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**Q2 12 Analyst Script Final**

Thank you, Tony.

I will cover the Core P&L for the second quarter...with an emphasis on the key drivers of operating profit and margin.

I'll briefly touch on restructuring.

I'll comment on our cash performance, and cash distributions to shareholders.

And finally, I will close with our thoughts on guidance for the full year.

**Operating Profit and Margins**

I will now turn to the second quarter P&L. I will focus here on Core margins and profit. The press release does, of course, contain the statutory numbers and a detailed reconciliation to the Core measures. When I refer to growth rates, they will all be on a constant currency basis.

Revenue was \$6.7 billion. Core gross margin in the quarter was 79.9 percent of sales. That is down 190 basis points compared with the second quarter last year, largely due to a change in product mix following the loss of exclusivity on key brands.

Core SG&A expense was down 18 percent compared with the second quarter last year. We continue to exercise discipline in managing these costs and see meaningful benefits from restructuring being realised, whilst at the same time creating headroom to support new product launches. The absence of Astra Tech also contributed to the lower SG&A in the quarter. The excise tax component of US healthcare reform amounted to 2.8 percent of SG&A expense in the second quarter.

Core other income of \$182 million was unchanged compared with the second quarter last year. There were some moving parts—royalty income from Entocort in the US was lower following generic entry, but it was largely offset by income from the Zomig marketing agreement with Impax Laboratories in the US.

That leads to a Core Pre-R&D operating margin of 49.9 percent of revenue, down 190 basis points compared to second quarter last year, on lower revenue and gross margin.

Core R&D investment in the quarter was just under \$1.1 billion. That is 4 percent lower than last year. Benefits from restructuring have more than offset increased spend on projects to progress the pipeline, including the additional projects from the Amgen collaboration.

For the full year, I expect Core R&D expense will be lower than last year in constant currency terms, both on an overall basis and if you exclude the impact from intangible impairments from both periods.

This leads to a Core operating profit of \$2.3 billion in the quarter, 27 percent lower than last year. Core operating margin was 34.1 percent of revenue, down 430 basis points.

## **Productivity/Restructuring**

Turning to our Productivity programme, in the first half we have charged \$907 million of the projected \$2.1 billion total cost for phase 3 of restructuring, with the split between Cost of Goods, R&D and SG&A as laid out in the table.

We still expect most of the restructuring costs associated with the programme we announced back in February will be taken in 2012, and we remain on track for delivering the estimated \$1.6 billion in annual benefits by the end of 2014.

## **Cash**

Cash generated from operating activities in the first half was \$2.8 billion, in line with last year. With disciplined management of working capital and lower tax spend, we were able to offset the lower operating profit and contributions to the pension fund.

In terms of cash distributions to shareholders, we maintain our commitment to our progressive dividend policy. The Board has recommended a first interim dividend of \$0.90...as you will recall the aim is to set the first interim at around 1/3 of the full year dividend for the prior year, which in 2011 was \$2.80 per share.

Subject to market conditions and business needs, the target for net share repurchases in 2012 remains \$4.5 billion. We completed gross repurchases of \$1.9 billion in the first half and issued \$0.3 billion in consideration of share option exercises, giving a net figure of \$1.6 billion.

In terms of the cash profile for the second half, we have the pending Amylin payments-- Approximately \$3.4 billion to expand the collaboration, subject to a final true-up; plus a further \$135 million related to the option to establish equal governance rights over key strategic and financial decisions regarding the collaboration.

We will be paying the first interim dividend in September.

The other potential call on cash this year was the Merck Shares option, or the Second option as it is also called.

We have reached an agreement with Merck to amend certain provisions related to the Second Option and now intend to exercise the option in 2014, barring unforeseen circumstances. We have agreed on the valuation methodology and the option exercise price, which will now be around \$407 million, representing \$327 million value for the PPI products (subject to a true-up) and around \$80 million for the profit allocation in the Partnership. The expected payments to Merck will be capitalised and amortised as set out in Note 5 of the Second quarter financial statements.

One other accounting item to note. With effect from 1 January 2013, we are updating our definition of Core financial measures to exclude all amortisation charges and intangible asset impairments. The new definition will provide better clarity of the impact from amortisation and impairment charges, which are included in Core results under our current

definition. In addition, it will aid comparability of our results versus the peer group. We will publish an update on this with our third quarter and nine months results.

## **Future Prospects/Guidance**

Finally, turning to guidance.

We knew that 2012 was going to be a challenging year in revenue terms, particularly with the loss of exclusivity on several products, most notably Seroquel IR.

We expect government interventions on pricing to continue at the upper bounds of what we anticipated, both in Europe and in the US.

We continue to vigorously defend our intellectual property. We prevailed in the US trial on the Seroquel XR patent, and we have also had positive outcomes in Spain and in the Netherlands. But we have also had an adverse judgment in the UK, and some at risk launches in Europe. There are rulings pending in other jurisdictions.

On balance, our revenue assumptions are unchanged. We expect a decline in revenue for the full year to be in the range of the low to mid-teens in constant currency terms, including any residual impact from supply issues.

The other items of guidance are also unchanged, with the exception of tax. With the tax benefit realised in the second quarter, we now expect the effective tax rate for the full year to be around 20 percent—that is around 2 points lower than our previous guidance. As we mentioned in the press release, we did have a probability weighted view of the likely realisation of this benefit when we revised our guidance at the first quarter results. This, taken together with the dilutive impact of the expansion of the diabetes alliance with BMS, means our Core EPS target for the full year remains unchanged, in the range of \$5.85 and \$6.15.

Whilst currency was negative to Core EPS in the first half compared with last year, it was broadly neutral versus our guidance, which was based on the January 2012 average exchange rates. Our forward look to guidance takes no account of the likelihood that average exchange rates for the remainder of the year may differ materially from the January 2012 average.

In summary, our revenue performance reflects many of the expected challenges that provided the framework for our guidance update in the first quarter.

We are seeing the benefits of disciplined cost management. Our restructuring programmes are delivering real benefits, through lower R&D and SG&A costs, that help provide the headroom for the investments in business development, our pipeline and new launches.

We continue to focus on shareholder returns with our progressive dividend policy and share repurchases.

I will now hand back to Simon, who will chair the Q&A session.