

Markets and divisional highlights

Alliance UniChem's strategy is to consistently grow shareholder value over an extended period of time by focusing on its key areas of expertise within the healthcare market, namely pharmaceutical wholesaling and retail pharmacies. In countries where regulations permit and it makes economic sense to do so, Alliance UniChem seeks to operate wholesale and retail pharmacy businesses alongside one another.

Alliance UniChem aims to grow its businesses organically through consistently delivering superior customer service, utilising its expertise in margin management and by obtaining productivity savings and synergies from managing its businesses closely together. This is combined with a strong emphasis on working capital efficiency and cash generation to fund profitable expansion.

In addition to organic growth, Alliance UniChem's strategy is to grow through the acquisition of businesses and associate interests, both in existing and new geographical markets, applying strict financial criteria for all investments.

Market environment and regulatory framework

The European healthcare markets in which the Alliance UniChem Group operates are forecast to continue to exhibit long-term relatively stable and manageable growth. This reflects socio-demographic trends across Europe which show an ageing population and rising quality of life expectations in old age.

These trends are placing increasing and operational demands on healthcare systems, resulting in continuing growth in prescription medicine volumes. Prescription medicines across Europe are primarily paid for by national governments, either directly to the retail pharmacy or via an intermediate body, patients sometimes having to make a co-payment, depending in some instances upon either their income or the product being prescribed.

Governments across Europe are continually seeking ways to curtail the annual growth in healthcare expenditure, including expenditure on prescriptions. They do however realise that high quality healthcare in the community, including the treatment of ailments using medicines, is typically more cost-effective than hospitalisation and surgery.

In recent years governments have sought to curtail the growth in their expenditure on prescription medicines by using a variety of tools such as:

- cutting the reimbursement price of branded ethical drugs;
- promoting the substitution of branded ethical drugs with their lower priced generic equivalent (typically reimbursing at the generic price and giving the dispensing pharmacist the right of substitution);
- delisting from reimbursement lists products deemed to have limited medical benefits;
- introducing more patient co-payments for prescription medicines;
- requiring manufacturers to be more thorough in demonstrating the medicinal benefits of their products prior to their being listed for reimbursement.

Markets

The wholesale markets in which our businesses operate grew year on year, we estimate, by around 2.5% in value on a constant currency basis, this growth being weighted on the basis of our wholesale revenue. This compares with estimated market growth of 4.5% in 2004. In almost all our markets growth rates were below those forecast at the beginning of 2005. In 2006 we forecast that our wholesale markets will grow in value by around 2.5%, the same as in 2005, reflecting regulatory measures recently announced in France and Spain which we expect will offset better forecast growth in the UK once we are beyond the anniversaries of the Department of Health's Pharmaceutical Price Regulation Scheme (PPRS) price cuts and lower drug tariff for generics which took place in the first half of 2005.

The long-term trends have continued in 2005. The value growth in the market driven by the introduction of higher priced new pharmaceuticals is being offset by the growth in generics.

In 2005 we estimate that generics comprised around 20% of our total wholesale market in volume terms, weighted on the basis of our wholesale volumes, this percentage typically being significantly higher in our markets in Northern Europe. During the year, penetration of generics grew in all our markets, the rate of growth being particularly strong in Italy, Norway and Spain. We anticipate this percentage continuing to rise as more products come off patent and generic penetration increases in Southern Europe.

Alliance UniChem network



The overall level of parallel trade in Europe was lower than in 2004, mainly due to manufacturers' quotas and other initiatives restricting product availability for export. Importing into the UK was further constrained by the impact of the PPRS price cuts at the beginning of January 2005 which reduced the price of branded pharmaceutical products by an average of 7%, resulting in fewer price differentials between the UK and certain other countries. Most manufacturers took the opportunity to modulate the PPRS price cuts on their products, reductions being larger on products where parallel importing was previously prevalent.

Retail markets, weighted on the basis of our retail revenue, grew year on year, we estimate, by around 1.5% in value on a constant currency basis. This was below the estimated market growth rate of 4% in 2004 and lower than our forecast at the beginning of 2005 due to lower growth rates in all retail markets. In 2006 we forecast that our retail markets will grow in value by around 4% as we expect the UK retail market to grow in 2006 once we are beyond the anniversaries of the PPRS price cuts and lower drug tariff for generics.

Divisional highlights for the year ended 31 December 2005

	Revenue £million	Operating profit* £million	Year on year growth	
			Revenue %	Operating profit* %
Wholesale				
– Northern Europe	2,913.1	92.2	+0.5	+3.1
– Southern Europe	5,821.0	77.4	+2.4	+0.4
Intra-segment	(46.8)	–	n/a	–
Wholesale	8,687.3	169.6	+1.8	+1.9
Retail	1,337.3	112.9	+9.4	+18.5
Corporate	–	(21.5)	–	n/a
Intra-group	(853.4)	–	n/a	–
Group	9,171.2	261.0	+3.1	+7.1
Share of associates' revenue and operating profit	1,965.3	70.8	+15.1	+53.6
Total	11,136.5	331.8	+5.0	+14.5

*Operating profit comprises profit from operations before share of associates' post tax earnings and exceptional items as classified by Alliance UniChem (comprising costs in relation to the proposed merger, profit on disposal of businesses and profit on disposal of/(amounts written off) investments)