
To open stores that are expected to be highly profitable for both companies by avoiding unnecessary competition, the two companies will provide each other with advance information on store openings and at the same time do their best to avoid opening stores in the vicinity of existing stores.

(6) Integration of LAWSON STORE100 and SHOP99
Consider the integration of stores in the future.

(7) Formation of a Business Alliance Promotion Committee
Establish a Business Alliance Promotion Committee made up of the presidents of both companies, heads of product departments and their subordinates.

■ Outlook

Although the Japanese economy appears to be recovering moderately, competition transcending the boundaries of the retail industry is becoming increasingly fierce, and customer needs are becoming increasingly diverse.

With regard to the CVS sector, if LAWSON focuses only on opening a large number of conventional format stores, which predominantly provide merchandise assortments and services for the core target of young male customers, pursuing only the need to save time and convenience, it will be forced into a war of attrition with other homogenized CVS stores in a mature market. As a consequence it would risk a drop in existing store sales undermining the motivation of existing franchised store owners. The CVS business is underpinned by the motivation of franchised store owners. But if the future expectations of franchised store owners don't improve, it will be increasingly difficult for a company operating in the industry to achieve stable, sustained growth.

To achieve stable, sustained growth over the medium to long term in such a changing operating environment, we believe LAWSON needs to become a more advanced company by pursuing innovation in all kinds of areas, without being bound by conventional ideas about the CVS sector. Based on this rationale, we initiated the medium-term management plan LAWSON Challenge 2007 in fiscal 2005. We have implemented management initiatives based on this plan, which ends in fiscal 2007.

In qualitative terms, we have derived considerable benefits from developing new format stores such as NATURAL LAWSON and LAWSON STORE100, which have attracted customers beyond the reach of the conventional format, and LAWSON PLUS, which leverages the know-how garnered from the two new formats. In quantitative terms, however, as a result of excessive competition created by major rival chains opening conventional stores, we failed to achieve our medium-term management targets for growth in existing store sales for two fiscal years, fiscal 2005 and fiscal 2006. Moreover, start-up and sales promotion costs for launching the new formats to break the conventional convenience store mold were higher than expected. For these and other reasons, we expect it to be difficult to achieve the LAWSON Challenge 2007 final-year management targets in fiscal 2007 of an average growth in EPS of 10% over the 3 years of the plan, and ROE of 15%.

Curbing costs for new projects, advertising, education and training in a bid to achieve these targets could compromise our growth prospects and have a negative effect on our ability to sustain growth from fiscal 2008 onwards. For these reasons, we decided to lower our targets for fiscal 2007—to average growth in EPS of 2.3% over the 3 years of the plan, and ROE of 11.1%—and make the necessary upfront investments aimed at sustained growth over the medium and long term.

Looking ahead, the LAWSON Group's single biggest theme is to vitalize existing stores. To this end, we will implement the following initiatives.

Increase customers by expanding our customer base

We will move into full gear in converting LAWSON stores to the LAWSON PLUS format, which targets more senior and women customers, based on merchandise assortments and store displays matched to the needs of local customers. At conventional LAWSON stores, we will use "store charts" to develop more attractive merchandise assortments better suited to the needs of each region. This will entail providing more perishable foods and daily delivered foods. Moreover, in a bid to reduce lost sales opportunities, we will provide merchandise popular with customers based on improved order precision from data collection and analysis.

Regarding sales promotion, we will continue to develop loyal customers by making effective use of LAWSON PASS and MY LAWSON POINT. In tandem with this, we will promote shopping point programs, which are popular with women, as we look to expand our customer base.

We are determined to convert the expected increase in customer numbers through these initiatives into higher earnings. In turn, this should also lead to a rise in franchised store owner satisfaction and motivation.

Improve asset efficiency by opening high-quality new stores and curbing store closures

The Group aims to improve asset efficiency as a whole by developing high-quality stores in accordance with proprietary store opening guidelines and reducing extraordinary losses from store closures by reducing store closures.

In particular, through the aforementioned measures to strengthen existing stores, we will enhance the motivation of franchised store owners, convert stores to the LAWSON PLUS format and actively propose initiatives designed to restore the sales capabilities of franchised owners. In this way, we aim to reduce store closures.

Strengthen the management base through personnel development, next-generation IT systems and internal controls

In accordance with our management policy and action guidelines, we are determined to nurture people who can think for themselves and not rely on direction from the top. In addition, we will enhance the regional headquarters management system consisting of seven headquarters nationwide, to promote detailed management suited to regional characteristics. Such management is necessary to foster management by individual stores.

LAWSON is making preparations for the scheduled full-scale introduction in fiscal 2008 of a next-generation IT system. The backbone for this new system will be an optical fiber network. The concept of the new system is to create a total company information system, one encompassing store-related systems such as POS, store computers and store operational equipment as well as systems for product development, store development, financial accounting and integration master code systems (which manage products, business partners and other operational aspects). The new system is expected to yield benefits in terms of reductions in lost operational time, improved ordering precision and an enhanced management infrastructure.

Where internal control is concerned, based on our "Basic Policy for Maintaining Internal Control Systems," we will enhance our system and ready ourselves for compliance with the Financial Instruments and Exchange Law.

We believe that steady implementation of these and other management initiatives will enhance customer satisfaction, and ultimately lead to improved corporate earnings from an expanded customer base as well as higher profits for franchised owners and greater corporate value.

For fiscal 2007, we are forecasting consolidated operating income of ¥45.9 billion, up 3.1% year on year, and net income of ¥22.2 billion, up 5.8% year on year.

■ Business Risk Factors

The eight main risks that may impact on LAWSON's performance and financial position are described below. Sufficiently aware that these risks may occur, LAWSON conducts risk management and is also building and reinforcing an internal control system so as to respond in the best manner possible should a risk materialize. Nevertheless, these risks are only within the range of what can be forecast based on information currently available to the Company, and we do not believe that they cover all potential risks relating to LAWSON's business operations.

Risks relating to changes in the business environment

Because LAWSON's main business is the operation of convenience stores, changes in consumer expenditure produced by changes in the economic environment, business cycle trends, or the social structure in Japan and overseas countries where the Company operates, as well as changes in competition with other companies in the CVS sector or different retail sectors, may impact LAWSON's earnings and financial condition.

Risks relating to food safety and hygiene management

In the CVS business, LAWSON's main business, the Company sells food products to customers. From the manufacturing process to sales in stores, in cooperation with suppliers, LAWSON strictly observes quality standards by performing thorough management and also performs rigorous hygiene management within stores. However, loss of customer trust in the event of a serious incident such as food poisoning or contamination by foreign matter could have an impact on the Company's performance and financial position. Should such an incident occur, the Company intends to make the utmost effort to minimize the effect on customers by making a public announcement as quickly as possible through the mass media and other channels.

Risks relating to handling of personal information

In the process of business operations, LAWSON handles personal information of customers, shareholders, suppliers, franchise owners and other parties. The Company recognizes that the leakage of personal information or improper access to personal information are serious risks. Consequently, we have devised the best possible information security measures and formulated a policy to protect personal information. We have also ensured that personnel within the Company are thoroughly aware of these matters. However, should personal information be leaked or divulged outside the Company under whatever circumstances, LAWSON's performance or financial position may be affected.

Legal and regulatory risks

LAWSON operates numerous stores in various regions throughout Japan and overseas, and the majority of stores operate 24 hours a day. Because of this, in operating its business, the Company must comply with various laws and regulations regarding store development, operating hours, hygiene management, product transactions, environmental protection, and other matters in Japan and overseas, and must obtain various permits and licenses. Therefore, should events arise such as an unforeseen change in laws or regulations or a change in the enforcement methods of administrative authorities, new compliance costs could arise, which could have an impact on LAWSON's performance or financial position.

Risks relating to franchise operations

In the CVS business, LAWSON's main business, the Company has adopted the franchise system. Based on franchise agreements concluded with franchised stores, LAWSON operates a chain of stores via store brand names that are owned by LAWSON. Therefore, if the brand image of the overall chain is affected by illegal or improper actions at a franchised store, there may be an impact on LAWSON's performance or financial position.

Furthermore, the franchise system is designed to encourage improved business performance for both franchised stores and the Company, based on a relationship of mutual trust. If this relationship of trust between LAWSON and franchised stores is damaged for any reason, and, as a consequence, many franchise agreements are cancelled, there may be an impact on LAWSON's performance or financial position.

Risks relating to unseasonable weather or disasters

Substantial differences in climate and temperatures from the average year could have an impact on LAWSON's performance. Moreover, LAWSON is a national chain with stores located throughout Japan's 47 prefectures, as well as in Shanghai, China. Therefore, an earthquake could physically damage LAWSON stores or other facilities, hampering business operations. In addition, there is a risk that performance will fluctuate due to natural disasters in regions where snowfalls are heavy or typhoons often occur.

Risks involving damage to IT systems

There is a risk that operation of the Group's IT systems might be impeded by a computer virus, or affected by natural disasters such as an earthquake, which could cause interference to the distribution network, creating delays in the delivery of products to stores. Such developments could impact on LAWSON's performance or financial position.

Risks involving soaring materials prices

LAWSON's performance or financial position could be materially affected by further increases in raw materials prices due to unpredictable developments, such as rising oil and other raw materials prices, bird flu, and unusual weather.

Consolidated Balance Sheets

LAWSON, INC. and Subsidiaries
February 28, 2007 and 2006

ASSETS	Millions of Yen 2007	Millions of Yen 2006	Thousands of U.S. Dollars (Note 1) 2007
CURRENT ASSETS:			
Cash and cash equivalents	**¥ 75,547**	¥ 60,441	**$ 637,850**
Marketable securities (Note 5)	**14,996**	19,652	**126,613**
Accounts receivable:			
Due from franchised stores (Notes 3 and 10)	**11,710**	10,762	**98,869**
Other	**26,002**	21,578	**219,537**
Allowance for doubtful accounts	**(115)**	(81)	**(971)**
Inventories	**1,789**	1,573	**15,105**
Short-term loan to associated company (Note 17)	**8,850**	6,250	**74,721**
Deferred tax assets (Note 14)	**2,795**	3,189	**23,598**
Prepaid expenses and other current assets	**7,448**	6,478	**62,885**
Total current assets	**149,022**	129,842	**1,258,207**
PROPERTY AND STORE EQUIPMENT (Notes 4 and 6)**:**			
Land (Note 7)	**4,709**	5,237	**39,759**
Buildings	**144,418**	130,108	**1,219,334**
Furniture, fixtures and equipment	**58,978**	60,410	**497,957**
Total	**208,105**	195,755	**1,757,050**
Accumulated depreciation	**(103,850)**	(96,483)	**(876,815)**
Net property and store equipment	**104,255**	99,272	**880,235**
INVESTMENTS AND OTHER ASSETS:			
Investment securities (Note 5)	**1,560**	1,962	**13,171**
Investments in associated companies	**1,553**	1,087	**13,112**
Long-term loans receivable	**24,380**	20,631	**205,843**
Lease deposits (Note 8)	**87,904**	89,928	**742,182**
Deferred tax assets (Note 14)	**11,551**	11,046	**97,526**
Deferred tax assets for land revaluation (Note 7)	**468**	3,331	**3,951**
Software	**14,786**	15,807	**124,840**
Other assets	**6,797**	6,663	**57,387**
Allowance for doubtful accounts	**(4,018)**	(4,462)	**(33,924)**
Total investments and other assets	**144,981**	145,993	**1,224,088**
TOTAL	**¥ 398,258**	¥375,107	**$3,362,530**

See notes to consolidated financial statements.

LIABILITIES AND EQUITY	Millions of Yen 2007	Millions of Yen 2006	Thousands of U.S. Dollars (Note 1) 2007
CURRENT LIABILITIES:			
Accounts payable:			
Trade (Notes 9 and 17)	**¥ 65,000**	¥ 63,170	**$ 548,801**
Due to franchised stores (Note 10)	**2,757**	3,417	**23,278**
Other	**16,611**	14,344	**140,248**
Income taxes payable (Note 14)	**4,755**	10,324	**40,147**
Money held as agent	**48,755**	44,615	**411,643**
Accrued expenses and other current liabilities	**5,636**	5,371	**47,585**
Total current liabilities	**143,514**	141,241	**1,211,702**
LONG-TERM LIABILITIES:			
Liability for employees' retirement benefits (Note 11)	**3,527**	2,817	**29,779**
Allowance for retirement benefits to executive officers and corporate auditors	**249**	318	**2,102**
Guarantee deposits received from franchised stores	**48,451**	50,466	**409,076**
Lease deposits from lessees	**875**	870	**7,388**
Allowance for impairment loss on leased property (Note 16)	**95**	140	**802**
Other (Note 15)	**2,054**	248	**17,342**
Total long-term liabilities	**55,251**	54,859	**466,489**
MINORITY INTERESTS		3,823	
CONTINGENT LIABILITIES (Note 18)			
EQUITY (Notes 12 and 20)**:**			
Common stock—authorized, 409,300,000 shares in 2007 and 2006; issued, 104,600,000 shares in 2007 and 2006	**58,507**	58,507	**493,980**
Capital surplus	**42,254**	41,520	**356,754**
Stock acquisition rights	**78**		**659**
Retained earnings	**95,344**	88,356	**804,998**
Land revaluation difference (Note 7)	**(682)**	(4,855)	**(5,758)**
Net unrealized gain on available-for-sale securities	**320**	696	**2,702**
Foreign currency translation adjustments	**135**	105	**1,140**
Treasury stock—at cost, 186,918 shares in 2007 and 2,313,932 shares in 2006	**(739)**	(9,145)	**(6,239)**
Total	**195,217**	175,184	**1,648,236**
Minority interests	**4,276**		**36,103**
Total equity	**199,493**	175,184	**1,684,339**
TOTAL	**¥398,258**	¥375,107	**$3,362,530**

Consolidated Statements of Income

LAWSON, INC. and Subsidiaries
Years Ended February 28, 2007 and 2006

	Millions of Yen		Thousands of U.S. Dollars (Note 1)
	2007	2006	2007
OPERATING REVENUES:			
Franchise commission from franchised stores	¥174,325	¥170,785	$1,471,842
Net sales from Company-operated stores	75,151	66,027	634,507
Other	33,577	31,246	283,494
Total	283,053	268,058	2,389,843
COST AND OPERATING EXPENSES:			
Cost of sales for Company-operated stores	55,371	48,297	467,503
Selling, general and administrative expenses (Notes 11 and 16)	183,169	175,894	1,546,513
Total	238,540	224,191	2,014,016
Operating income	44,513	43,867	375,827
OTHER INCOME (EXPENSES):			
Interest income—net	628	386	5,302
Equity in gains of associated companies	102	286	861
Gain on sales of investment securities	44	989	372
Gain on sales of property and store equipment	746	24	6,299
Reversal of allowance for doubtful accounts	311	263	2,626
Loss on disposal of property and store equipment	(4,638)	(3,014)	(39,159)
Impairment of long-lived assets (Note 6)	(1,811)	(2,708)	(15,290)
Loss on replacement of computer system (Note 15)	(2,202)		(18,592)
Other—net	(845)	(1,370)	(7,135)
Other expenses—net	(7,665)	(5,144)	(64,716)
INCOME BEFORE INCOME TAXES AND MINORITY INTERESTS	36,848	38,723	311,111
INCOME TAXES (Note 14)**:**			
Current	12,378	17,823	104,509
Deferred	3,011	(1,606)	25,422
Total	15,389	16,217	129,931
MINORITY INTERESTS IN NET INCOME	(476)	(481)	(4,019)
NET INCOME	¥ 20,983	¥ 22,025	$ 177,161

	Yen		U.S. Dollars
	2007	2006	2007
PER SHARE OF COMMON STOCK (Notes 2.q and 19)**:**			
Net income—basic	¥201.50	¥215.50	$1.70
Net income—diluted	201.40	215.46	1.70
Cash dividends	100.00	90.00	0.84

See notes to consolidated financial statements.

Consolidated Statements of Changes in Equity

LAWSON, INC. and Subsidiaries
Years Ended February 28, 2007 and 2006

Thousands of Shares/Millions of Yen

	Common Stock								Treasury Stock				
	Shares	Amount	Capital Surplus	Stock Acquisition Rights	Retained Earnings	Land Revaluation Difference	Net Unrealized Gain on Available-for-sale Securities	Foreign Currency Translation Adjustments	Shares	Amount	Total	Minority Interests	Total Equity
BALANCE, MARCH 1, 2005	104,600	¥58,507	¥41,523		¥76,721	¥(7,038)	¥ 110	¥ 34	(2,423)	¥(9,575)	¥160,282		¥160,282
Net income					22,025						22,025		22,025
Year end cash dividends, ¥35 per share					(3,576)						(3,576)		(3,576)
Interim cash dividends, ¥45 per share					(4,598)						(4,598)		(4,598)
Reversal of land revaluation difference					(2,183)	2,183							
Net increase in unrealized gain on available-for-sale securities							586				586		586
Net increase in foreign currency translation adjustments								71			71		71
Treasury stock—at cost:													
Purchase of treasury stock									(1)	(2)	(2)		(2)
Exercise of stock options			(3)		(33)				110	432	396		396
BALANCE, FEBRUARY 28, 2006	104,600	58,507	41,520		88,356	(4,855)	696	105	(2,314)	(9,145)	175,184		175,184
Reclassified balance as of February 28, 2006 (Note 2.l.)												¥3,823	3,823
Net income					20,983						20,983		20,983
Year end cash dividends, ¥45 per share					(4,603)						(4,603)		(4,603)
Interim cash dividends, ¥50 per share					(5,219)						(5,219)		(5,219)
Reversal of land revaluation difference					(4,173)						(4,173)		(4,173)
Treasury stock—at cost:													
Purchase of treasury stock									(1)	(1)	(1)		(1)
Sale of treasury stock			753						2,093	8,268	9,021		9,021
Exercise of stock options			(19)						35	139	120		120
Others—net				¥78		4,173	(376)	30			3,905	453	4,358
BALANCE, FEBRUARY 28, 2007	104,600	¥58,507	¥42,254	¥78	¥95,344	¥ (682)	¥ 320	¥135	(187)	¥ (739)	¥195,217	¥4,276	¥199,493

Thousands of U.S. Dollars (Note 1)

	Common Stock	Capital Surplus	Stock Acquisition Rights	Retained Earnings	Land Revaluation Difference	Net Unrealized Gain on Available-for-sale Securities	Foreign Currency Translation Adjustments	Treasury Stock	Total	Minority Interests	Total Equity
BALANCE, FEBRUARY 28, 2006	$493,980	$350,557		$745,998	$(40,991)	$5,876	$ 887	$(77,212)	$1,479,095		$1,479,095
Reclassified balance as of February 28, 2006 (Note 2.l.)										$32,278	32,278
Net income				177,161					177,161		177,161
Year end cash dividends, $0.38 per share				(38,864)					(38,864)		(38,864)
Interim cash dividends, $0.42 per share				(44,064)					(44,064)		(44,064)
Reversal of land revaluation difference				(35,233)					(35,233)		(35,233)
Treasury stock—at cost:											
Purchase of treasury stock								(8)	(8)		(8)
Sale of treasury stock		6,357						69,807	76,164		76,164
Exercise of stock options		(160)						1,174	1,014		1,014
Others—net			$659		35,233	(3,174)	253		32,971	3,825	36,796
BALANCE, FEBRUARY 28, 2007	$493,980	$356,754	$659	$804,998	$ (5,758)	$2,702	$1,140	$ (6,239)	$1,648,236	$36,103	$1,684,339

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

LAWSON, INC. and Subsidiaries
Years Ended February 28, 2007 and 2006

	Millions of Yen		Thousands of U.S. Dollars (Note 1)
	2007	2006	**2007**
OPERATING ACTIVITIES:			
Income before income taxes and minority interests	**¥ 36,848**	¥ 38,723	**$ 311,111**
Adjustments for:			
Income taxes paid	**(17,947)**	(19,217)	**(151,528)**
Depreciation and amortization	**21,352**	20,896	**180,277**
Impairment of long-lived assets	**1,811**	2,708	**15,290**
Loss on replacement of computer system	**2,202**		**18,592**
Provision for allowance for doubtful accounts	**(410)**	324	**(3,462)**
Loss on disposal of property and store equipment	**2,881**	1,846	**24,325**
Equity in gains of associated companies	**(102)**	(286)	**(861)**
Gain on sales of investment securities	**(44)**	(989)	**(372)**
Gain on sales of property and store equipment	**(746)**	(24)	**(6,299)**
Other—net	**1,262**	1,849	**10,656**
Changes in assets and liabilities:			
Increase in accounts receivable	**(5,345)**	(2,908)	**(45,128)**
Increase in prepaid expenses and other current assets	**(283)**	(588)	**(2,389)**
Increase in inventories	**(216)**	(197)	**(1,824)**
Increase in accounts payable	**3,438**	376	**29,027**
Increase in money held as agent	**4,140**	4,345	**34,954**
Increase in accrued expenses and other liabilities	**125**	52	**1,055**
Increase in allowance for retirement benefits to employees and executive officers and corporate auditors	**641**	1,022	**5,412**
Decrease in guarantee deposits received from franchised stores	**(2,016)**	(1,056)	**(17,021)**
Increase in lease deposits from lessees	**5**	57	**42**
Total adjustments	**10,748**	8,210	**90,746**
Net cash provided by operating activities	**47,596**	46,933	**401,857**
INVESTING ACTIVITIES:			
Purchases of marketable securities	**(57,193)**	(44,709)	**(482,886)**
Proceeds from redemption of marketable securities	**61,850**	33,076	**522,205**
Proceeds from sales of investment securities	**185**	1,705	**1,562**
Purchases of property and store equipment	**(28,760)**	(28,631)	**(242,823)**
Decrease in lease deposits	**2,024**	37	**17,089**
Increase in short-term loan	**(2,600)**	(1,250)	**(21,952)**
Increase in long-term loan	**(3,749)**	(3,821)	**(31,653)**
Other	**(3,511)**	(11,689)	**(29,644)**
Net cash used in investing activities	**(31,754)**	(55,282)	**(268,102)**
FINANCING ACTIVITIES:			
Cash dividends paid	**(9,822)**	(8,188)	**(82,928)**
Proceeds from sales of treasury stock	**9,021**		**76,165**
Proceeds from issuance of share upon exercise of stock option	**120**	395	**1,013**
Purchase of treasury stock	**(1)**	(2)	**(8)**
Cash dividends paid to minority shareholders	**(54)**		**(456)**
Net cash used in financing activities	**(736)**	(7,795)	**(6,214)**
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	**15,106**	(16,144)	**127,541**
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	**60,441**	76,585	**510,309**
CASH AND CASH EQUIVALENTS, END OF YEAR	**¥ 75,547**	¥ 60,441	**$ 637,850**

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

LAWSON, INC. and Subsidiaries
Years Ended February 28, 2007 and 2006

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 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 of International Financial Reporting Standards.

On December 27, 2005, the Accounting Standards Board of Japan (the "ASBJ") published a new accounting standard for the statement of changes in equity, which is effective for fiscal years ending on or after May 1, 2006. The consolidated statement of shareholders' equity, which was previously voluntarily prepared in line with the international accounting practices, is now required under generally accepted accounting principles in Japan and has been renamed "the consolidated statement of changes in equity" in the current fiscal year.

In preparing these consolidated financial statements, certain reclassifications and rearrangements have been made to the consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan. In addition, certain reclassifications have been made in the 2006 financial statements to conform to the 2007 presentation.

The consolidated financial statements are stated in Japanese yen, the currency of the country in which LAWSON, INC. (the "Company") is incorporated and operates. The translations of Japanese yen amounts into U.S. dollar amounts are included solely for the convenience of readers outside Japan and have been made at the rate of ¥118.44 to $1, the approximate rate of exchange at February 28, 2007. Such translations should not be construed as representations that the Japanese yen amounts could be converted into U.S. dollars at that or any other rate.

Mitsubishi Corporation ("Mitsubishi") owned 32,399 thousand shares of common stock of the Company (including indirect holdings) as of February 28, 2007 which represented 31.02% of the total voting rights of the Company. Accordingly, Mitsubishi is a principal shareholder.

2. Summary of Significant Accounting Policies

a. Consolidation—The consolidated financial statements include the accounts of the Company and its subsidiaries (together the "Companies").

Under the control or influence concept, those entities in which the Company, directly or indirectly, is able to exercise control over operations are fully consolidated, and those entities over which the Companies have the ability to exercise significant influence are accounted for by the equity method.

The excess of the cost of the Company's investments in consolidated subsidiaries and associated companies over the fair value of the net assets at the dates of acquisition is being amortized over a period of 5 years.

All significant intercompany balances and transactions have been eliminated in consolidation. All material unrealized profit included in assets resulting from transactions within the Companies is eliminated.

b. Franchise Agreement and Basis of Recognizing Franchise Commission—The Company operates principally in a single industry commonly classified as the convenience store business with its own stores and franchised stores. The Company allows each independent franchisee to operate relatively small-sized convenience stores using specific designs and the LAWSON brand names, and provides related managerial or technical know-how under a franchise agreement. Under the agreement, all franchised stores are provided with a variety of services and advice on the operation of convenience stores from the Company as the franchisor. In return, such franchised stores are required to pay continuing franchise commissions to the Company based on certain percentages of the respective franchised store's annual gross margin. As the franchisor, the Company accounts for franchise commissions on an accrual basis by reference to the annual gross margin earned by each franchised store and the applicable commission percentage. According to the franchise agreement, a franchised store may pay additional guarantee deposits equal to twice of the average monthly sales amounts of the respective store and pay a lower commission percentage.

The term of a franchise agreement is effective primarily for 10 years from the commencement date of a new store's operation as a franchised store, and may be extended or renewed upon expiration subject to renegotiation of contract terms between the Company and the franchisee.

The franchise agreement usually provides that the franchised store shall make a cash payment to the Company in the amount of ¥3 million upon commencement. Upon receipt of such payment, ¥1.5 million is credited to income of the Company as "Operating revenues—franchise commission from franchised stores" for services related to the opening of the LAWSON store. The remaining amount received by the Company is credited to "Due to franchised stores" account and then applied to working capital for purchases of merchandise and supplies for the franchised store.

As part of the contractual obligations of the franchisor under the agreement, the Company generally provides franchisees with furniture, fixtures and equipment designed for the LAWSON stores. In some cases, franchisees may also be provided with the land or buildings for the stores. However, the Company does not require the franchisees to make lease payments related to the stores. Instead, a higher percentage applicable to the gross margin would be used as the basis for determining the franchise commissions. The portion of franchise commission attributable to property and store equipment leases is not separately accounted for by the Company.

c. Cash and Cash Equivalents—Cash and cash equivalents include cash on hand, demand deposits and short-term investments, which mature or become due within three months of the date of acquisition and which are readily convertible into cash and are exposed to insignificant risk of changes in value.

d. Inventories—Inventories are stated at cost determined by the retail method as generally applied in the retail industry.

e. Marketable and Investment Securities—Marketable and investment securities are classified and accounted for, depending on management's intent, as follows: (1) held-to-maturity debt securities, which are expected to be held to maturity with the positive intent and ability to hold to maturity are reported at amortized cost and (2) available-for-sale securities, which are not classified as the aforementioned securities, are stated at fair value based on market quotation. Unrealized gains and losses net of applicable taxes are reported in a separate component of equity. The cost of securities sold is determined based on the moving-average method.

Non-marketable available-for-sale securities are stated at cost determined by the moving-average method. For other than temporary declines in fair value, non-marketable available-for-sale securities are reduced to net realizable value by a charge to income.

f. Property and Store Equipment—Property and store equipment are stated at cost except for land (see Note 7). Depreciation is computed by the declining-balance method at rates based on the estimated useful lives of the assets. The range of useful lives is principally from 10 to 34 years for buildings and structures and from 5 to 8 years for furniture, fixtures and equipment.

g. Long-lived Assets—The Companies review its long-lived assets for impairment whenever events or changes in circumstance indicate the carrying amount of an asset or asset group, mainly by each store, may not be recoverable. An impairment loss would be recognized if the carrying amount of an asset or asset group exceeds the sum of the undiscounted future cash flows expected to result from the continued use and eventual disposition of the asset or asset group. The impairment loss would be measured as the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of the discounted cash flows from the continued use and eventual disposition of the assets or the net selling price at disposition.

h. Software—Software used by the Companies is amortized using the straight-line method based on the estimated useful life (mainly 5 years).

i. Employees' Retirement Benefits—The Company and a certain domestic subsidiary have defined benefit lump-sum severance indemnity plans which cover substantially all of their employees. The Company established a trust fund for its lump-sum severance indemnity plan.

The Companies account for the liability for retirement benefits based on the projected benefit obligations and plan assets at the balance sheet date.

In addition to the lump-sum severance indemnity plan, the Company has a defined contribution plan for severance payments. The Company recognizes expenses in the period when the contribution was called for.

j. Allowance for Retirement Benefits to Executive Officers and Corporate Auditors—
The provisions are calculated to state the liability at 100% of the amount that would be required if all executive officers and corporate auditors resigned as of each balance sheet date.

k. Stock Options—On December 27, 2005, the ASBJ issued ASBJ Statement No. 8, "Accounting Standard for Stock Options" and related guidance. The new standard and guidance are applicable to stock options newly granted on and after May 1, 2006. This standard requires companies to recognize compensation expense for employee stock options based on the fair value at the date of grant and over the vesting period as consideration for receiving goods or services. The standard also requires companies to account for stock options granted to non-employees based on the fair value of either the stock option or the goods or services received. In the balance sheet, the stock option is presented as a stock acquisition right as a separate component of equity until exercised. The standard covers equity-settled, share-based payment transactions, but does not cover cash-settled, share-based payment transactions. In addition, the standard allows unlisted companies to measure options at their intrinsic value if they cannot reliably estimate fair value.

The Company applied the new accounting standard for stock options to those granted on and after May 1, 2006. The effect of adoption of this accounting standard for the year ended February 28, 2007 was to decrease income before income taxes and minority interests by ¥78 million ($659 thousand).

l. Presentation of Equity—On December 9, 2005, the ASBJ published a new accounting standard for presentation of equity. Under this accounting standard, certain items which were previously presented as liabilities are now presented as components of equity. Such items include stock acquisition rights, minority interests, and any deferred gain or loss on derivatives accounted for under hedge accounting. This standard is effective for fiscal years ending on or after May 1, 2006. The consolidated balance sheet as of February 28, 2007 is presented in line with this new accounting standard.

m. Leases—All leases are accounted for as operating leases. Under Japanese accounting standards for leases, finance leases that deem to transfer ownership of the leased property to the lessee are to be capitalized, while other finance leases are permitted to be accounted for as operating lease transactions if certain "as if capitalized" information is disclosed in the notes to the consolidated financial statements.

n. Income Taxes—The Companies provide for income taxes applicable to all items included in the consolidated statements of income regardless of when such taxes are payable. Deferred income taxes are recorded to reflect the impact of temporary differences between assets and liabilities recognized for financial reporting purposes and such amounts recognized for tax purposes. These deferred taxes are measured by applying currently enacted tax laws to the temporary differences.

o. Appropriations of Retained Earnings—Appropriations of retained earnings at each year end are reflected in the consolidated financial statements for the following year upon shareholders' approval.

p. Foreign Currency Financial Statements—The balance sheet accounts of an associated company denominated in foreign currencies are translated into Japanese yen at the current exchange rate as of the balance sheet date except for equity, which is translated at the historical rate. Differences arising from such translation are shown as "Foreign currency translation adjustments" in a separate component of equity. Revenue and expense accounts of an affiliated company denominated in foreign currencies are translated into yen at the current exchange rate.

q. Per Share Information—Basic net income per share is computed by dividing net income available to common shareholders by the weighted-average number of common shares outstanding for the period.

The number of shares used in computing net income per share was 104,134 thousand shares for 2007 and 102,202 thousand shares for 2006.

Diluted net income per share for the years ended February 28, 2007 and 2006 is computed by using the weighted-average number of common shares outstanding adjusted to include the potentially dilutive effect of stock options that were outstanding during the year.

Cash dividends per share presented in the accompanying consolidated statements of income are dividends applicable to the respective years including dividends to be paid after the end of year.

r. New Accounting Pronouncements

Lease accounting—On March 30, 2007, the ASBJ issued ASBJ Statement No. 13, "Accounting Standard for Lease Transactions," which revised the existing accounting standard for lease transactions issued on June 17, 1993.

Under the existing accounting standard, finance leases that deem to transfer ownership of the leased property to the lessee are to be capitalized, however, other finance leases are permitted to be accounted for as operating lease transactions if certain "as if capitalized" information is disclosed in the note to the lessee's financial statements.

The revised accounting standard requires that all finance lease transactions should be capitalized. The revised accounting standard for lease transactions is effective for fiscal years beginning on or after April 1, 2008 with early adoption permitted for fiscal years beginning on or after April 1, 2007.

3. Accounts Receivable—Due From Franchised Stores

Under the franchise agreement, the Company is responsible for providing architectural and designing services with respect to the franchised stores' facilities, for training of the franchisees' personnel, and for the centralized processing of invoices from suggested vendors of merchandise and subsequent payments of amounts payable to such vendors.

The EDP system of the Company generates a record of merchandise purchased by each franchised store and accumulates the amounts payable to respective vendors. Under the franchise agreement, the Company, as a representative for all franchised stores, pays amounts payable to the vendors on the stores' behalf. When the merchandise is received by each franchised store, the Company records the cost of the merchandise in the "Accounts receivable—due from franchised stores" account since such costs shall be subsequently recovered from respective franchised stores.

The "Accounts receivable—due from franchised stores" account represents net amounts recoverable from the franchised stores.

4. Property and Store Equipment

Property and store equipment as of February 28, 2007 and 2006, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	2007
Used by franchised stores:			
Land	¥ 2,202	¥ 1,423	$ 18,592
Buildings	130,492	118,297	1,101,756
Furniture, fixture and equipment	50,701	51,404	428,073
Total	183,395	171,124	1,548,421
Accumulated depreciation	92,448	84,850	780,547
Net	90,947	86,274	767,874
Used by Company-operated stores and other:			
Land	2,507	3,814	21,167
Buildings	13,926	11,811	117,578
Furniture, fixture and equipment	8,277	9,006	69,884
Total	24,710	24,631	208,629
Accumulated depreciation	11,402	11,633	96,268
Net	13,308	12,998	112,361
Net property and store equipment—total	¥104,255	¥ 99,272	$ 880,235

5. Marketable and Investment Securities

Marketable and investment securities as of February 28, 2007 and 2006, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	2007
Current—Bonds	¥14,996	¥19,652	$126,613
Non-current—Marketable and other equity securities	763	1,464	6,442
Non-current—Bonds	797	498	6,729

The costs and aggregate fair values of marketable and investment securities at February 28, 2007 and 2006, were as follows:

	Millions of Yen			
February 28, 2007	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities classified as:				
Held-to-maturity	**¥13,997**	**¥ 3**		**¥14,000**
Available-for-sale:				
Equity securities	**77**	**540**	**¥1**	**616**
Bonds	**1,799**		**3**	**1,796**
February 28, 2006				
Securities classified as:				
Held-to-maturity	16,012	1	3	16,010
Available-for-sale:				
Equity securities	288	1,175		1,463
Bonds	4,141		3	4,138

	Thousands of U.S. Dollars			
February 28, 2007	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities classified as:				
Held-to-maturity	**$118,178**	**$ 25**		**$118,203**
Available-for-sale:				
Equity securities	**650**	**4,559**	**$ 8**	**5,201**
Bonds	**15,189**		**25**	**15,164**

Available-for-sale securities whose fair value is not readily determinable as of February 28, 2007 and 2006, were as follows:

	Carrying Amount		
	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	**2007**
Available-for-sale—Equity securities	**¥147**	¥1	**$1,241**

Proceeds from sales of available-for-sale securities for the years ended February 28, 2007 and 2006 were ¥185 million ($1,562 thousand) and ¥1,705 million, respectively. Gross realized gains on these sales, computed on the moving average cost basis, were ¥44 million ($372 thousand) for the year ended February 28, 2007, and ¥989 million for the year ended February 28, 2006.

6. Long-Lived Assets

The Companies recognized an impairment loss mainly for each store as the smallest cash generating unit, which declined in value due mainly to continuous operating losses. The carrying amount of those assets was written down to the recoverable amount and an impairment loss was recorded in other expenses in the consolidated statements of income.

The Companies recognized impairment loss on the following asset categories for the years ended February 28, 2007 and 2006:

Category	Related Assets	Location	Millions of Yen 2007	Millions of Yen 2006	Thousands of U.S. Dollars 2007
Stores	Buildings and furniture, fixtures and equipment	Tokyo	**¥ 111**	¥ 272	**$ 937**
		Osaka	**303**	183	**2,558**
		Other	**1,397**	1,870	**11,795**
Other	Land			316	
	Software, etc.			67	
Total			**¥1,811**	¥2,708	**$15,290**

The above assets which incurred impairment losses for the years ended February 28, 2007 and 2006, consisted of the following:

	Millions of Yen 2007	Millions of Yen 2006	Thousands of U.S. Dollars 2007
Fixed assets and leased property:			
Building	**¥1,475**	¥1,676	**$12,454**
Leased property	**58**	204	**489**
Land		316	
Others	**278**	512	**2,347**
Total	**¥1,811**	¥2,708	**$15,290**

The recoverable amount of those assets were measured based on net selling price or value in use. The net selling price of land was calculated based on appraised value by real estate appraiser or expected contract price. The value in use was calculated by discounting estimated future cash flows to which the discount rate was applied. The discount rate was 6.9% and 6.0% for the years ended February 28, 2007 and 2006, respectively.

7. Land Revaluation

Under the "Law of Land Revaluation," promulgated on March 31, 1998 and revised on March 31, 1999 and 2001, the Company chose a one-time revaluation of its own-use land to a value based on real estate appraisal information as of February 28, 2002.

The resulting land revaluation difference represents unrealized depreciation of land and is stated, net of income taxes, as a component of equity. There was no effect on the consolidated statements of income. Continuous readjustment is not permitted unless the land value subsequently declines significantly.

As at February 28, 2007, the carrying amount of the land after the above one-time revaluation exceeded the market value by ¥181 million ($1,528 thousand).

8. Lease Deposits

Under certain circumstances, the Company leases land and/or buildings, as a lessee, for its offices and Company-operated stores or for franchisees to operate as franchised stores. The leases are based on long-term, cancelable lease agreements with owners. In connection with such agreements, the lessor requires leasehold deposits equivalent to approximately several months' rent, which are non-interest bearing and refundable only when the leases are terminated.

Lease deposits as of February 28, 2007 and 2006, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	**2007**
Lease deposits for franchised stores	**¥72,870**	¥74,856	**$615,248**
Lease deposits for Company-operated stores and other	**15,034**	15,072	**126,934**
Total	**¥87,904**	¥89,928	**$742,182**

9. Accounts Payable—Trade

The balances of "Accounts payable—trade" represent the amounts payable to vendors for merchandise purchased by Company-operated stores and franchised stores. The Company centralizes all merchandise purchasing procedures both for Company-operated stores and franchised stores and makes collective payments to vendors (see Note 3).

Accounts payable—trade as of February 28, 2007 and 2006, were summarized below:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	**2007**
Accounts payable—trade for franchised stores	**¥60,817**	¥59,795	**$513,484**
Accounts payable—trade for Company-operated stores	**4,183**	3,375	**35,317**
Total	**¥65,000**	¥63,170	**$548,801**

10. Accounts Payable—Due to Franchised Stores

The cost of merchandise supplied to the franchised stores is recorded as "Accounts receivable—due from franchised stores" as described in Note 3.

All franchised stores make remittances of cash proceeds from daily sales to the Company. In certain instances, the remittance from a franchised store exceeds the balance of "Accounts receivable—due from franchised stores." In the accompanying consolidated balance sheets, such excess balances are presented as "Accounts payable—due to franchised stores."

11. Employees' Retirement Benefits

The Company and a certain domestic subsidiary have each of defined benefit lump-sum severance indemnity plan.

Under the plans, employees terminating their employment are entitled to retirement benefits determined based on the rate of pay, years of service and certain other factors at the time of termination. Such retirement benefits are made in the form of a lump-sum severance payment from the Company or from a certain subsidiary. Employees are entitled to larger payments if the termination is involuntary, by retirement at the mandatory retirement age, by death, or by voluntary retirement at certain specific ages prior to the mandatory retirement age.

The funded status of these plans as of February 28, 2007 and 2006 was as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	**2007**
Projected benefit obligation	**¥10,736**	¥10,710	**$ 90,645**
Fair value of plan assets	**(5,548)**	(5,536)	**(46,842)**
Unrecognized prior service cost	**(1,230)**	(1,406)	**(10,385)**
Unrecognized actuarial loss	**(431)**	(951)	**(3,639)**
Net liability	**¥ 3,527**	¥ 2,817	**$ 29,779**

The components of net periodic benefit costs for the years ended February 28, 2007 and 2006 were as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	**2007**
Service cost	**¥1,105**	¥ 812	**$ 9,330**
Interest cost	**213**	197	**1,798**
Amortization of prior service cost	**176**	176	**1,486**
Recognized actuarial loss	**128**	119	**1,081**
Contribution to defined contribution plan	**246**	248	**2,077**
Net periodic benefit costs	**¥1,868**	¥1,552	**$15,772**

Assumptions used for the years ended February 28, 2007 and 2006, were as follows:

	2007	2006
Discount rate	**2.0%**	2.0%
Expected rate of return on plan assets	**0%**	0%
Amortization period of prior service cost	**10 years**	10 years
Recognition period of actuarial gain/loss	**10 years**	10 years

12. Equity

On and after May 1, 2006, Japanese companies are subject to a new corporate law of Japan (the "Corporate Law"), which reformed and replaced the Commercial Code of Japan (the "Code") with various revisions that are, for the most part, applicable to events or transactions which occur on or after May 1, 2006 and for the fiscal years ending on or after May 1, 2006. The significant changes in the Corporate Law that affect financial and accounting matters are summarized below:

a. Dividends

Under the Corporate Law, companies can pay dividends at any time during the fiscal year in addition to the year-end dividend upon resolution at the shareholders meeting. For companies that meet certain criteria such as: (1) having the Board of Directors, (2) having independent auditors, (3) having the Board of Corporate Auditors, and (4) the term of service of the directors is prescribed as one year rather than two years of normal term by its articles of incorporation, the Board of Directors may declare dividends (except for dividends in kind) at any time during the fiscal year if the company has prescribed so in its articles of incorporation. The Company meets all the above criteria.

The Corporate Law permits companies to distribute dividends-in-kind (non-cash assets) to shareholders subject to a certain limitation and additional requirements.

Semiannual interim dividends may also be paid once a year upon resolution by the Board of Directors if the articles of incorporation of the company so stipulate. The Corporate Law provides certain limitations on the amounts available for dividends or the purchase of treasury stock. The limitation is defined as the amount available for distribution to the shareholders, but the amount of net assets after dividends must be maintained at no less than ¥3 million.

b. Increases/Decreases and Transfer of Common Stock, Reserve and Surplus

The Corporate Law requires that an amount equal to 10% of dividends must be appropriated as a legal reserve (a component of retained earnings) or as additional paid-in capital (a component of capital surplus) depending on the equity account charged upon the payment of such dividends until the total of aggregate amount of legal reserve and additional paid-in capital equals 25% of the common stock. Under the Corporate Law, the total amount of additional paid-in capital and legal reserve may be reversed without limitation. The Corporate Law also provides that common stock, legal reserve, additional paid-in capital, other capital surplus and retained earnings can be transferred among the accounts under certain conditions upon resolution of the shareholders.

c. Treasury Stock and Treasury Stock Acquisition Rights

The Corporate Law also provides for companies to purchase treasury stock and dispose of such treasury stock by resolution of the Board of Directors. The amount of treasury stock purchased cannot exceed the amount available for distribution to the shareholders which is determined by specific formula. Under the Corporate Law, stock acquisition rights, which were previously presented as a liability, are now presented as a separate component of equity. The Corporate Law also provides that companies can purchase both treasury stock acquisition rights and treasury stock. Such treasury stock acquisition rights are presented as a separate component of equity or deducted directly from stock acquisition rights.

13. Stock Option

The Company has a stock option plan as an incentive plan for directors, executive officers and selected employees.

A summary of information for the Company's stock option plans is as follows:

Stock Option	Persons Granted	Number of Options Granted	Date of Grant	Exercise Price	Exercise Period
Stock subscription rights	18 directors and 574 employees	1,773,000 shares	2000.6.12	¥7,500 ($63.32)	From May 27, 2002 to May 25, 2007
1st Stock Option	8 directors, 14 executive officers and 561 employees	313,000 shares	2002.6.25	¥3,680 ($31.07)	From December 1, 2002 to May 31, 2007
2nd Stock Option	9 directors and 17 executive officers	92,000 shares	2003.7.3	¥3,517 ($29.69)	From July 3, 2005 to July 2, 2008
3rd Stock Option	9 directors and 20 executive officers	99,000 shares	2004.6.10	¥4,320 ($36.47)	From June 10, 2006 to June 9, 2009
4th Stock Option	9 directors and 24 executive officers	114,000 shares	2005.10.12	¥4,160 ($35.12)	From October 12, 2007 to December 31, 2010
5th Stock Option	9 directors	22,400 shares	2005.10.12	¥1 ($0.01)	From October 13, 2005 to May 31, 2025
6th (a) Stock Option	9 directors	21,300 shares	2006.10.26	¥1 ($0.01)	From October 27, 2006 to May 26, 2026
6th (b) Stock Option	9 directors and 14 executive officers	83,000 shares	2006.10.26	¥4,053 ($34.22)	From October 28, 2008 to October 26, 2011

The stock option activity is as follows:

	Stock Subscription Rights	1st Stock Option	2nd Stock Option	3rd Stock Option	4th Stock Option	5th Stock Option	6th (a) Stock Option	6th (b) Stock Option
								(Shares)
For the Year Ended February 28, 2006								
Non-vested:								
February 28, 2005—outstanding				99,000	114,000			
Granted								
Canceled								
Vested								
February 28, 2006—outstanding				99,000	114,000			
Vested:								
February 28, 2005—outstanding	1,089,000	192,900	92,000					
Vested						22,400		
Exercised		(65,500)	(43,800)					
Canceled	(72,000)	(3,100)						
February 28, 2006—outstanding	1,017,000	124,300	48,200			22,400		

	Stock Subscription Rights	1st Stock Option	2nd Stock Option	3rd Stock Option	4th Stock Option	5th Stock Option	6th (a) Stock Option	6th (b) Stock Option
								(Shares)
For the Year Ended February 28, 2007								
Non-vested:								
February 28, 2006—outstanding				99,000	114,000			
Granted							**21,300**	**83,000**
Canceled								
Vested				**(99,000)**			**(21,300)**	
February 28, 2007—outstanding					**114,000**			**83,000**
Vested:								
February 28, 2006—outstanding	1,017,000	124,300	48,200			22,400		
Vested				**99,000**			**21,300**	
Exercised		**(28,200)**	**(4,600)**			**(2,400)**		
Canceled	**(169,000)**	**(8,400)**						
February 28, 2007—outstanding	**848,000**	**87,700**	**43,600**	**99,000**		**20,000**	**21,300**	
Exercise price	**¥7,500**	**¥3,680**	**¥3,517**	**¥4,320**	**¥4,160**	**¥1**	**¥1**	**¥4,053**
	($63.32)	**($31.07)**	**($29.69)**	**($36.47)**	**($35.12)**	**($0.01)**	**($0.01)**	**($34.22)**
Average stock price at exercise		**¥4,489**	**¥4,386**			**¥4,060**		
		($37.90)	**($37.03)**			**($34.28)**		
Fair value price at grant date							**¥3,178**	**¥618**
							($26.83)	**($5.22)**

The assumptions used to measure fair value of 6th Stock Option were as follows:

	6th (a) Stock Option	6th (b) Stock Option
Estimate method	Black-Scholes option pricing model	Black-Scholes option pricing model
Volatility of stock price	37.06%	25.80%
Estimated remaining outstanding period	9.8 years	3.5 years
Estimated dividend	¥95 per share	¥95 per share
Interest rate with risk free	1.74%	0.98%

14. Income Taxes

The Company and its domestic subsidiaries are subject to a number of different taxes based on income, which in the aggregate, resulted in a normal effective statutory tax rate of approximately 40.7% for the years ended February 28, 2007 and 2006.

The tax effects of significant temporary differences and tax loss carryforwards which resulted in deferred tax assets and liabilities at February 28, 2007 and 2006, are as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	**2007**
Deferred tax assets:			
Accrued enterprise tax	**¥ 498**	¥ 833	**$ 4,205**
Accrued employees' bonuses	**1,100**	1,144	**9,287**
Excess of depreciation	**3,445**	3,320	**29,086**
Excess of amortization of software	**648**	930	**5,471**
Employees' retirement benefits	**3,673**	3,255	**31,011**
Allowance for doubtful accounts	**1,671**	1,772	**14,108**
Tax loss carryforward	**1,758**	1,425	**14,843**
Impairment loss	**1,129**	2,197	**9,532**
Loss on replacement of computer system	**896**		**7,565**
Other	**1,575**	1,527	**13,300**
Less valuation allowance	**(1,827)**	(1,690)	**(15,426)**
Total	**14,566**	14,713	**122,982**
Deferred tax liabilities—Unrealized gain on available-for-sale securities	**220**	478	**1,858**
Total	**220**	478	**1,858**
Net deferred tax assets	**¥14,346**	¥14,235	**$121,124**

As of February 28, 2007, certain subsidiaries have tax loss carryforwards aggregating approximately ¥4,247 million ($35,858 thousand) which are available to be offset against taxable income of such subsidiaries in future years. These tax loss carryforwards, if not utilized, will expire as follows:

Year Ending February 28 or 29	Millions of Yen	Thousands of U.S. Dollars
2010	¥ 484	$ 4,086
2011	415	3,504
2012	287	2,424
2013	1,605	13,551
2014 and thereafter	1,456	12,293
Total	¥4,247	$35,858

15. Replacement of Computer System

The Company decided to replace its computer system to the next generation, including core information systems, based on an optical fiber network in 2008 and 2009. The Company recognized loss on replacement system, as special depreciation of the related equipment and software and equivalent of those related to lease cancellation of existing system.

	Millions of Yen	Thousands of U.S. Dollars
	2007	**2007**
Loss on replacement of computer system:		
Lease property (cancellation)	**¥1,624**	**$13,712**
Equipment	**542**	**4,576**
Software	**36**	**304**
Total	**¥2,202**	**$18,592**

The amount of the lease cancellation loss, equivalent to special depreciation, was included in other under long-term liabilities.

16. Leases

The Companies lease certain store facilities, machinery, computer equipment, office space and other assets.

Total lease payments under finance leases for the years ended February 28, 2007 and 2006, were ¥17,485 million ($147,627 thousand) and ¥16,900 million, respectively.

Pro forma information of leased property such as acquisition cost, accumulated depreciation, accumulated impairment loss, obligations under finance leases, depreciation expense, interest expense and impairment loss for finance leases that do not transfer ownership of the leased property to the lessee on an "as if capitalized" basis for the years ended February 28, 2007 and 2006 was as follows:

Leased to franchised stores:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	**2007**
Furniture, Fixtures and Equipment:			
Acquisition cost	**¥65,163**	¥68,378	**$550,177**
Accumulated depreciation	**40,122**	38,352	**338,754**
Accumulated impairment loss	**204**	158	**1,722**
Net leased property	**¥24,837**	¥29,868	**$209,701**

Obligations under finance leases:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	**2007**
Due within one year	**¥11,976**	¥11,972	**$101,114**
Due after one year	**13,607**	18,898	**114,886**
Total	**¥25,583**	¥30,870	**$216,000**

Allowance for impairment loss on leased property of ¥79 million ($667 thousand) as of February 28, 2007 is included in obligations under finance leases.

Used by Company-operated stores and other:

	Millions of Yen		
	2007		
	Furniture, Fixtures and Equipment	Software	Total
Acquisition cost	**¥18,848**	**¥734**	**¥19,582**
Accumulated depreciation	**11,310**	**342**	**11,652**
Accumulated impairment loss	**30**		**30**
Net leased property	**¥ 7,508**	**¥392**	**¥ 7,900**

	Millions of Yen		
	2006		
	Furniture, Fixtures and Equipment	Software	Total
Acquisition cost	¥17,073	¥734	¥17,807
Accumulated depreciation	10,311	196	10,507
Accumulated impairment loss	17		17
Net leased property	¥ 6,745	¥538	¥ 7,283

	Thousands of U.S. Dollars		
	2007		
	Furniture, Fixtures and Equipment	Software	Total
Acquisition cost	**$159,135**	**$6,197**	**$165,332**
Accumulated depreciation	**95,491**	**2,887**	**98,378**
Accumulated impairment loss	**253**		**253**
Net leased property	**$ 63,391**	**$3,310**	**$ 66,701**

Obligation under finance leases:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	**2007**
Due within one year	**¥3,432**	¥3,378	**$28,977**
Due after one year	**4,851**	4,469	**40,957**
Total	**¥8,283**	¥7,847	**$69,934**

Allowance for impairment loss on leased property of ¥17 million ($144 thousand) as of February 28, 2007 is included in obligations under finance leases.

The imputed interest expense portion which is computed using the interest method is excluded from the above obligations under finance leases.

Depreciation expense, interest expense and other information under finance leases:

	Millions of Yen		Thousands of U.S. Dollars
	2007	2006	**2007**
Depreciation expense	**¥16,342**	¥15,782	**$137,977**
Interest expense	**1,004**	1,090	**8,477**
Reversal of allowance for impairment loss on leased property	**82**	37	**692**
Impairment loss	**58**	204	**490**

Depreciation expense and interest expense, which are not reflected in the accompanying consolidated statements of income, are computed by the straight-line method and the interest method, respectively.

The minimum rental commitments under noncancelable operating leases at February 28, 2007 were as follows:

	Millions of Yen	Thousands of U.S. Dollars
	2007	**2007**
Due within one year	**¥ 549**	**$ 4,635**
Due after one year	**861**	**7,270**
Total	**¥1,410**	**$11,905**

17. Related Party Transactions

Balances to LAWSON CS Card, Inc. (an associated company) as of February 28, 2007 were as follows:

	Millions of Yen	Thousands of U.S. Dollars
	2007	**2007**
Short-term loan receivable	**¥ 8,850**	**$74,721**
Guarantee for bank loans	**11,350**	**95,829**

Mitsubishi became a direct principal shareholder when they purchased all shares in the Company, which had been held by their wholly owned subsidiary, in December 2004.

Since then, Mitsubishi has been treated as an affiliated company of the Company. Therefore, the Company discloses transactions with subsidiaries of Mitsubishi, including those transactions related to the franchised stores.

Balances and transactions with subsidiaries of the principal shareholder as of and for the year ended February 28, 2007 were as follows:

	Millions of Yen	Thousands of U.S. Dollars
	2007	**2007**
RYOSHOKU LIMITED:		
Accounts payable—trade	**¥ 6,466**	**$ 54,593**
Purchases	**88,968**	**751,165**
Food Service Network Co., Ltd.:		
Accounts payable—trade	**16,445**	**138,847**
Purchases	**218,341**	**1,843,473**
SAN-ESU INC.:		
Accounts payable—trade	**2,795**	**23,598**
Purchases	**31,286**	**264,151**

18. Contingent Liabilities

As of February 28, 2007, the Company guaranteed an associated company's bank loan in the amount of ¥11,350 million ($95,829 thousand).

19. Net Income per Share

Reconciliation of the differences between basic and diluted net income per share ("EPS") for the years ended February 28, 2007 and 2006 is as follows:

	Millions of Yen	Thousands of Shares	Yen	U.S. Dollars
Year Ended February 28, 2007	Net Income	Weighted-average Shares		EPS
Basic EPS—Net income available to common shareholders	**¥20,983**	**104,134**	**¥201.50**	**$1.70**
Effect of dilutive securities—Stock options		**52**		
Diluted EPS—Net income for computation	**¥20,983**	**104,186**	**¥201.40**	**$1.70**
Year Ended February 28, 2006				
Basic EPS—Net income available to common shareholders	¥22,025	102,202	¥215.50	
Effect of dilutive securities—Stock options		20		
Diluted EPS—Net income for computation	¥22,025	102,222	¥215.46	

20. Subsequent Events

a. The following appropriation of retained earnings was approved at the general shareholders meeting held on May 25, 2007:

	Millions of Yen	Thousands of U.S. Dollars
Cash dividends, ¥50 ($0.42) per share	¥5,221	$44,081

b. The Company resolved at the meeting of the Board of Directors on May 11, 2007 to acquire, through a public tender process, shares of Lawson Ticket Inc., a consolidated subsidiary of the Company that is publicly listed on the Jasdaq Securities Exchange.

The Company executed a capital participation agreement with Rakuten, Inc. on January 5, 2004, to accompany the business tie-up agreement that was executed between Lawson Ticket Inc. and Rakuten, Inc. on the same day. Under the capital participation agreement, if certain circumstances occur such as the termination of the business tie-up agreement or the capital participation agreement, the Company has the right to purchase part or all of the Rakuten-owned shares on condition that the notification of the intent to exercise the share purchase rights is made within two months from the day the aforesaid circumstance occurs. On March 13, 2007, the Company canceled the business tie-up agreement and the capital participation agreement upon cancellation of these agreements, the Company exercised its right to purchase all of Rakuten-owned shares.

The Company made a tender offer with the primary objective of purchasing all shares held by Rakuten, Inc., that is 9,800 shares (17.8% equity interest) of 55,000, the total number of Lawson Ticket shares issued, as follows:

(1) Period of tender offer
From May 14, 2007 to June 12, 2007 (22 working days)

(2) Price of tender offer
¥140,000 per share

(3) Intended number of shares to purchase
9,800 shares

(4) Total cost of tender offer (estimate)
¥1,372,000,000

Independent Auditors' Report

Deloitte.

Deloitte Touche Tohmatsu
MS Shibaura Building
4-13-23 Shibaura
Minato-ku, Tokyo 108-8530
Japan

Tel: +81 (3) 3457 7321
Fax: +81 (3) 3457 1694
www.deloitte.com/jp

To the Board of Directors of LAWSON, INC.:

We have audited the accompanying consolidated balance sheets of LAWSON, INC. (the "Company") and subsidiaries as of February 28, 2007 and 2006, and the related consolidated statements of income, changes in equity, and cash flows for the years then ended, all expressed in Japanese yen. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to 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 LAWSON, INC. and subsidiaries as of February 28, 2007 and 2006, and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in Japan.

Our audits also comprehended the translation of Japanese yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made in conformity with the basis stated in Note 1. Such U.S. dollar amounts are presented solely for the convenience of readers outside Japan.

Deloitte Touche Tohmatsu

May 25, 2007

Member of
Deloitte Touche Tohmatsu

Directors, Corporate Auditors and Executive Officers

PRESIDENT AND CEO	Takeshi Niinami	
MEMBER OF THE BOARD AND SENIOR EXECUTIVE VICE PRESIDENT	Toru Moriyama	General Manager, Merchandizing & Logistics Division
MEMBER OF THE BOARD AND EXECUTIVE VICE PRESIDENT	Yoshiyuki Yahagi	Chief Financial Officer (CFO); in charge of Corporate Planning Office; in charge of Human Resources Office
MEMBER OF THE BOARD AND SENIOR VICE PRESIDENT	Manabu Asano	Chief Compliance Officer (CCO); in charge of General Affairs; in charge of Internal Audit
MEMBERS OF THE BOARD	Hiroshi Tasaka	Professor, Graduate School of Tama University
	Reiko Okutani	President, The R Co., Ltd.
	Takehiko Kakiuchi	General Manager, Living Essentials Group CEO Office, Mitsubishi Corporation
STANDING CORPORATE AUDITORS	Munehiko Nakano	
	Kenji Yamakawa	
CORPORATE AUDITORS	Tetsuo Ozawa	Lawyer
	Hiroshi Kuwata	General Manager, Risk Management Dept., Mitsubishi Corporation
EXECUTIVE VICE PRESIDENTS	Susumu Hasegawa	Chief Information Officer (CIO); General Manager, Information Systems Station
	Ichiro Okuda	General Manager, Kinki LAWSON Branch
	Takatoshi Kawamura	General Manager, Kanto LAWSON Branch, Next-Generation Business Development Division
SENIOR VICE PRESIDENTS	Konoshin Deguchi	General Manager, Corporate Franchisee Development Division
	Shigeru Niikura	General Manager, Operations Office
	Katsuyuki Imada	General Manager, Corporate Planning Office
	Kiyoteru Suzuki	General Manager, Services Development Division
	Yoshio Shinozaki	General Manager, CSR Promotion Office
	Shigeaki Kawahara	Executive Assistant to CEO President and CEO, VALUE LAWSON, Inc
	Kenji Morimoto	General Manager, Finance & Accounting Office General Manager, Management Services Office
	Takaki Mizuno	General Manager, Chubu LAWSON Branch
	Norikazu Nishiguchi	General Manager, Store Development Planning Division
	Jyun Miyazaki	General Manager, PR, Corporate Communications Office
	Masatoshi Okada	President, NATURAL LAWSON, Inc.
	Hajime Nakai	Deputy General Manager, Kinki LAWSON Branch
	Yoichi Yokomizo	Executive Assistant to CIO

(As of May 25, 2007)

Corporate Data

ENGLISH COMPANY NAME
LAWSON, INC.

ADDRESS
Tokyo Headquarters:
East Tower, Gate City Osaki
11-2, Osaki 1-chome, Shinagawa-ku,
Tokyo 141-8643, Japan

NUMBER OF EMPLOYEES
3,614 (Consolidated) (As of February 28, 2007)

BUSINESS ACTIVITIES
Development of LAWSON convenience store franchise chain

NET SALES OF ALL STORES
¥1,386.6 billion (Consolidated) (Fiscal 2006)

NUMBER OF STORES
8,564 (Consolidated) (As of February 28, 2007)

OPERATING AREA
All 47 prefectures in Japan; Shanghai, PRC (Joint Venture)

ESTABLISHED
April 15, 1975

CAPITAL
¥58,506,644,000

AUTHORIZED SHARES
409,300,000

SHARES ISSUED
104,600,000

SHAREHOLDERS
40,904

MAJOR SHAREHOLDERS

	Number of Shares Held	Percentage of Total Shares Held
1. Mitsubishi Corporation	32,089,300	30.7
2. Japan Trustee Services Bank, Ltd. (Trust Account)	7,769,000	7.4
3. Marubeni Foods Investment Co., Ltd.	5,939,500	5.7
4. The Master Trust Bank of Japan, Ltd. (Trust Account)	5,910,300	5.7
5. Trust & Custody Services Bank, Ltd. (Securities Investment Trust Company)	2,610,800	2.5
6. NTT DoCoMo, Inc.	2,092,000	2.0
7. MELLON BANK N.A. AS AGENT FOR ITS CLIENT MELLON OMNIBUS US PENSION	1,401,868	1.3
8. The Nomura Trust & Banking Co., Ltd. (Trust account)	1,194,900	1.1
9. STATE STREET BANK AND TRUST COMPANY 505103	1,126,896	1.1
10. The Sumitomo Trust & Banking Co., Ltd. (Trust account B)	1,093,300	1.0

STOCK EXCHANGE LISTINGS
Tokyo Stock Exchange (1st Section)
Osaka Securities Exchange (1st Section)

STOCK TRANSFER AGENT
Mitsubishi UFJ Trust and Banking Corporation
4-5, Marunouchi, 1-chome, Chiyoda-ku, Tokyo 100-8212, Japan

(As of February 28, 2007)

LAWSON

LAWSON, INC.

Corporate Planning Office,
East Tower, Gate City Osaki
11-2, Osaki 1-chome, Shinagawa-ku,
Tokyo 141-8643, Japan
http://www.lawson.co.jp/
Published in August 2007.

B-(2)-060001

This annual report was produced using "Kanbatsu White," which contains 70% Japan-made pulp, including 10% clear-cut lumber.

Printed in Japan