

Roche Group

Group results

The Roche Group posted record results in 2007. Group sales were up significantly, advancing 10% in local currencies (10% in Swiss francs; 15% in US dollars) to 46.1 billion Swiss francs. This 4.1 billion Swiss franc rise in full-year sales was all organic growth. The Pharmaceuticals Division's sales increased 11% in local currencies (10% in Swiss francs; 15% in US dollars) to 36.8 billion Swiss francs; this was approximately twice the global market growth rate. Demand remained very strong for the cancer medicines Avastin, Herceptin, MabThera/Rituxan, Tarceva and Xeloda. Combined sales of the division's oncology products were up 20% for the year, reinforcing Roche's market leadership in this therapeutic area. Other pharmaceuticals driving growth included Bonviva/Boniva for osteoporosis, CellCept in transplantation, Pegasys in virology and the ophthalmology medicine Lucentis. The Diagnostics Division strengthened its market leadership with sales totalling 9.3 billion Swiss francs, a 6% increase in local currencies (7% in Swiss francs; 12% in US dollars) over 2006. Professional Diagnostics and Applied Science were the business areas posting the strongest growth.

Last year's higher Group sales had a very positive impact on earnings performance. The Group's operating profit increased 22% in local currencies to 14.5 billion Swiss francs. The operating profit margin grew 3.5 percentage points to 31.4%. In the Pharmaceuticals Division, operating profit rose 22% in local currencies to 13.0 billion Swiss francs, with the corresponding margin showing a 3.8 percentage point increase to 35.5%. This margin growth was achieved while the Group continued to significantly increase investments in its strong development pipeline. This is reflected in the Pharmaceuticals Division's higher research and development expenses, which grew 18% in local currencies to 7.6 billion Swiss francs. The Diagnostics Division's operating profit rose 14% in local currencies to 1.6 billion Swiss francs, and its oper-

ating profit margin improved 1.3 percentage points to 17.6%.

Net financial income totalled 834 million Swiss francs, compared with 855 million Swiss francs in 2006. The Group's effective tax rate declined to 25.3% from 27.3%.

Net income increased 25% to 11.4 billion Swiss francs. Core Earnings per Share (Core EPS), which excludes amortisation and impairment of intangible assets, increased by 20% to 11.85 Swiss francs.

The Group's business operations continued to show strong cash generation of 18.5 billion Swiss francs, driven by continued growth in EBITDA. Net cash increased by more than one billion to 17.3 billion Swiss francs.

There was a further significant improvement in the Group's financial position. The ratio of equity to total assets reached 68% (up from 63% in 2006), and over 80% of total assets are now financed long-term.

Outlook

For 2008 we expect Group sales in local currencies to increase at a high single-digit rate, with above-market sales growth in both divisions. This excludes government and corporate stockpiling orders of Tamiflu for pandemic use. As most of the existing pandemic stockpiling orders have now been filled, we anticipate a significant decrease in Tamiflu sales in 2008.

The progress in our rich clinical development pipeline is especially important to our future growth outlook. Accordingly, we plan to increase research and development spending again significantly in 2008 in order to realise the full potential of our strong development portfolio. The activities this will support include late-stage clinical testing of promising compounds such as pertuzumab

(breast cancer), ocrelizumab (autoimmune disorders), GLP-1 analogue (type 2 diabetes) and the CETP inhibitor (dyslipidemia), and several programmes aimed at expanding the use of our leading anticancer medicines into additional indications.

We anticipate continued strong growth in 2009 and 2010, driven by the launch of Actemra, Mircera and additional new indications for MabThera in rheumatoid arthritis, Avastin and other cancer medicines. Very importantly, we also anticipate pivotal clinical trial data on the use of Avastin in early-stage cancer (adjuvant therapy) by the end of 2009.

Despite anticipated considerably lower Tamiflu sales and significantly higher R&D spending we are aiming for 2008 Core EPS at constant exchange rates to remain at least in line with the record level achieved in 2007.

We expect and intend to continue raising our dividend payout ratio over the next three years.

Group strategy

Responding to demographic challenges

Despite significant advances in medicine, the need for innovative new products to diagnose and treat disease is greater than ever. One reason for this is demographic – the fact that the world's population is growing and ageing. As life expectancy increases, so does the incidence of age-related diseases such as cancer, Alzheimer's, diabetes and rheumatoid arthritis. These and other diseases are already placing an ever greater financial burden on healthcare systems. Another factor is that today people are better informed about medical advances and available treatments than they used to be. And well-informed patients and patient organisations can and do influence medical decision-making in ways that add to the overall demand for healthcare services. As a result, there is mounting political pressure to control health spending more effectively. Increasingly, this is also an issue in developing countries, where healthcare systems are massively under-resourced and many patients cannot afford to pay for treatment themselves.

To stay competitive in an increasingly cost-sensitive marketplace, research-based healthcare companies like Roche aim to develop products with health economic as well as clinical benefits. Medicines that extend patients' lives or reduce costly complications and side effects can deliver both. And so can diagnostic tests that help physicians detect diseases earlier and choose the most appropriate therapies for their patients the first time around. This leads to better and more cost-effective outcomes for both patients and healthcare providers.

Focusing on innovation in therapeutics and diagnostics

At Roche we focus our resources on two research-intensive businesses: pharmaceuticals and diagnostics. Within these businesses we prioritise those areas of significant unmet need where we have the expertise to make a difference. Our aim is to develop new and improved drugs, diagnostic tests and services offering significant benefits over existing options. For this reason, we invest heavily in research and development – 8.4 billion Swiss francs in 2007 alone – and we will continue to do so in future.

The clinical return on this investment has been impressive. As the world leader in *in vitro* diagnostics, we supply a wide range of rapid, reliable instruments and tests for disease screening and diagnosis in laboratories, at the point of care in hospitals and doctors' offices, and for patient self-management. In therapeutics our achievements include developing five anticancer medicines which have been shown to prolong patients' lives. These medicines represent significant advances in a therapeutic area which for decades saw little real progress.

Research network spurs innovation

Our innovation model relies on the drug and diagnostics research of our own operating divisions augmented by a global collaborative R&D network. Within the Group, our majority-owned subsidiaries Genentech in the United States and Chugai in Japan operate largely independently. This encourages a greater diversity of ideas and approaches, increasing the chances of bringing new products to patients.

To make sure we have broad access to new technologies and products of interest, we also maintain a host of scientific and commercial collaborations with external biotech companies, universities and research organisations around the world. Identifying and investing in important emerging technologies is critical for ensuring the future strength of our product pipeline. Recent investments include an alliance giving us access to Alnylam's RNAi technologies (see page 70) and the acquisitions of 454 Life Sciences, BioVeris Corporation and NimbleGen Systems, Inc., all completed in 2007.

The acquisition of Ventana Medical Systems, Inc., agreed in January 2008, will enable us to move into the fast-growing market for tissue-based diagnostics and strengthen our capabilities for developing companion diagnostic tests. These make it possible to assess or predict patients' responses to particular medicines so that drug therapy can be tailored more specifically, effectively and cost-efficiently to individual patients' needs.

In early 2007 Roche Pharmaceuticals realigned its global research and development activities around five new organisational units known as Disease Biology Areas (DBAs): Oncology, Virology, Inflammation, Metabolism and Central Nervous System. Each DBA covers all activities from research and development to strategic marketing in a particular therapeutic field. By enhancing the flow of information and streamlining decision-making, this realignment will support our efforts to efficiently translate research activity into clinically differentiated medicines (see page 23).

Pioneering personalised healthcare

Two patients can have the same diagnosis yet respond in dramatically different ways to the same medicine. One patient may be helped by treatment, while the other experiences unwanted side effects without the desired clinical benefit. Some of this variability is due to genetic and other biological differences between patients. The idea of personalised medicine is to use insights into these differences at the molecular level to develop treatments and tests tailored to the needs of specific patient populations. This has enormous potential to make healthcare better, safer and more cost-effective.

It will be a while before this potential is fully realised, but the market is clearly shifting away from 'one size fits all' products. Roche is a driving force behind this trend and already has several personalised healthcare products on the market. An important part of personalising medicine will be developing therapeutics and diagnostics that work in tandem. The fact that we are leaders in both these areas is a source of competitive advantage when it comes to meeting the healthcare challenges of the future.

Creating sustainable value for all stakeholders

Our focus is on enduring success. This can only be achieved by adopting and adhering to sustainable business practices. We recognise that we must manage all aspects of our business – whether economic, ethical, social or environmental – in a responsible way. One factor that is vital to our company's long-term prosperity is our ability to recruit and retain the best people (see page 72).

Looking beyond the financial bottom line, we strive to identify and address the societal, environmental and other management issues of greatest importance to our stakeholders. For detailed information on our performance in these areas, see pages 65 to 70 of this report.

We make our greatest contribution to a sustainable future by developing clinically differentiated healthcare products that meet the needs of patients, healthcare providers, payers and society.



A Roche scientist performing a DNA sequencing experiment

DNA sequencing. In their quest for new ways to fight disease, scientists rely on cutting-edge instruments and highly specific tests. Some of the most innovative tools being used today in the world's top research centres are from Roche. These include a DNA sequencer that is setting new standards in genome research and helping to expand our knowledge of the molecular basis of disease.