

Financial review

The Group this year has delivered improved financial performance with growth in sales, earnings per share and operational cash flow in a period when we have continued our expansion.

Overview

Our businesses operate in a relatively stable, and growing, part of the economy which is subject to periodic governmental action as countries attempt to control their growing healthcare expenditure. We have continued to deliver growth from our operating businesses whilst expanding the Group, achieving growth beyond that of our markets. This has resulted in further enhancements to shareholder returns with the maintenance of strong cashflows.

The Group prudently manages its financial activities with a number of Board committees having responsibility for the review and approval of proposals for acquisitions, allocation of capital, determination of treasury policies and risk management together with the approval of significant debt facilities and control over the financial structure of the Group.

Sales

The Group's turnover grew by 18.1 per cent to £7,314 million (€11,798 million), including £150 million (€242 million) from acquisitions. Excluding acquisitions and currency movements, Group turnover was 9.1 per cent higher than last year.

Operating profit

Group operating profit before amortisation of goodwill and exceptional items increased by 21.8 per cent to £198.7 million (€320.5 million). After goodwill amortisation, total operating profit grew by 17.5 per cent to £187.4 million (€302.3 million). The growth has been achieved by a focus on our core businesses together with acquisitions both on an in-fill basis and into new territories. The total goodwill amortisation charge increased to £11.3 million (€18.2 million) from £3.5 million (€5.7 million) as a result of the acquisitions during the year and the full year effect of acquisitions in the prior year.

Interest

During the year we spent over £271 million (€437 million) on acquiring new businesses, almost £188 million (€304 million) of which was invested in the expansion of our retail businesses across Europe. This has resulted in the Group's interest charge increasing by £10.2 million (€15.7 million) to £39.6 million (€63.9 million) for 2001, offset by a small fall in the average interest rate paid by the Group. This gives us interest cover on a pre-goodwill basis of 5.0 times. Clearly, the level of interest cover is

a function of the level of borrowings and it is the Group's policy to utilise the most efficient capital structure so as to optimise shareholder returns, whilst at the same time maintaining a secure risk profile. Although not officially rated the Board believes these objectives will be best met by maintaining a debt profile that, if rated, would be investment grade.

Taxation

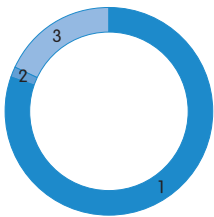
The Group's effective tax rate for the year, based on profit before amortisation of goodwill, was 31.9 per cent. This is higher than the UK standard corporate tax rate, due to the higher tax rates suffered by the Group's non-UK operations but broadly in line with the weighted average nominal tax rate of 32.0 per cent for 2001.

Shareholder return and dividends

Diluted earnings per share before goodwill amortisation were 33.4 pence, up from 30.4 pence in the prior year. The Board has proposed a total dividend of 14.0 pence per share, a rise of 9.4 per cent over last year. Over the last ten years we have maintained compound annual growth rates of 10.8 per cent in diluted earnings per share and 11.3 per cent in dividends. The total dividend for the year is →

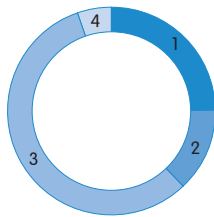
Sources of funding 2001

1. Operating activities
2. Share capital issued for cash
3. Increase in net borrowings



Application of funds 2001

1. Dividends and interest
2. Taxation
3. Acquisitions
4. Capital expenditure



covered 2.1 times by earnings after goodwill amortisation.

Shareholders' funds

Shareholders' funds have increased by £83.3 million (€162.7 million) to £684.5 million (€1,119.2 million) through £50.2 million (€81.0 million) of retained profits and £41.2 million (€66.5 million) of shares issued to fund acquisitions.

Cash flow and investment in the business

Operational cash flow (i.e. cash flow after working capital movements) amounted to £234.6 million (€378.4 million) compared to £157.4 million (€258.3 million) in the previous year as a result of higher operating profits, the UK debtor securitisation and good working capital control.

Treasury and risk management

The objectives of the Group's treasury function are to ensure that there is sufficient liquidity to meet foreseeable needs, to invest cash assets safely and profitably and to reduce or eliminate financial risk. Group Treasury operates policies and procedures that are periodically reviewed and approved by the Board and which are subject to Group Internal Audit reviews. It transacts in relation to underlying

business requirements and is expected to contribute to the profitability of the Group, through efficient management of all treasury activities. It does not operate as a profit centre in its own right.

One of the key financial ratios on which the Group is most focused is maintaining levels of interest cover that are commensurate with an implied investment grade debt rating. The Board policy is to maintain long-term interest cover of around five times on a pre-goodwill basis. This level may temporarily fall where the Group has undertaken a strategically important investment in any year. The Group has the advantage of operating in a business environment that is not subject to the same degree of swings in demand that are experienced in other sectors of the economy. Together with a prudent policy on interest rate hedging, this enables the Group to predict interest cover to a high level of accuracy. The Board's policy is to hedge against adverse movements in interest rates by requiring that the interest cost on about 60 per cent of average projected borrowings over a three-year horizon is fixed or capped.

Liquidity and funding

We have continued to pursue our policy of prudent financing from →

a portfolio of sources. During the year we maintained the stringent management of our debt portfolio, while using our equity to meet part of the consideration of the investment in Hedef, and loan notes to fund an element of our retail development in the UK. All sources of funding and indebtedness are included in the Group's financial statements.

At 31 December 2001, the Group had net borrowings of £781.4 million (€1,277.6 million), and securitised loans of £267.8 million (€437.9 million). This shows an increase of £119.9 million (€225.2 million) in our net borrowings and £95.3 million (€163.5 million) in securitised loans. This was primarily caused by debt funded acquisitions being greater than the cash generated by the business after financing costs. To help minimise refinancing risk, the debt strategy adopted by the Group is to increase, whenever possible, the maturity profile of its borrowings. At the year-end, 34 per cent of borrowings fall to be repaid between two years and five years and 27 per cent in more than five years. In addition we have the flexibility to use undrawn committed facilities to cover another 12 per cent of borrowings. This has been achieved through the diversification of funding

sources into debt capital markets. In November 2001, the Group successfully placed a second series of notes into the US Private Placement market, raising €224 million on a swapped basis in 10 year committed funds.

In August 2001, the Group further diversified its liquidity sources through a debut issue of £100 million of secured floating rate notes, due August 2006. These AAA-rated notes are listed on the Luxembourg Stock Exchange and are backed by UK wholesale and retail (prescription) receivables. The notes are shown on the balance sheet in accordance with accounting standards through the adoption of linked presentation. Further details may be found in note 14 to the financial statements.

Interest rate management

The Group's interest rate exposure is managed by the use of fixed and floating facilities and by the use of interest rate swaps and caps to hedge the exposure of floating rate facilities to interest rate movements.

Currency risk management

The Group manages its balance sheet exposure to the impact of foreign exchange fluctuations by hedging its foreign currency

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net assets with borrowings denominated in the same currency and the use of cross currency swaps.

Approximately 32 per cent of the Group's earnings after goodwill amortisation generated in 2001 was earned in currencies other than sterling of which 94 per cent was in Euro and consequently the Group's reported profit can be affected by currency movements. The Group does not transact specific financial instruments to hedge this translation risk. The borrowings to finance the relatively higher working capital requirements in certain Euro-denominated markets gives rise to higher interest expenses, which provide a natural hedge against translation exposure.

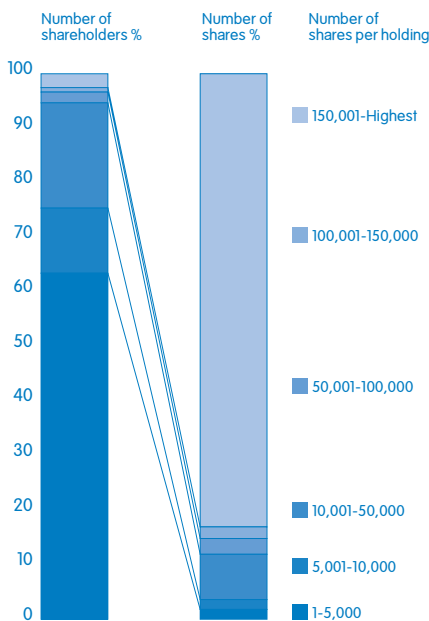
The Group has a policy of hedging foreign currency denominated transactions, including dividends receivable, by entering into forward exchange sale and purchase contracts where these transaction exposures arise.

Share price

The Alliance UniChem share price ranged from a low of 478 pence to a high of 594 pence during the financial year. On 31 December 2001, the mid-market price was 518 pence, giving a market capitalisation of £1.7 billion on that date. →

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Analysis of shareholders at 18 March 2002



Accounting policies and standards

The principal accounting policies used by the Group are shown in note 1 to the financial statements. This year the Group has made additional disclosures in respect of the defined benefit pension schemes operated in the UK, The Netherlands and France, in line with the developing practice. There is an aggregate deficit of £10 million or 1.4 per cent of the Group's net assets.

The Euro

Those Group companies affected by the launch of European Economic and Monetary Union have successfully addressed its operations and financial impact and were fully prepared for the introduction of Euro-denominated notes and coins in January 2002. The total costs of this project amounted to about £1 million (€1.6 million).

Acquisitions

The Group operates strict procedures for the evaluation of acquisitions. All acquisitions are subject to detailed pre-acquisition appraisal to ensure they fit with the Group's strategy and required levels of expected financial return. All investments are reviewed in

a post-investment audit process culminating in a presentation to the audit committee. The majority of acquisitions achieve the targets set in the pre-acquisition appraisal; those few that do not are subject to more detailed review with the management team concerned to find corrective measures and improve the approval process.

Auditors

The Group has a policy of not awarding management consultancy assignments to its auditors except where they have specific knowledge not available to others. The Group has a preference to use its auditors for due diligence assignments on potential acquisitions where their knowledge of the industry can provide insights useful in assessing the target company. Tax-related work is shared between a small number of selected firms including the auditors of the Group. ○