Dechra Pharmaceuticals PLC Annual Report and Accounts 2003

About Dechra

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Our Business

An emerging pharmaceutical business, focused on the veterinary market

Our Strategic focus

The continuing development of our veterinary pharmaceutical portfolio

Increasing own branded pharmaceutical penetration into international markets

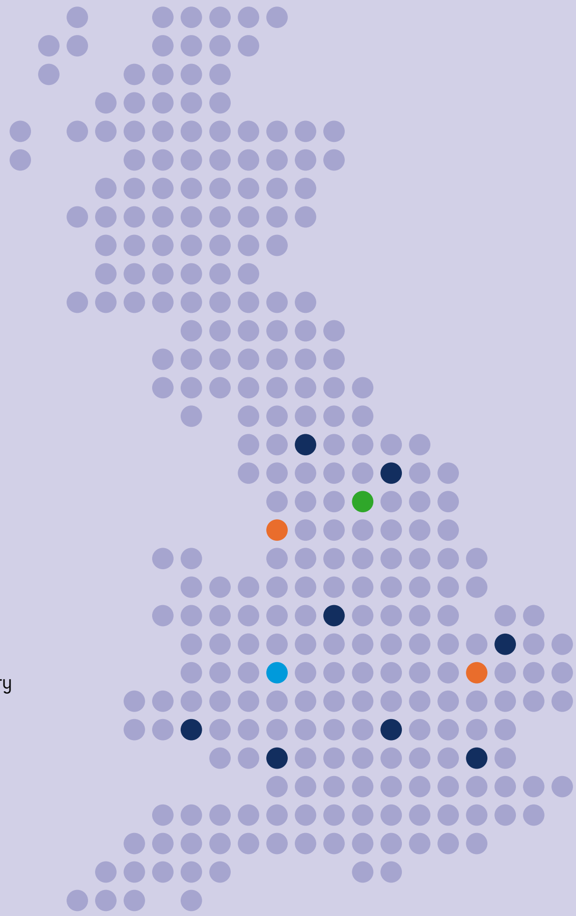
Increasing revenues from our existing businesses focusing on high margin products and services

National Veterinary Services
UK market leader in the supply of pharmaceuticals and added value services to the veterinary profession

Arnolds Veterinary Products
Veterinary sales and marketing specialists, and market leaders in the supply of licensed branded pharmaceuticals, instruments and equipment to the veterinary profession worldwide

NationWide Laboratories/ Cambridge Specialist Laboratory Services
NWL is a multi-disciplined independent commercial veterinary laboratory
CSLS is the UK's leading veterinary endocrine specialist

Dales Pharmaceuticals
Licensed manufacturer of human and veterinary pharmaceuticals for Arnolds and third party customers



Highlights

- Further progress in product licensing and development — key to future growth
- North American product development and marketing rights secured for Vetoryl
- Arnolds — fastest growing of the Top 20 veterinary pharmaceutical companies
- Laboratory businesses — strong earnings enhancing performance
- NVS — significantly improved H2 operating margin, market share remains above 42%

	Pre-exceptional items and goodwill amortisation	Post-exceptional items and goodwill amortisation
Turnover	£179.3m	£179.3m
Profit before tax	£6.75m	£5.7m
Earnings per share	9.39p	7.52p
Total dividend per share	4.12p	4.12p

Chairman's Statement

"Key to future strategic growth is the development of new licensed products that can be marketed and sold both in the UK and internationally . . ."

Michael Redmond, Chairman

INTRODUCTION

The Group made an encouraging start to the financial year being reported, producing a good first quarter performance with National Veterinary Services reporting sales up 11% in that period. We were then affected by a decline in market growth and the second quarter results were flat on the previous year. As previously reported, this shortfall in sales, together with increased overheads due to the expansion programme of the central warehouse facility at Stoke, a trebling of insurance premiums and an aggressive pricing environment, impacted on net margins during the first half.

As the veterinary market continued to remain flat during the first two months of the second half, key initiatives were introduced to enhance operating margins which resulted in an improved second half performance compared to the first half. Our added-value services provided through National Veterinary Services continued to perform well. Our overall market share remains in excess of 42%.

Sales of our own branded pharmaceuticals through Arnolds have grown significantly during the year, principally through the success of recent introductions to Arnolds' licensed veterinary product portfolio, including our own developed products, Vetoryl® and Felimazole®. We have also continued to expand sales of core pharmaceuticals through our major European distributors.

Our laboratory businesses, NationWide Laboratories and Cambridge Specialist Laboratory Services, produced a strong earnings enhancing performance with results being at their best ever. Customer orders, benefiting from synergies created through the Group structure, were increased by 25%.

Our manufacturing operation, Dales Pharmaceuticals, saw turnover increase by £2.7million, reflecting the integration of Anglian Pharma. A number of initiatives and challenging new performance targets were introduced at this facility in January this year and although progress has been made, the full benefits of these actions in efficiency and productivity will not be realised until the current financial year ending 30 June 2004.

COMPETITION COMMISSION INQUIRY

The Competition Commission findings from its inquiry into the supply of prescription only medicines in the UK were reported in April of this year. The Commission provisionally concluded in the statement of issues released on 16 April 2002 that a scale monopoly exists in favour of National Veterinary Services, our principal trading subsidiary.

In our statement issued on 20 September 2002, we stated that this was "a purely technical finding and did not imply that the situation operates or might be expected to operate against the public's interest". I am pleased to report that the Competition Commission's findings issued on 11 April 2003 confirm this statement. The remedies from the Report are unlikely to have any material impact on the performance of Dechra.

We continue to believe that Dechra is in a strong position to service and support the requirements of our existing and new customers when change is implemented.

PRODUCT DEVELOPMENT AND LICENSING

Key to the future strategic growth of the Group's business is the development of new licensed products within its veterinary drug

portfolio that can be marketed and sold both in the UK and internationally. The lead time for development, regulatory approval through to marketing and distribution of veterinary drugs can take up to five years. As we widen our exposure to this part of our business, our product development expenditure will increase accordingly.

During the year ended June 2003, we have made significant investments in product licensing and marketing authorisations. In particular, the Group made an initial payment of £784,000 as part of its exclusive rights to the intellectual property in Trilostane, the active compound in the Group's proprietary drug Vetoryl, in respect of animal health applications in the USA and Canada.

FINANCIAL HIGHLIGHTS

Group turnover increased 5.4% from £170.2 million to £179.3 million, whilst operating margin (pre-goodwill amortisation and exceptional items) reduced from 5.15% to 4.55%. Pre-tax profit (pre-goodwill amortisation and exceptional items) was £6.75 million against £7.60 million in 2002. Adjusted earnings per share (pre-goodwill amortisation and exceptional items) was 9.39 pence (2002: 10.59 pence). Net debt at the end of the period remained broadly in line with last year at £15 million.

DIVIDEND

The Board is recommending a maintained final dividend of 2.75 pence per share (2002: 2.75 pence per share). This, together with the interim dividend of 1.37 pence per share, gives a total for the year of 4.12 pence per share. The total dividend is covered 2.3 times by profit after taxation before exceptional items and goodwill amortisation. If approved at the Annual General Meeting on 23 October 2003, the final dividend will be paid on 26 November 2003 to shareholders on the Register as at 31 October 2003.

PEOPLE

In May, we welcomed Neil Warner to the Main Board as a Non-Executive Director. Neil is Finance Director at Chloride Group PLC, a position he has held since 1997. His technical skills in financial control, tax and treasury enhance and strengthen the scope of the Board in delivering continuous improvement across the Group.

At the same time, in order to service our customers and drive our strategy forward, we made a number of additional senior operating management appointments across the Group and these are covered under the Chief Executive's Review.

Following the AGM in October, Mike Annice will step down from the Main Board in order to allow him to concentrate on the ongoing development of Dales.

On behalf of the Board and shareholders, I would like to welcome all new staff who joined the Group during the last year whilst also thanking all our people across the Group's subsidiaries for all the hard work and dedication that they have demonstrated throughout the year.

PROSPECTS

We believe that the Group has made operational improvements and progress in delivering our strategy despite the challenges the business faced both commercially and economically in the year ended 30 June 2003.

Following our actions to improve operational efficiencies around the Group, together with the further development and growth of our own licensed and branded pharmaceuticals portfolio both in the UK and internationally, we remain cautiously optimistic that the Group will continue to see an improved trading performance in the year ending 30 June 2004.

Michael Redmond
Chairman
2 September 2003

Chief Executive's Review

"... all our businesses are now stronger in management and infrastructure to deliver and support future growth opportunities."

Ian Page, Chief Executive

Throughout the year, our business and the veterinary market in which we trade have faced significant economic and commercial challenges. Although the Group results are lower than we originally envisaged at the start of the financial year, I believe that all our businesses are now stronger in management and infrastructure to deliver and support future growth opportunities. Furthermore, significant advancements in delivering our key strategic objectives have been made which we believe will deliver strong medium and long term growth.

DISTRIBUTION AND SERVICES

National Veterinary Services ("NVS") is the UK's leading veterinary wholesaler and a supplier of added value services to veterinary practices. NVS had a solid start to the year; however, in the second quarter sales declined. External market data also showed a downturn in the overall market during this period. The shortfall in budgeted sales at NVS combined with the other factors detailed in the Chairman's statement, coupled with a general lack of confidence within veterinary practices created by the Competition Commission Report, impacted on our performance. Initiatives implemented in the second half to respond to these challenges have subsequently resulted in an improvement in gross margins, efficiency and cost controls which is reflected in a much better second half performance.

The year has seen a number of significant developments at NVS. We have developed a stronger management team with the appointment of a new divisional Finance Director, Dan Shipman, Sales and Marketing Director, Sheryl Greentree, and Buying Director, Colin Higham. The skills of the new team have been instrumental in implementing the changes that will deliver future growth.

Vetcom® Windows, our in-house developed practice management software system, continues to provide operational benefits to customers and has now been installed in almost 100 veterinary practices. The advanced practice management facilities will assist veterinary practices throughout the UK in developing good business practices and allow them to drive their businesses forward. Within the year we also developed Vetcom "Handyscan", a barcode-based ordering system which was launched in June 2003. The system enables veterinary practices to improve their stock control through barcode technology and allows them to place orders directly with NVS or to download data into the Vetcom practice management system. NVS are continuing to develop leading veterinary information technology solutions for veterinary practices.

In July 2003 we introduced the NVS own branded "Valu" range of quality products at economic prices, initially focusing on disposables such as surgical gloves, bandages, swabs and syringes. These products will assist veterinary practices to reduce their daily

National Veterinary Services

"The skills of the new team have been instrumental in implementing the changes that will deliver future growth."

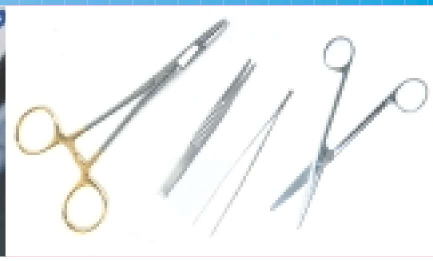
costs of essential items whilst at the same time will provide NVS with a competitive edge over other wholesalers, which will allow us to deliver improved margins to both ourselves and our veterinary customers.

The warehouse expansion and site development, which doubled capacity, is now complete. The improved facilities will lead to greater efficiency and improved quality systems as we move forward. To support our high levels of service to customers we have enhanced our Customer Services, introducing extended office opening hours and installing new customer call centre technology.

NVS is in the process of implementing an extension to our semi-automated picking system which will include an automatic weight checking system. This will deliver operating efficiencies and improved order accuracy.

Arnolds®

Arnolds Veterinary Products



"... 51% of all veterinary practices are now using Vetoryl on a regular basis."

SALES AND MARKETING

Arnolds Veterinary Products ("Arnolds"), the Group's veterinary sales and marketing business based in Shrewsbury, is a market leader in a number of specialist pharmaceutical sectors and also supplies a wide range of instruments and consumable products. Arnolds' growth in pharmaceuticals at 32.2% was the highest growth seen by any of the top twenty veterinary pharmaceutical suppliers within the UK. This was predominantly driven by our new products; however, further good growth was also achieved on our mature market leading products such as Equipalazone®, Intubeaze® and Intra-epicaine®. Two of our most recently licensed products, Vetoryl and Felimazole, are making an increasingly significant contribution.

Vetoryl achieved sales in excess of £1 million during the year and achieved a high market penetration, with 51% of all veterinary practices now using Vetoryl on a regular basis. High levels of brand recognition have been gained through an ongoing education process as we continue to assist veterinarians in the diagnosis and treatment of dogs with Cushing's disease. Felimazole has achieved significant growth during the second half since we announced that a new licence has been granted for the product to be used for life-time stabilisation of feline hyperthyroidism. Sales by the end of the financial year were approaching £0.5 million with sales in the fourth quarter in particular indicating an uplift in sales in the coming year.

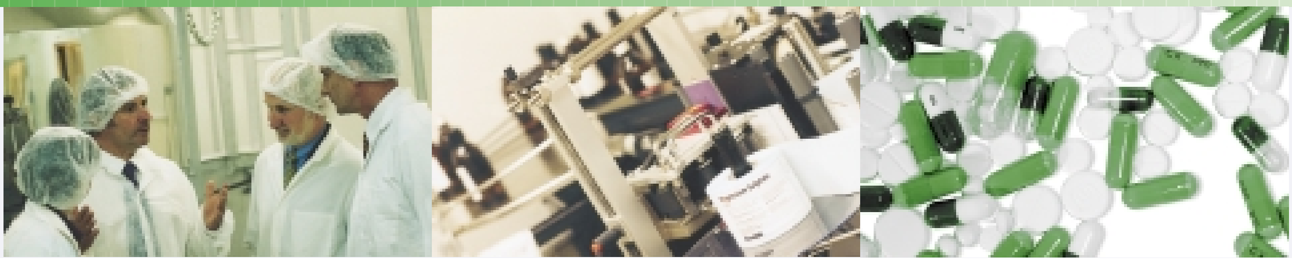
Key structural changes have been implemented throughout the year. In October 2002, UK Sales and Marketing was divided into two business units, one with specific focus on the sale of capital equipment and consumables, the other, being the larger team, focusing on the sale of pharmaceuticals. This has been a significant factor in driving forward exceptional growth.

Towards the end of the year we merged our Export and UK administration operations into one cohesive unit. This has resulted in better customer service through faster response times and improved communications. Operational efficiencies are now also being realised from these initiatives.

We have also strengthened the technical team with the appointment of a second veterinary adviser and have added further resource into the Regulatory and Licensing department.

In a very competitive market we have achieved growth within a number of sectors of our instruments, disposables and agency products. Our agency agreements, namely Portex®, 3m® and Global Veterinary Products (formerly Cook Veterinary Products) have continued to deliver good results. The overall performance from this part of the business has been offset by a decrease in sales of Braun® sutures, an agency agreement which has seen erosion in sales as a result of cheap imports.

DALES PHARMACEUTICALS



"... the business has been successful in retaining all its key customers and has also gained new accounts during the course of the year."

MANUFACTURING

Dales Pharmaceuticals ("Dales"), the Group's manufacturing operation based in Skipton, North Yorkshire has experienced a demanding year.

Following the acquisition of Anglian Pharma Plc in April 2002, its manufacturing operations were transferred to our site in Skipton, allowing an increased service offering in the manufacturing and production of liquids, ointments and solid dose pharmaceuticals. Following the commissioning of a new liquids products facility at Dales, the transfer was completed to schedule in January 2003. The enlarged business, which involved the manufacture of over 60 products and the associated licence variations, and which doubled the headcount at Skipton, has taken longer to integrate than originally anticipated. Although Dales has now made significant progress towards full integration, the benefits have not been realised within the year.

Although the year has seen many challenges for Dales it is pleasing to note that this business has been successful in retaining all its key customers and has also gained new accounts during the course of the year. These include a new third party contract manufacturing account where commercial production started at the end of June 2003. This £0.5 million contract with a major pharmaceutical company involved several months of technical transfer work carried out in collaboration with the customer.

"The extension to the facilities allows the laboratory to process diagnostic samples more efficiently . . ."

LABORATORY SERVICES

The Group's laboratory businesses are NationWide Laboratories ("NWL"), a full service provider of clinical and diagnostic pathology services to the veterinary profession in the UK, and Cambridge Specialist Laboratory Services ("CSLS"), a provider of highly specialised diagnostic services with a principal focus on veterinary endocrinology and in high quality immunoassay measurement techniques.

Both NWL and CSLS have made considerable progress in the year with turnover increasing 35% on the year immediately preceding acquisition. Operating margin also improved across both businesses, resulting in operating profit more than doubling.

The past financial year has seen improvements across the laboratory businesses, with growth in customer orders, a considerable expansion of facilities, the strengthening of both the technical specialist and management teams together with the synergistic benefits from across the Group as a whole.

NWL has updated and increased its testing repertoire, particularly in respect of veterinary endocrinology and has also enhanced its schedule of UKAS accredited test procedures. The extension to the facilities allows the laboratory to process diagnostic samples more efficiently and comfortably whilst providing capacity for significant growth of the business in the future.

In April 2003, we took the step of rebranding the trading style of the business, from 'North Western Laboratories' to 'NationWide Laboratories'. This change better reflects the true nature of the geographical area now served by the laboratory, across the UK.

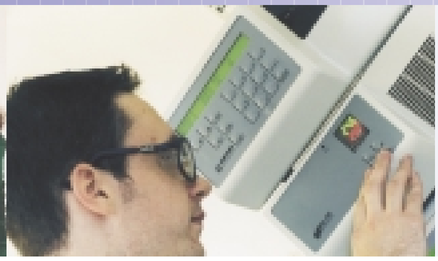
During the year we secured new contracts for both businesses, partly reflecting the synergistic relationships that have developed with other Group companies. NWL has been able to widen its services to its clients by offering the collection of diagnostic specimens through the NVS distribution network whilst at the same time NWL benefited from sales leads from NVS territory managers. Additionally, NWL has assisted NVS in sourcing lower cost laboratory products for resale.

NWL and CSLS have benefited from the appointment of Dr Peter Graham as Managing Director. Peter is one of the world's leading veterinary endocrine specialists, and joined us from Michigan State University, where he ran the world's largest dedicated veterinary diagnostic endocrinology laboratory.

We have further developed and integrated the laboratory businesses into the Group and have identified a number of new product and service opportunities which will enhance future growth.

PRODUCT DEVELOPMENT AND LICENSING

During the year we successfully secured a number of partnerships and licensing agreements. The ongoing product development programme continues to deliver good opportunities for medium and long-term growth.



"Product development expenditure is directly related to recognised quantifiable projects that have a high probability of being delivered to market."

Within the UK the long-term usage licence for Felimazole has been granted. Two further products have been submitted for licensing and are expected to deliver products for marketing within the next twelve months. Additional licences for new dosing regimes for both Felimazole and Vetoryl are also being prepared; these licences, once granted, will further increase market penetration of these key products.

In May 2003, the Group entered a joint venture partnership with LAB International® Inc. ("LAB"), a Canadian-based drug development company. The partnership will run for an initial period of five years and strengthens the Group strategy to further develop and accelerate our licensed branded veterinary pharmaceutical portfolio. Under the partnership, LAB provides research studies on selected therapeutic agents whilst Dechra is responsible for the formulation and regulatory submission of these products. I am pleased to report that we have already started work on the development of two generic veterinary pharmaceuticals.

Of even greater significance is the sub-licence agreement concluded in May 2003 with Bioenvision® Inc. to develop Vetoryl for future marketing in the USA and Canada. This veterinary drug, which as I have already indicated has been successfully developed and marketed in the UK by Arnolds, is highly effective in the treatment of Cushing's disease, an endocrine disorder in dogs. Vetoryl's introduction into the North American market, which is some ten times larger than the UK, represents a substantial opportunity for Dechra.

The current Vetoryl licence submission is still being developed with a view to submitting the product for mutual recognition within Europe during the current financial year. Negotiations are at an advanced stage with a major pharma company as a potential marketing partner for the EU market.

Product development expenditure is directly related to recognised quantifiable projects that have a high probability of being delivered to market. Several new projects are being investigated, including two potential cross-over products from human pharma and an equine laminitis research project being conducted in association with the Royal Veterinary College.

SUMMARY

Although we have experienced a difficult and demanding financial year, we have continued to invest significantly in product development, which is key to delivering our medium and long-term growth strategy. With strengthened management teams across the Group, NVS now moving forward again and Arnolds and the laboratory businesses continuing to deliver strong results, the Group is well positioned to achieve sustained organic growth.

Ian Page
Chief Executive
2 September 2003

Financial Review

"… sales of our own branded pharmaceuticals, our key strategic focus, increased by 32.2% compared to last year."

Simon Evans, Group Finance Director

OPERATING RESULTS

The Group achieved a profit before tax, exceptional items and goodwill amortisation of £6.75 million for the year, a decrease of 11.3% compared to last year calculated on the same basis. The results reflect a difficult year in which the Group has suffered the double impact of challenging market conditions combined with a number of cost increases.

Group turnover increased by 5.4% (which included the full year effect of acquisitions made in 2002) compared to 8.3% on a like-for-like basis last year. This principally reflected slower sales growth at NVS. However, sales of our own branded pharmaceuticals, our key strategic focus, increased by 32.2% compared to last year.

Gross margin improved from 12.1% to 12.8%. This was due to the relatively high gross margins of the acquired businesses and the benefit of the margin improvement initiatives undertaken at NVS during the second half of the financial year.

Operating costs before exceptional items and goodwill amortisation increased by 26.0% above last year. This represented 8.3% of sales compared to 6.9% last year.

The principal cost increases were:

- insurance premiums increased from £219,000 to £573,000
- product development expenditure increased from £525,000 to £997,000
- acquisitions added £1.2 million to the cost base
- expansion of the NVS facility added £250,000 to the cost base

Excluding the above, the cost increase above last year was 6.7% which represented further investment in people and systems to strengthen our core businesses.

Overall, Group operating margin (before exceptional items and goodwill amortisation) reduced slightly from 5.15% to 4.55%.

NET INTEREST CHARGE

The net interest charge increased to £1.4 million from £1.2 million, principally reflecting the additional borrowings to partly fund the acquisitions made in the latter part of the year ended 30 June 2002.

Interest was covered 5.8 times by operating profit before goodwill amortisation and exceptional items.

EXCEPTIONAL ITEM

The exceptional item comprised the costs of integrating the operations of Dales and Anglian onto a single site at Skipton together with the costs of reorganising the Group's trading operations into a single statutory entity.

TAXATION

The current year tax charge on profit before exceptional items and goodwill amortisation is 30.4%, slightly higher than the standard UK corporation tax rate of 30%. The difference is principally due to certain expenses that are not allowable for tax. There was a credit in respect of prior years of £91,000 and this reduced the overall tax charge on profit before exceptional items and goodwill amortisation to 29.1%.

EARNINGS PER SHARE AND DIVIDEND

Adjusted earnings per share (before exceptional items and goodwill amortisation) was 9.39p. The proposed final dividend is maintained at 2.75p per share making a total maintained dividend for the year of 4.12p. The total dividend is covered 2.3 times by adjusted profit after taxation (before exceptional items and goodwill amortisation).

SUMMARY OF RESULTS

	2003 Before exceptional items and goodwill amortisation	2003 After exceptional items and goodwill amortisation	2002 Before exceptional items and goodwill amortisation	2002 After exceptional items and goodwill amortisation
Turnover	£179.3m	£179.3m	£170.2m	£170.2m
Operating profit	£8.2m	£7.1m	£8.8m	£8.5m
Profit before tax	£6.75m	£5.7m	£7.6m	£7.3m
Earnings per share	9.39p	7.52p	10.59p	10.12p
Dividend per share	4.12p	4.12p	4.12p	4.12p

CAPITAL EXPENDITURE

Total capital expenditure for the year was £1.6 million. The main items included the addition of a liquids manufacturing suite at Dales to allow the transfer of production of the acquired Anglian business and an expansion of the NationWide Laboratories premises to enable future growth.

In addition, the Group spent £784,000 including legal costs as the first stage payment for the acquisition of the rights to Vetoryl in the North American market. Further stage payments of $0.75 million and $3.0 million are due on the submission of a new animal drug application to the US Food and Drug Administration and the granting of a marketing authorisation respectively.

During the year the Group entered into a sale and leaseback of its van and car fleet. This raised net proceeds of £0.5 million after settling outstanding hire purchase liabilities.

CASH FLOW AND NET DEBT

The Group achieved an increased operating cash flow to £6.5 million (2002: £6.4 million) despite the lower level of profits this year. This reflects the continued strong focus on cash management.

The second half of the financial year saw a strong cash inflow which reduced net debt by £4.3 million compared to 31 December 2002. Net debt at 30 June 2003 was £15.0 million, broadly similar to the figure at 30 June 2002.

BALANCE SHEET AND SHAREHOLDERS' FUNDS

Shareholders' funds increased to £7.47 million during the year reflecting the retained profit.

Working capital increased from £8.9 million to £11.1 million. Stock turn improved from 7.8 times to 9.0 times due to a reduction in stocks at NVS, whilst debtor days were broadly similar to last year at 46 days (2002: 45 days). Creditor days reduced from 66 to 58 due to a reduction in creditors inherited from the Anglian acquisition, together with a reduction in stock purchased under deferred payment terms.

CAPITAL POLICY

It is the policy of the Company to maintain an appropriate balance between equity financing and debt financing so as to reduce the weighted average cost of capital of the Company but without over-gearing.

TREASURY POLICY

Overall treasury policy is set by the Board and monitored by myself. The Company does not speculate on short-term interest rate or exchange rate movements. All of the Group's borrowings, with the exception of hire purchase contracts, are currently at floating rates.

No borrowings are denominated in foreign currencies and the Group has no significant foreign exchange exposure.

LIQUIDITY MANAGEMENT

The Group's cash position is monitored on a daily basis by myself. The Group has available overdraft and revolving credit facilities from the Bank of Scotland for its day-to-day working capital requirements.

Further information on Financial Instruments is shown in note 19 to the financial statements.

S D Evans

Simon Evans
Group Finance Director
2 September 2003

Board of Directors

EXECUTIVE DIRECTORS

Ian Page
CHIEF EXECUTIVE
Aged 42, Ian joined the Group's principal trading subsidiary NVS at its formation in 1989 and was appointed Managing Director in 1998. He joined the Board in 1997 and became Chief Executive in November 2001. Ian has played a key role in the development of the Group's growth strategy. Prior to joining the Company, he gained extensive knowledge and experience through various positions he held within the pharmaceutical and medical arena.

Simon Evans BCom, ACA
GROUP FINANCE DIRECTOR
Aged 39, Simon qualified as a Chartered Accountant in 1988 and spent seven years at KPMG. He joined NVS in 1992 and, was appointed Group Finance Director in 1997 following the MBO.

Ed Torr
EXECUTIVE DIRECTOR
Aged 43, Ed joined NVS as Sales Director in 1997 and was part of the MBO team. In 1998, he was appointed Managing Director of Arnolds and Dales. Prior to joining the Group, he worked within the animal healthcare sector for a number of companies including ICI, Wellcome and Alfa Laval Agri.

Michael Annice BSc (Hons), MRPharmS
EXECUTIVE DIRECTOR
Aged 43, Mike graduated from The School of Pharmacy at Aston University in 1980. Prior to joining Dales in 1990 as Site Manager he worked within the Hospital Pharmacy Service, Glaxo and SSS International (formerly Cupal Pharmaceuticals). He was appointed Production Director at the time of the MBO and joined the Board in 1997. Mike was appointed Managing Director at Dales in March 2002.

NON-EXECUTIVE DIRECTORS

Michael Redmond
NON-EXECUTIVE CHAIRMAN
Aged 59, Michael joined the Group as a Non-Executive Director in April 2001, and was appointed Chairman in July 2002. He has extensive pharmaceutical industry experience having begun his career with Glaxo and through senior positions with Schering Plough Corporation. In 1991, he joined Fisons plc and in 1993 was appointed to the Board as Managing Director of the Group's Pharmaceuticals Division. Michael left Fisons in 1995 following its takeover by RPR. He is currently also a Non-Executive Director and Chairman at Microscience Ltd, Synexus Ltd and Arakis Ltd and a Non-Executive Director at Strakan Ltd. Former Non-Executive Directorships include Biocompatibles International plc, CeNeS plc and Cantab Pharmaceuticals plc.

Malcolm Diamond MBE
SENIOR NON-EXECUTIVE DIRECTOR
Aged 54, he joined the Board in August 2000 prior to the Group's flotation in September of the same year. Malcolm retired after 18 years as Chief Executive of Trifast plc in March 2002 and has continued to be involved with the Company until September 2003. Currently, he is also advising a number of private businesses on their strategic planning, management development programmes and marketing initiatives. He was, until its takeover in March 2002, a Non-Executive Director of Sytner Group plc and was formerly a Member of both the CBI Smaller Quoted Companies Working Committee (SQC) and the National Manufacturing Council.

Neil Warner BA, FCA, MCT
NON-EXECUTIVE DIRECTOR
Aged 50, Neil joined the Board in May 2003. He is Finance Director at Chloride Group PLC, a position he has held since 1997. Prior to this, he spent six years at Exel PLC (formerly Ocean Group PLC) where he held a number of senior posts in financial planning, treasury and control. Previous to this, he worked for Balfour Beatty PLC (formerly BICC Group plc), Alcoa and PricewaterhouseCoopers.

Stephen Whitehouse FCCA
COMPANY SECRETARY
Aged 55, Stephen has been with the Group since 1989 and was part of the MBO team. He was Finance Director at Arnolds and was appointed Company Secretary at flotation in 2000. Prior to this, he worked for twelve years at GKN Sankey and ten years at British Oxygen.

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Corporate Governance

COMPLIANCE WITH THE COMBINED CODE

The Directors note the issue of the revised Combined Code by the Financial Reporting Council on 23 July 2003 and will report on the Company's compliance as and when required (not effective for current period).

In the opinion of the Directors, the Company has complied throughout the period with Section 1 of the existing code with the exception of the following items (references in brackets are to provisions in the Combined Code):

a) Composition of the Remuneration Committee. Until May 2003 the Remuneration Committee consisted of two Non-Executive Directors; after this date it has consisted of three Non-Executive Directors (B.2.2).

b) Composition of the Audit Committee. Until May 2003 the Audit Committee consisted of two Non-Executive Directors (both of whom were independent); after this date it has consisted of three Non-Executive Directors (who are all independent) (D.3.1).

This compliance was achieved following the appointment of N.W. Warner as Non-Executive Director in May 2003.

BOARD OF DIRECTORS

The details of the Board of Directors are shown on page 12 and in the Directors' Report on page 24. There is a clear division of responsibilities between the Chairman and Chief Executive. The Board consists of an Independent Non-Executive Chairman, two other Independent Non-Executive Directors and four Executive Directors (including the Chief Executive).

At least two members of the Board are required to retire from office by rotation at the Annual General Meeting subject to all Directors having submitted themselves for re-election every three years.

The Board considers that all the Non-Executive Directors are independent of Management and free of any business or other relationship which could materially interfere with the exercise of their independent judgement, and are not dependent on the Company for their primary source of income or paid by the Company in any capacity other than a Non-Executive Director. In addition, an independent Director will not have previously been a Senior Manager of the Company, and will not have participated in the Company's incentive bonus schemes or pension schemes.

The Board considers M.M. Diamond to be the senior independent Director.

CONDUCT OF BOARD MEETINGS

The Board normally has twelve regular monthly Board Meetings including two meetings where the full year and half year results are dealt with. Strategy meetings are convened as required with at least one meeting per year. In addition, the Board has three standing committees — the Audit, Remuneration and Nomination committees, the details of which are shown on page 15.

The Board has reserved to itself powers relating to matters which it considers significant to the Group's business, operational and financial risks. These include the approval of corporate policies, plans and budgets, acquisitions and disposals of companies or businesses; major investment and financial decisions; appointments to the Board; and major management or organisational changes.

At all Board meetings an agenda is established reflecting the Directors' responsibilities. This comprises reports from the Chief Executive, Finance Director and Operating Company Directors, reports on the performance of the business, major items of strategic planning, investments and significant policy issues. The Board considers at least annually the strategic plans of the Group and individual businesses. Periodically, the Directors receive presentations from management concerning key areas of the Group's operations.

Full year and interim results are reviewed by the audit committee and the Board and approved prior to publication. Other price sensitive information may be published only with the approval of the Board of Directors.

Each Director is entitled on request to receive information to enable him to make informed judgements and adequately discharge his duties. In addition, all Directors have access to the advice and services of the Company Secretary and senior managers generally, and may take independent professional advice at the Company's expense in connection with their duties. The Company Secretary is responsible to the Board for ensuring that Board procedures are followed and that applicable rules and regulations are complied with. Any question of the removal of the Company Secretary is a matter for the Board as a whole.

All newly appointed Directors receive an induction programme to the Company including Corporate Governance training and background to the Company. All Directors are encouraged to keep up to date on all matters relevant to the Group and attend briefings and seminars as appropriate.

The following committees, all of which operate within written terms of reference, assist the Board.

THE AUDIT COMMITTEE

Members: N.W. Warner (Chairman), M. Redmond, and M.M. Diamond.

The Audit Committee generally meets twice a year. The terms of reference of the Audit Committee include the following responsibilities:

- To review and advise the Board on the interim and annual financial statements.
- To review with the external auditors the nature and scope of their audit, the results of that audit, any control issues raised by them and management's responses.
- To make recommendations as to the appointment and remuneration of the external auditors and any question of their resignation or removal.
- To review and oversee the Company's approach to internal control and risk management.
- To review the use of Auditors on non-audit work.
- To review the requirement for an Internal Audit function.

THE REMUNERATION COMMITTEE

Members: M.M. Diamond (Chairman), M. Redmond and N.W. Warner.

The Directors consider that the Company has fully complied with Schedule A of the Directors' Remuneration Report Regulations 2002.

The Remuneration Committee meets at least twice a year and sets the pay and benefits of the Executive Directors, approves their terms and conditions and bonus schemes, having regard to performance. A report on the remuneration of Directors appears on pages 17 to 22.

The terms of reference of the Remuneration Committee include the following responsibilities:

- To make recommendations to the Board on executive remuneration packages.
- To determine targets for any performance related pay schemes.
- To determine the policy for and scope of any pension arrangements for Executive Directors.
- To approve contracts of employment with Executive Directors.
- To determine the terms of Executive Directors' compensation packages.
- To ensure that shareholders should be invited to approve the policy set out in the Directors' remuneration report at the Company's AGM.

THE NOMINATIONS COMMITTEE

Members: M. Redmond (Chairman), M.M. Diamond, and N.W. Warner.

The Nominations Committee normally meets once per year and oversees the plans for management succession, recommends appointments and reappointments to the Board and considers the structure and composition of the Board generally.

INTERNAL CONTROL

The Directors are responsible for the Company's system of Internal Control, which aims to safeguard the Company's assets, to ensure that proper accounting records are maintained to ensure compliance with statutory and regulatory requirements and the effectiveness of, and efficiency of operations including the assessment and management of risk. A system of internal control is designed to manage rather than eliminate risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance particularly against material misstatement or loss.

The Company has a well-established framework of internal financial and operational control for identifying, evaluating and managing the risks faced by the Company.

In complying with the Internal control requirements of the Combined Code, the Directors have taken guidance from the Institute of Chartered Accountants in England and Wales publication "Internal Control: Guidance for Directors on the Combined Code" ("the Turnbull Guidance"). As a result, the Board prepares and updates a six-monthly thorough review of relevant risk areas and systems of internal control. The review is structured by business area and key risk strategy. The current review was prepared to 30 June 2003.

The Company's key systems of internal control include:

Business Plans
Business plans provide a framework from which annual budgets and forecasts are agreed with each business unit, including financial and strategic targets against which business performance is monitored. The plans are reviewed by Executive management, and then by the Board for ultimate approval. Actual performance during the year is monitored monthly against budget, forecast and previous year. Full year forecasts are updated at regular intervals during the year based on trended historical data and realistic forecasts.

Investment Approval
The Group has clear requirements for the approval and control of expenditure. Strategic investment decisions involving both capital and revenue expenditure are subject to formal detailed appraisal and review according to approval levels set by the Board. Operating expenditure is controlled within each business with approval levels for such expenditure determined by the individual businesses.

Management Structure
Executive management are responsible for the identification, evaluation and management of the significant risks applicable to their business areas. The risks are assessed on a periodic basis and may be associated with a variety of internal and external sources.

The Company and its business units operate control procedures designed to ensure complete and accurate accounting of financial transactions, and to limit the loss of assets or fraud. Measures taken include physical controls, segregation of duties in key areas, and internal reviews and checks.

Key functions such as tax, treasury, insurance, legal and personnel are controlled centrally.

RISK CONTROL

Responsibility for monitoring the Group's system of internal control rests with the Board. It is assisted by the Audit Committee, which reviews the interim and annual reports provided to shareholders, the audit process and the systems of internal control and risk management, the latter by way of consideration of the Board's updated progress report and action plan regarding internal controls.

Whilst the Board recognises this does not constitute an internal audit function, it believes that due to the size of the Group this review provides sufficient comfort as to the controls in place. The audit committee reviews the requirement for an internal audit function annually.

The Board has reviewed the effectiveness of the Group's internal control systems from the period from 1 July 2002 to the date of approval of the financial statements by means of the updated progress report and internal controls action plan.

The Board reviews the operation and effectiveness of its control assessment on a regular basis.

INVESTOR RELATIONS

A rolling programme of meetings between institutional shareholders and Executive Directors is held throughout the year, in addition to the annual and interim results presentations and the Annual General Meeting to foster mutual understanding of objectives. Such meetings are conducted so as to ensure protection of share price sensitive information that has not already been made generally available to the Company's shareholders. Similar guidelines also apply to communications between the Company and parties such as Financial Analysts, brokers and the press. The Company also organises site visits on a periodic basis. All members of the Board usually attend the Annual General Meeting. The Chairmen of the Audit Committee, Remuneration Committee and Nominations Committee will normally be available to answer shareholders' questions at that meeting. Notice of the meeting, together with a letter from the Chairman and the Annual Report and financial statements, are posted to shareholders not fewer than 23 days prior to the date of the Annual General Meeting. The package sent to shareholders includes a summary of the business to be covered at the Annual General Meeting, where a separate resolution is prepared for each substantive matter. Where a vote is taken on a show of hands, the level of proxies received for and against the resolution and any abstentions will be disclosed at the meeting.

GOING CONCERN

After consideration of budgets and other financial information, the Directors are satisfied that the Group is in a sound financial position with adequate resources to continue in operation for the foreseeable future. For this reason, the Group's financial statements have been prepared on the basis that the Group is a going concern.

Directors' Remuneration Report

This report is presented in accordance with the relevant provisions of the Combined Code on Corporate Governance (the "Combined Code") and the Directors' Remuneration Report Regulations 2002 (the regulations). The regulations require the Company's auditors to report on certain "auditable" information required to be included in the Directors' Remuneration Report. The audited information has therefore been separately highlighted.

The Board is responsible for the Group's remuneration policy and setting non-executive fees, although the task of determining and monitoring the remuneration packages of Executive Directors has been delegated to the Remuneration Committee.

REMUNERATION COMMITTEE

The Remuneration Committee is responsible for ensuring that the remuneration packages provided to Executive Directors are appropriate to individual levels of experience, responsibility and performance, are consistent with the Company's remuneration policy, and are in line with the principles of good corporate governance. The committee considers remuneration packages payable to executives at comparable companies when setting remuneration of Executive Directors and also considers pay structures around the Group.

The Remuneration Committee comprises solely Non-Executive Directors: M.M. Diamond, M. Redmond and N.W. Warner. The committee usually meets twice a year and is chaired by M.M. Diamond. During the year the Group Chief Executive attended all of these meetings in order to assist on matters concerning remuneration of other senior executives within the Group. The Chief Executive was not present during the part of the meetings where his own remuneration was discussed.

The committee appointed DLA during the year to provide it with external advice in establishing a new long-term incentive plan for Executive Directors and senior management (see below). The committee will, if considered appropriate, also seek independent external advice relating to the broader remuneration package but did not do so in the year ended 30 June 2003.

REMUNERATION POLICY

The Company's policy on Directors' remuneration for the forthcoming year is that its remuneration packages should be capable of attracting, rewarding and retaining Executive Directors whilst being arrived at responsibly and fairly, when compared with similar organisations.

The remuneration packages of Executive Directors are structured to include a performance related element linked to corporate and individual objectives. Both the Executive Share Plan and the Executive Bonus Scheme are performance related. Bonuses are not pensionable.

Remuneration for Non-Executive Directors is limited to salary only with no performance related element.

The Company's policy on the remuneration of all Directors is reviewed annually.

Once remuneration has been approved by the Board, the Chairman, where considered appropriate, will consult the Company's principal shareholders regarding remuneration issues. This remuneration policy is included in the Annual General Meeting agenda for shareholder approval.

COMPONENTS OF THE REMUNERATION PACKAGE

Basic Salary

The basic salary of each Executive Director is determined taking into account the responsibilities and performance of the individual together with independently furnished information on rates for similar jobs in comparable industry sectors. Details of salaries, bonuses and benefits paid to Executive Directors are included in the table headed "Summary of Remuneration" shown on page 21.

Non-Executive Directors have a service contract for an initial 12 month period which is thereafter terminated by either party giving 12 months' notice. Participation in share option schemes, bonus schemes or entitlement to a pension is not allowed under the service contract.

Benefits in kind

Executive Directors receive other benefits, including the use of a fully expensed car, medical cover and life insurance, which overall provide a competitive package comparable to that provided by other comparable quoted companies.

Pensions

The scheme is a funded, contributory, Inland Revenue approved money-purchase occupational pension scheme and is contracted into the State Earnings Related Pension Scheme.

Share Option Schemes

The Company operates the Executive Share Plan, the Approved Share Option Scheme, the Unapproved Share Option Scheme together with a savings related share option scheme. The key features of the schemes are described on page 19.

Directors' Remuneration Report continued

Executive Incentive Plan
In the forthcoming year the Company will operate, subject to shareholder approval, the Executive Incentive Plan, a new share based incentive plan.

The following table illustrates eligibility under each of these schemes in the forthcoming year:

	SAYE Scheme	Executive Share Plan	Approved Scheme	Unapproved Scheme	Executive Incentive Plan
I.D. Page	✓	—	—	—	✓
S.D. Evans	✓	—	—	—	✓
E.T.W. Torr	✓	—	—	—	✓
M.D. Annice	✓	—	—	—	✓

Executive Incentive Plan
Under this new plan the Remuneration Committee will make awards to senior executives over a specified number of shares in the Company, with vesting to individuals being subject to the achievement of performance targets. The first target is based on Total Shareholder Return (TSR) over a specified measurement period expressed as an annual percentage return over that period. The TSR would be calculated and compared to the TSR's of other companies in the FTSE Small Cap Index. If the Company is ranked in the top quartile of the list of TSR's achieved by the companies in the FTSE Small Cap Index throughout the measurement period, all of the shares over which an award had been made would vest.

If the TSR of the Company was ranked in the second quartile then a specified number of shares over which the award had been made would vest in the ownership of the relevant participant. The number of shares that vested for a participant would be determined by reference to a straight line graph which ensured that half of the shares over which the award had been made would vest on the achievement of a TSR that placed the Company at the bottom of the second quartile and ownership of all of the shares would vest on an achievement of a TSR that placed the Company at the top of the second quartile.

If the TSR of the Company was ranked in the third or fourth quartile then none of the shares over which an award had been made would vest and the relevant participant would not be entitled to any of the shares.

In addition to the TSR performance target, no award will vest unless in the opinion of the Remuneration Committee the underlying financial performance of the Company has been satisfactory over the measurement period.

The maximum length of the measurement period for any award will be four years. If, however, after three years the TSR achieved by the Company over a three year period is sufficient to indicate a comparative performance that would rank the Company in the second quartile or above, the measurement period will be three years.

It is intended that, for Executive Directors, the initial awards will represent 100% of basic salary with awards in subsequent years being capped at 50% of basic salary.

Executive Bonus Scheme
This scheme rewards Executive Directors for achieving operating efficiencies and profitable growth in the relevant year by reference to challenging, but achievable operational performance targets derived at the beginning of the financial year. The bonus is calculated on formulae which are determined each year by the Remuneration Committee.

In the case of I.D. Page and S.D. Evans, the bonus target for 2003 was based solely on Group performance, whereas the bonus of E.T.W. Torr and M.D. Annice was based equally upon Group and Business Unit performance.

In respect of the year ended 30 June 2003, a 5% bonus would be payable on achieving in excess of 95% of target, with 10% becoming payable on meeting target. Thereafter for each 1% achieved above target, a further 1% of salary is payable, capped at 30% of annual salary. No bonus payments are pensionable.

Executive bonuses in the forthcoming year will be payable on the fulfilment of the prescribed conditions set out below.

	Bonus Payable for achievement of target (% of Salary)	Proportion Payable on Group/ Business Unit Performance	
		Group	Business Unit
I.D. Page	30%	100%	—
S.D. Evans	25%	100%	—
E.T.W. Torr	25%	100%	—
M.D. Annice	20%	30%	70%

In addition, each further 1% achieved above 105% of target attracts a further bonus of 1% of salary capped at a maximum additional 10% of annual salary.

THE EXECUTIVE SHARE PLAN

The Executive Share Plan was adopted by the Company in addition to three share option schemes (the Approved Scheme, the Unapproved Scheme and the SAYE scheme — all detailed below). As a consequence of the imposition of very demanding performance targets, the Executive Share Plan was intended to motivate Executive Directors to increase significantly the market value of the Company for the benefit of the shareholders. In addition, it was expected that the plan would play a major part in retaining the services of the Directors and Executives who have demonstrated, over recent years, their drive and commitment to the Company and its shareholders.

The Executive Share Plan is administered by the trustees of the Dechra Pharmaceuticals PLC Employment Benefit Trust under the authority of the Remuneration Committee.

Any Executive Director who is participating in the Executive Share Plan will not be granted options under the Approved Share Option Scheme or the Unapproved Share Option Scheme.

There are two performance criteria that are attached to awards made under the Executive Share Plan, both of which must be satisfied before any shares can vest.

Firstly, the share price of the Company in the six months following the third anniversary of the award must be at least 220% of the Initial Award Value for at least 90 days (the Initial Award Value being 120p for the awards made on 14 September 2000 or an amount equal to the three day average closing mid-market value of an ordinary share on the date that any further awards are made).

Secondly, the earnings per ordinary share of the Company must exceed inflation by a compound 15% per annum in the three financial years following an award.

No awards were made in the year to 30 June 2003.

Outstanding awards made previously under the scheme are shown on page 21. These awards are share options with an aggregate exercise price of £1 and will vest to the relevant Director if the performance criteria detailed above are achieved within the required timescales.

Other than in circumstances which the Remuneration Committee considers exceptional, any further awards can only be made in the 42 day period following the announcement of the interim or final results of the Company.

APPROVED AND UNAPPROVED SCHEMES

In accordance with the terms of both schemes, employees, unless participating in the Executive Share Plan, may receive options to buy Company Shares at market price of those shares at the date of grant. Options can be exercised, subject to certain criteria relating to the performance of earnings per share, between three and ten years after grant.

Approved Scheme

No awards were made under this scheme.

Unapproved Scheme

The Remuneration Committee made awards on 11 April 2003 to key employees within the Group. No Executive Directors received awards under this scheme.

The performance target to be achieved under the Unapproved Share Option Scheme has been set by the Remuneration Committee in accordance with the scheme rules and is based on the growth in the earnings per share over a consecutive three year period (commencing no earlier than the beginning of the accounting period immediately preceding the grant of the option) being greater than the percentage increase in the Retail Prices Index for the same period by at least 12 per cent.

SAVE AS YOU EARN (SAYE) SCHEME

Under a savings related scheme, options may be offered to employees including Executive Directors, enabling them to subscribe for ordinary shares in the Company at the market price of those shares at the date of grant less a discount up to a maximum of 20%, subject to participation in a designated savings scheme. There are no specific performance criteria attaching to these options.

The Company granted options under the Dechra Pharmaceuticals PLC SAYE scheme on 3 April 2003.

The table on page 22 provides an analysis of outstanding SAYE Directors' share options.

Directors' Remuneration Report continued

CONTRACTS OF SERVICE

Each Executive Director has a service contract with the Company which contains details regarding remuneration, restrictions and disciplinary matters.

Executive Directors are appointed on contracts terminable by the Company on not more than 12 months' notice and by the Director on 6 months' notice.

Non-Executive Directors are appointed for an initial term of one year, continuing thereafter until terminated by either party giving not less than 12 months' notice.

Details of Directors' service contracts and notice periods are set out below:

Name	Commencement	Notice Period (Director)	Notice Period (Company)
M. Redmond	25 April 2001	12 months	12 months
I.D. Page	23 August 2000	6 months	12 months
S.D. Evans	23 August 2000	6 months	12 months
E.T.W. Torr	23 August 2000	6 months	12 months
M.D. Annice	23 August 2000	6 months	12 months
M.M. Diamond	23 August 2000	12 months	12 months
N.W. Warner	2 May 2003	12 months	12 months

There are no expiry dates applicable to either Executive or Non-Executive Directors' service contracts.

The Company may in its absolute discretion at any time after written notice of termination has been given by either party lawfully terminate the service contract by paying to the Director an amount equal to his salary entitlement for the unexpired period of notice together with an amount representing the fair value of any other benefits to which the Director is contractually entitled for the unexpired period of notice (subject in either case to deduction at source of income tax and national insurance contributions).

In the event that the service contract is terminated part way through any financial year the Director shall not be entitled to any bonus in respect of that financial year.

Non-Executive Directors' compensation entitlements are confined to 12 months' remuneration entitlement.

Individual Directors' eligibility for the various elements of compensation are set out below:

Name	Salary	Bonus	Benefits
M. Redmond	12 months	n/a	n/a
I.D. Page	12 months	Nil	12 months
S.D. Evans	12 months	Nil	12 months
E.T.W. Torr	12 months	Nil	12 months
M.D. Annice	12 months	Nil	12 months
M.M. Diamond	12 months	n/a	n/a
N.W. Warner	12 months	n/a	n/a

Where applicable, payment of this compensation would be in full and final settlement of all claims other than in respect of share options and pension arrangements.

In an appropriate case the Directors would have a regard to the departing Director's duty to mitigate loss, except in the event of dismissal following a change of control of the Company.

Other than as described above, there are no express provisions within the Directors' service contracts for the payment of compensation or liquidated damages on termination of employment.

No awards of compensation for loss of office or any other reason have been made to any person, whether a Director or a former Director, during the year.

No compensation payments were made to Executive or Non-Executive Directors during the year.

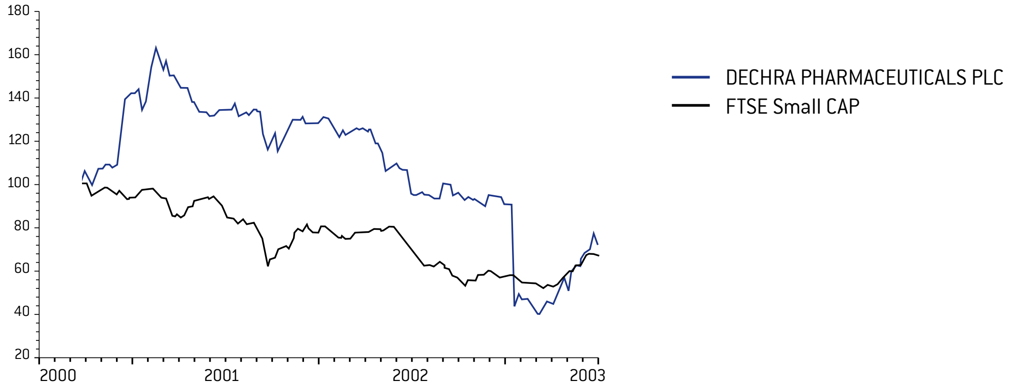
Directors' Shareholdings

The beneficial interests of the Directors in office at 30 June 2003 and their families in the share capital of Dechra Pharmaceuticals PLC at 30 June 2003 was as follows:

Shareholdings	Ordinary Shares 2003	Ordinary Shares 2002
M. Redmond	35,000	10,000
I.D. Page	592,167	592,167
S.D. Evans	663,000	663,000
E.T.W. Torr	342,414	342,414
M.D. Annice	596,334	596,334
M.M. Diamond	5,000	5,000
N.W. Warner	—	—

Total Shareholder Return
The graph below shows the total shareholder return performance of the Company over the past three years compared with the total shareholder return over the same period for the FTSE Small Cap Total Return Index. The FTSE Small Cap Index is considered to be an appropriate index as the Company is a constituent of that index.

Total Shareholder Return Indices



The information shown above relates to the three-year period since the Company's flotation in September 2000.

AUDITED INFORMATION
The auditors are required to report on the information contained in the remainder of this report.

Summary of Remuneration

	Salaries & Fees £'000	Bonuses £'000	Other Benefits £'000	Total 2003 £'000	Total 2002 £'000
Executive Directors					
I.D. Page (Chief Executive)	145	—	15	160	141
S.D. Evans	100	—	10	110	116
E.T.W. Torr	92	2	15	109	106
M.D. Annice	85	—	12	97	85
G.B. Evans (resigned 5 November 2001)*	—	—	—	—	251
Non-Executive Directors					
M. Redmond (Chairman)	40	—	—	40	20
M.M. Diamond	22	—	—	22	20
N.W. Warner (appointed 2 May 2003)	3	—	—	3	—
P.J. Redfern (deceased 23 January 2002)	—	—	—	—	14
	487	2	52	541	753

* Includes £194,000 compensation for loss of office

SHARE OPTIONS
Awards made previously under the Executive Share Plan are as follows:

	Exercise Dates	As at 30 June 2002 and 30 June 2003
I.D. Page	2004–2010	166,666
S.D. Evans	2004–2012	166,666
E.T.W. Torr	2004–2010	166,666
M.D. Annice	2004–2012	166,666

Directors' Remuneration Report continued

Executive Share Plan
No options were exercised, lapsed or granted during the year. Share options have an aggregate exercise price of £1 and vest subject to achieving the performance criteria described above.

Directors' entitlements under savings related share option schemes are as follows:

	Exercise Dates	Exercise Price	At 1 July 2002 Total	2003 Cancelled	2003 Granted at 39p	At 30 June 2003 Total
I.D. Page	2006	158p	10,680	(10,680)	—	—
	2008	39p	—	—	42,115	42,115
S.D. Evans	2004	158p	6,131	—	—	6,131
E.T.W. Torr	2004	158p	2,452	—	—	2,452
	2005	129p	4,418	—	—	4,418
M.D. Annice	2006	158p	4,272	(4,272)	—	—
	2008	39p	—	—	14,538	14,538

Directors' interests in share options remains unchanged at 2 September 2003.

The middle market price for the Company's shares on 30 June 2003 was 87.50p and the range of prices during the year was 47.50p to 136.50p.

PENSION ENTITLEMENT
All Executive Directors were members of the Dechra Holdings Limited money purchase scheme throughout the year. Contributions made by Dechra Pharmaceuticals PLC on behalf of the Executive Directors during the year are based on a percentage of pensionable salary and were paid as follows:

	Age	Contributions 2003 £000	Contributions 2002 £000
I.D. Page	42	17	14
S.D. Evans	39	12	11
E.T.W. Torr	43	11	7
M.D. Annice	43	10	9
G.B. Evans (resigned 5 November 2001)		—	6
		50	47

By order of the Board

M.M. Diamond
Chairman Remuneration Committee
2 September 2003

Social, Ethical and Environmental Responsibilities

The Board has received adequate information and has not identified any risks that affect the Company's short and long term value.

ENVIRONMENTAL POLICY

Dechra Pharmaceuticals PLC acknowledges the importance of good environmental controls. It is the Company's policy to comply and exceed environmental legislation currently in place, adopt responsible environmental practices and is committed to minimising the impact of its operations on the environment.

This is being achieved within our manufacturing unit by complying with and bettering effluent discharge standards into local water supplies which is monitored by Yorkshire Water Authority and standard operating procedures which ensure contaminated waste is disposed of only under strict controls. Exhaust air is fully filtered before discharge.

The Group complies with the Waste Packaging Obligations Regulations and maintains a modern fleet of low CO_2 emission diesel vehicles, which are subject to a leasing arrangement and are replaced every three years.

Dechra will continue to review its environmental controls and encourage its own staff, suppliers and customers to achieve similar high standards.

HEALTH AND SAFETY POLICY

Dechra Pharmaceuticals PLC attaches great importance to the health and safety of its employees and the public. The management are responsible and committed to the maintenance, monitoring and promoting of a policy of Health and Safety at work, to ensure the care and well-being of its employees and on-site visitors. A written Health and Safety policy manual is in use throughout the Group.

Individual sites operate Health and Safety Committees, which meet regularly to consider Health and Safety issues and ensure risk assessments are carried out where necessary.

Dechra's commitment to Health and Safety will be achieved by adhering to the following policies:

- We will meet and where necessary exceed the requirements of all legislation.
- We will ensure the involvement and consultation of all employees to achieve the implementation of our policy by risk assessment, continuous improvement and the monitoring of resources.

Directors' Report

The Directors present their Annual Report and audited financial statements for the year ended 30 June 2003.

PRINCIPAL ACTIVITY

The Group manufactures and sells pharmaceuticals and also markets and sells veterinary equipment and related services including computer systems, predominantly to the UK veterinary market, but also to overseas markets. The Company acts as a holding company to all Group subsidiaries.

SHARE CAPITAL

Details of the changes in share capital are shown in note 21 to the financial statements.

RESULTS AND DIVIDENDS

The results for the year are set out on page 28. The Directors recommend the payment of a final dividend of 2.75p per share which, if approved by shareholders, will be paid on 26 November 2003 to shareholders registered at 31 October 2003. An Interim Dividend of 1.37p per share was paid on 9 April 2003 making a total dividend for the year of 4.12p (2002: 4.12p). The total dividend payment is £2,093,000 (2002: £2,069,000). A retained profit of £1,740,000 (2002: £2,989,000) is transferred to reserves.

BUSINESS REVIEW AND FUTURE DEVELOPMENTS

A review of the Group's activities during the year and likely future developments are dealt with in the Chairman's Statement, Chief Executive's Review and Financial Review.

DIRECTORS

The Directors who served during the year were as follows:

M. Redmond (Chairman)
I.D. Page
S.D. Evans
E.T.W. Torr
M.D. Annice
M.M. Diamond
N.W. Warner (appointed 2 May 2003)

The interests of the Directors in the share capital of the Company are shown in the remuneration report on pages 17 to 22.

In accordance with the articles of association, M.M. Diamond and S.D. Evans retire by rotation and, being eligible, offer themselves for re-election. N.W. Warner being a new appointee offers himself for election to the Board.

Following the AGM in October, M.D. Annice will step down from the Board. This will mean the structure of the Board is fully compliant with the 'New Combined Code'.

POLITICAL AND CHARITABLE CONTRIBUTIONS

The Group made no political or charitable contributions during the year.

EMPLOYEES

It is the Group's policy to encourage employee involvement as the Directors consider that this is essential for the successful running of the business. The Group keeps employees informed of performance, developments and progress by way of regular team briefing sessions and notices.

It is the Company's policy to provide equal recruitment and other opportunities for all employees, regardless of sex, religion, race or disability. The Group gives full consideration to applications for employment from disabled people, where they adequately fulfil the requirements of the job.

Where existing employees become disabled, it is the Group's policy whenever practicable to provide continuing employment under the Company's terms and conditions and to provide training and career development whenever appropriate.

The Group operates a SAYE share option scheme in which all employees of the Group can participate.

RESEARCH AND DEVELOPMENT

The Group has a structured research and development programme with the aim of identifying and bringing to market new pharmaceutical products. The expenditure on this activity for the year ended 30 June 2003 was £997,000 (2002: £525,000).

SUPPLIERS

The Company does not adhere to any code of practice regarding the payment of suppliers but seeks to agree the terms of payment with suppliers prior to placing business and it is the Company's policy to settle liabilities by the due date. At 30 June 2003, the Group had an average of 68 days (2002: 77 days) purchases outstanding in creditors. The Company had an average of NIL days (2002: NIL days) purchases outstanding in creditors.

SUBSTANTIAL SHAREHOLDINGS

As at 27 August 2003, the Company is aware of the following material interests representing 3% or more of the issued share capital in the Company:

	No. of Shares	% of Shares Held
Threadneedle Asset Management	5,755,000	11.29%
Hermes Pension Management	4,989,864	9.79%
Platinum Fund Managers	2,536,800	4.98%
Montanaro Investment Management	2,180,000	4.28%
Insight Investment	2,056,600	4.03%
3i Asset Management	1,550,000	3.04%

AUDITORS

A resolution to reappoint KPMG Audit Plc as auditors is to be proposed at the forthcoming Annual General Meeting.

By order of the Board

S.P. Whitehouse Secretary

2 September 2003

Dechra House
Jamage Industrial Estate
Talke Pits
Stoke-on-Trent
ST7 1XW

Statement of Directors' Responsibilities

Company law requires the Directors to prepare financial statements for each financial period which give a true and fair view of the state of affairs of the Company and the Group and of the profit or loss for that period. In preparing the financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Company or Group will continue in business.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Independent Auditor's Report to the Members of Dechra Pharmaceuticals PLC

We have audited the financial statements on pages 28 to 46. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

This report is made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company, and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The Directors are responsible for preparing the Annual Report and the Directors' Remuneration Report. As described on page 26, this includes responsibility for preparing the financial statements in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board, the Listing Rules of the Financial Services Authority and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Directors' remuneration and transactions with the Group is not disclosed.

We review whether the statement on pages 14 to 16 reflects the Company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read the other information contained in the Annual Report, including the corporate governance statement, and the unaudited part of the Directors' Remuneration Report, and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

BASIS OF AUDIT OPINION

We conducted our audit in accordance with the Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the part of the Directors' Remuneration Report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Directors' Remuneration Report to be audited.

OPINION

In our opinion:

— the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 30 June 2003 and of the profit of the Group for the year then ended; and

— the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985.

KPMG Audit Plc
Chartered Accountants
Registered Auditor
Birmingham

2 September 2003

Consolidated Profit and Loss Account

For the year ended 30 June 2003

	Note	2003 Before Exceptional Items and goodwill amortisation £'000	2003 Exceptional Items and goodwill amortisation (note 3) £'000	2003 Total £'000	2002 Before Exceptional Items and goodwill amortisation £'000	2002 Exceptional Items and goodwill amortisation (note 3) £'000	2002 Total £'000
TURNOVER	2	179,309	–	179,309	170,202	–	170,202
Cost of sales		(156,319)	–	(156,319)	(149,664)	–	(149,664)
GROSS PROFIT		22,990	–	22,990	20,538	–	20,538
Distribution costs		(7,252)	–	(7,252)	(6,166)	–	(6,166)
Administrative expenses		(7,576)	(1,061)	(8,637)	(5,599)	(295)	(5,894)
Operating profit		8,162	(1,061)	7,101	8,773	(295)	8,478
Net interest payable and similar charges	5	(1,416)	–	(1,416)	(1,170)	–	(1,170)
Profit on ordinary activities before taxation	6	6,746	(1,061)	5,685	7,603	(295)	7,308
Tax on profit on ordinary activities	9	(1,960)	108	(1,852)	(2,308)	58	(2,250)
Profit on ordinary activities after taxation		4,786	(953)	3,833	5,295	(237)	5,058
Dividends	10			(2,093)			(2,069)
Retained profit for the financial year				1,740			2,989
Earnings per ordinary share							
Basic	11	9.39p	(1.87p)	7.52p	10.59p	(0.47p)	10.12p
Diluted	11	9.36p	(1.86p)	7.50p	10.56p	(0.47p)	10.09p

A statement of movements on reserves is given in note 22 to the financial statements.

All amounts relate to continuing operations.

There were no recognised gains and losses other than shown above.

Balance Sheets

As at 30 June 2003

		Group		Company	
		2003	2002	2003	2002
	Note	£'000	£'000	£'000	£'000
FIXED ASSETS					
Intangible assets	12	5,730	5,284	–	–
Tangible assets	13	5,572	6,324	–	–
Investments	14	–	–	4,608	4,619
		11,302	11,608	4,608	4,619
CURRENT ASSETS					
Stocks	15	17,296	19,302	–	–
Debtors	16	28,001	25,822	55,004	46,440
		45,297	45,124	55,004	46,440
CREDITORS: amounts falling due within one year	17	(42,420)	(42,445)	(20,373)	(13,997)
NET CURRENT ASSETS		2,877	2,679	34,631	32,443
TOTAL ASSETS LESS CURRENT LIABILITIES		14,179	14,287	39,239	37,062
CREDITORS: amounts falling due after more than one year	17	(6,708)	(8,538)	(6,639)	(8,200)
NET ASSETS		7,471	5,749	32,600	28,862
CAPITAL AND RESERVES					
Called up share capital	21	510	504	510	504
Shares to be issued	22	–	750	–	5
Share premium account	22	26,783	26,783	26,783	26,783
Merger reserve	22	1,720	994	–	–
Profit and loss account	22	(21,542)	(23,282)	5,307	1,570
TOTAL EQUITY SHAREHOLDERS' FUNDS		7,471	5,749	32,600	28,862

The financial statements were approved by the Board of Directors on 2 September 2003 and are signed on its behalf by:

I.D. Page Director

S.D. Evans Director

Reconciliation of Movements in Shareholders' Funds

For the year ended 30 June 2003

	Group		Company	
	2003	2002	2003	2002
	£'000	£'000	£'000	£'000
At 1 July 2002	5,749	1,010	28,862	28,579
Profit for the financial year	3,833	5,058	5,830	2,341
Dividends	(2,093)	(2,069)	(2,093)	(2,069)
New shares issued	732	1,000	6	6
(Decrease)/increase in shares to be issued	(750)	750	(5)	5
At 30 June 2003	7,471	5,749	32,600	28,862

Consolidated Cash Flow Statement

For the year ended 30 June 2003

	Note	2003 £'000	2002 £'000
NET CASH INFLOW FROM OPERATING ACTIVITIES	24	6,542	6,397
RETURNS ON INVESTMENT AND SERVICING OF FINANCE			
Interest received		62	16
Interest paid		(1,400)	(1,103)
Interest element of finance lease rentals		(46)	(39)
Net cash outflow for returns on investment and servicing of finance		(1,384)	(1,126)
TAXATION			
Corporation tax paid		(2,066)	(2,155)
CAPITAL EXPENDITURE			
Purchase of tangible fixed assets		(1,553)	(2,845)
Purchase of intangible fixed assets		(784)	–
Sale of tangible fixed assets		1,113	141
Net cash outflow for capital expenditure and financial investment		(1,224)	(2,704)
ACQUISITIONS AND DISPOSALS			
Acquisitions of subsidiary undertakings		32	(3,214)
Overdrafts of acquired businesses		–	(429)
Purchase of business		–	(180)
Net cash inflow/(outflow) for acquisitions and disposals		32	(3,823)
EQUITY DIVIDENDS PAID		(2,078)	(1,927)
CASH OUTFLOW BEFORE FINANCING		(178)	(5,338)
FINANCING			
New bank loans		–	3,000
Term loans repaid		(2,842)	(3,364)
Capital element of finance lease payments		(568)	(401)
Net cash outflow from financing		(3,410)	(765)
Decrease in cash in the period		(3,588)	(6,103)
(Bank overdraft)/cash at 30 June 2002		(2,110)	3,993
Bank overdraft at 30 June 2003		(5,698)	(2,110)

	Note	2003 £'000	2002 £'000
RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET DEBT			
Decrease in cash during the period		(3,588)	(6,103)
Cash inflow from new loans		–	(3,000)
Debt repayments		2,842	3,364
Repayment of finance leases		568	401
Change in net debt resulting from cash flows		(178)	(5,338)
New finance leases		(75)	(418)
Loan stock issued		–	(500)
Other non-cash changes		(7)	(8)
MOVEMENT IN NET DEBT IN THE PERIOD		(260)	(6,264)
NET DEBT AT 1 JULY 2002	25	(14,728)	(8,464)
NET DEBT AT 30 JUNE 2003	25	(14,988)	(14,728)

Notes to the Financial Statements

For the year ended 30 June 2003

1. ACCOUNTING POLICIES

The following accounting policies have been applied in dealing with items which are considered material in relation to the Group and parent Company's financial statements.

BASIS OF PREPARATION

The financial statements have been prepared under the historical cost convention and in accordance with applicable accounting standards.

CONSOLIDATION PRINCIPLES

The consolidated financial statements incorporate those of Dechra Pharmaceuticals PLC and its subsidiary undertakings made up to 30 June.

The acquisition method of accounting has been adopted and the results of subsidiary undertakings acquired are included from the date of acquisition.

In accordance with Section 230(4) of the Companies Act 1985, no separate profit and loss account is presented for the Company. The profit for the year dealt with in the accounts of the Company was £5,830,000 (2002: £2,341,000).

TURNOVER

Turnover represents cash and credit sales excluding value added tax and net of discounts allowed.

TANGIBLE FIXED ASSETS AND DEPRECIATION

Depreciation is calculated so as to write off the cost less estimated residual value of tangible fixed assets over their estimated useful lives. The principal rates used are as follows:

Short leasehold property	Period of the lease on a straight line basis
Fixtures, fittings and equipment	10–33$\frac{1}{3}$% on a straight line basis
Motor vehicles	25% on a straight line basis

INVESTMENTS

Investments held as fixed assets are stated at cost less any impairment losses. Where the consideration for the acquisition of a subsidiary undertaking includes shares in the Company to which the provisions of section 131 of the Companies Act 1985 apply, cost represents the nominal value of the shares issued together with the fair value of any additional consideration given and costs. In the Group balance sheet the excess of the fair value of the shares issued as consideration over their nominal value is credited to a merger reserve.

GOODWILL AND INTANGIBLE ASSETS

Goodwill relating to the acquisition of companies and businesses up to 30 June 1998 was written off immediately against reserves. On a subsequent disposal or termination of a previously acquired business, the profit or loss on disposal or termination is calculated after charging the amount of any related goodwill not written off through the profit and loss account, including any previously taken direct to reserves. Purchased goodwill arising subsequent to 30 June 1998 is capitalised and amortised to nil over its estimated useful economic life.

The cost of intangible assets acquired, which are capitalised only if separately identifiable, is amortised over estimated useful lives.

LEASED ASSETS

Assets acquired under finance leases are capitalised and the outstanding future lease obligations are shown in creditors. Rental payments are apportioned between the finance element, which is charged to the profit and loss account, and the capital element, which reduces the outstanding lease obligations.

Operating lease rentals are charged to the profit and loss account on a straight line basis over the lease term.

STOCKS

Stocks are valued at the lower of cost and net realisable value. The cost of work in progress and finished goods includes an appropriate proportion of attributable overheads.

RESEARCH AND DEVELOPMENT

Research and development expenditure is written off as it is incurred.

1. ACCOUNTING POLICIES continued

DERIVATIVE FINANCIAL INSTRUMENTS

Short term debtors and creditors that meet the definitions of a financial asset or liability respectively have been excluded from the numerical disclosures as permitted by FRS 13 "Derivatives and Other Financial Instruments Disclosures", as detailed in note 19.

ARRANGEMENT FEES

Arrangement fees incurred on the raising of loans are written off over the expected life of the relevant loan.

TAXATION

The charge for taxation is based on the profit for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes. Deferred tax is measured on a non-discounted basis at the tax rates that are expected to apply in the periods in which the timing differences reverse and is provided in respect of all timing differences which have arisen but not reversed by the balance sheet date, except as otherwise required by FRS19 "Deferred Tax".

PENSIONS

The Group operates a defined contribution pension scheme. The amount charged to the profit and loss account represents contributions payable to the Scheme in the accounting period.

The assets of the Scheme are held separately from those of the Group in an independently administered fund.

2. ANALYSIS OF TURNOVER BY GEOGRAPHICAL REGION

Destination	2003 £'000	2002 £'000
UK	176,804	167,907
Rest of the world	2,505	2,295
	179,309	170,202

The Directors consider that all turnover is derived from a single class of business. The origin of all turnover was in the UK.

3. EXCEPTIONAL ITEMS AND GOODWILL AMORTISATION

	2003 £'000	2002 £'000
Reorganisation and rationalisation costs	500	–
Compensation for loss of office	–	194
Total exceptional items	500	194
Goodwill amortisation	561	101
Total exceptional items and goodwill amortisation	1,061	295

The reorganisation and rationalisation costs relate to the integration of the Group's manufacturing operations onto a single site at Skipton, together with the costs of reorganising the Group's trading operations into a single statutory entity.

The compensation for loss of office in 2002 relates to the termination of the contract of Gary Evans, the former Chief Executive, and associated legal fees.

Notes to the Financial Statements continued

For the year ended 30 June 2003

4. ACQUISITIONS

The financial statements for the year ended 30 June 2002 included provisional amounts for fair value adjustments and total consideration in respect of the acquisition of Anglian Pharma Plc and Anglian Pharma Manufacturing Limited. Total consideration was previously contingent on the finalisation of completion accounts. The completion accounts have now been finalised resulting in total consideration payable to the vendors being reduced by £50,000. The effect of this was a net reduction of £32,000 in total cash consideration and a further £18,000 reduction in shares to be issued.

In addition, further fair value adjustments were made of £216,000 (net of £92,000 related tax credit) in respect of stock and £57,000 (net of £25,000 related tax credit) in respect of tangible fixed assets. Both fair value adjustments were made on the basis of better information becoming available regarding the state and condition of those assets at the time of acquisition. The impact on goodwill of all adjustments, including the reduction in consideration, is an increase of £223,000 (see note 12).

No further fair value adjustments are considered necessary in relation to the acquisition of North Western Laboratories Limited which also took place last year.

5. NET INTEREST PAYABLE AND SIMILAR CHARGES

	2003 £'000	2002 £'000
Bank loans and overdrafts	1,316	1,070
Amortisation of arrangement fees	97	74
Other loans	19	3
Finance charges payable on finance leases and hire purchase contracts	46	39
Total interest payable	1,478	1,186
Bank deposit and other interest receivable	(62)	(16)
Net interest payable and similar charges	1,416	1,170

6. PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION IS STATED AFTER CHARGING/(CREDITING):

	2003 £'000	2002 £'000
Research and development	997	525
Depreciation of owned assets	1,044	1,033
Depreciation of assets held under finance leases	204	256
Amortisation of goodwill	561	101
Profit on disposal of tangible fixed assets	(100)	(43)
Operating lease rentals:		
land and buildings	753	603
plant and machinery	404	10
Audit fees (including £27,000 for the Parent Company (2002: £9,000))	75	66
Other payments to the auditors for non-audit services	115	54

In addition to the non-audit fees shown above, a further £nil (2002: £66,000) has been capitalised in respect of payments made for non-audit services provided by the auditors.

Analysis of total fees payable to the Group auditors:

	2003 £'000	2002 £'000
Audit services	75	66
Further assurance services	17	74
Tax compliance services	33	20
Tax advisory services	25	17
Other services	40	9
	190	186

7. REMUNERATION OF DIRECTORS

Details of the remuneration, shareholdings, share options and pension contributions of the Directors' are included in the Directors' Remuneration Report on pages 17 to 22.

8. EMPLOYEES

The monthly average numbers of staff employed by the Group, which includes Directors, were:

	2003 Number	2002 Number
Manufacturing	140	70
Distribution	308	289
Administration	167	141
	615	500

The costs incurred in respect of these employees were:

	2003 £'000	2002 £'000
Wages and salaries	8,748	6,475
Social security costs	755	530
Other pension costs	281	191
	9,784	7,196

9. TAX ON PROFIT ON ORDINARY ACTIVITIES

A) TAX CHARGE FOR THE YEAR

	2003 £'000	2002 £'000
Current taxation		
UK Corporation tax charge	1,866	2,281
Adjustments in respect of prior periods	(63)	(35)
Total current tax charge for the year	1,803	2,246
Deferred taxation		
Origination and reversal of timing differences	77	(24)
Adjustments in respect of prior periods	(28)	28
Total deferred tax charge for the year	49	4
Tax on profit on ordinary activities	1,852	2,250
Tax credit included above attributable to exceptional operating items	108	58

Notes to the Financial Statements continued

For the year ended 30 June 2003

9. TAX ON PROFIT ON ORDINARY ACTIVITIES continued

B) FACTORS AFFECTING THE TAX CHARGE FOR THE CURRENT PERIOD

The current tax charge is higher than the standard rate of corporation tax in the UK of 30% (2002: 30%). The differences are explained below:

	2003 £'000	2002 £'000
Profit on ordinary activities before taxation	5,685	7,308
Current tax charge at 30% (2002: 30%)	1,705	2,192
EFFECTS OF		
Permanent timing differences:		
– goodwill amortisation	168	30
– depreciation on assets not eligible for tax allowances	18	18
– disallowable expenses	52	17
	238	65
Temporary timing differences:		
– capital allowances in excess of/(less than) depreciation	14	(20)
– other short term timing differences	(91)	44
	(77)	24
Adjustments to tax charge in respect of previous periods	(63)	(35)
Total current tax charge (see above)	1,803	2,246

10. DIVIDENDS

	2003 £'000	2002 £'000
Interim paid 1.37p per share (2002: 1.37p)	691	682
Final proposed 2.75p per share (2002: 2.75p)	1,402	1,387
	2,093	2,069

11. EARNINGS PER SHARE

Earnings per ordinary share have been calculated by dividing the profit on ordinary activities after taxation for each financial year by the weighted average number of ordinary shares in issue during the year.

	2003 pence	2002 pence
Basic earnings per share after exceptional items and goodwill amortisation	7.52	10.12
Effect of exceptional items	0.77	0.27
Basic earnings per share before exceptional item	8.29	10.39
Effect of goodwill amortisation	1.10	0.20
Adjusted earnings per share	9.39	10.59
Diluted earnings per share	7.50	10.09
Effect of exceptional items	0.76	0.27
Diluted earnings per share before exceptional items	8.26	10.36
Effect of goodwill amortisation	1.10	0.20
Adjusted diluted earnings per share	9.36	10.56

11. EARNINGS PER SHARE continued

	£'000	£'000
The calculation of basic and diluted earnings per share is based upon:		
Earnings for basic and diluted earnings per share calculations	3,833	5,058
Exceptional items	392	136
Earnings for basic and diluted earnings per share calculations before exceptional items	4,225	5,194
Goodwill amortisation	561	101
Earnings for adjusted and adjusted diluted earnings per share	4,786	5,295

	2003 No.	2002 No.
Weighted average number of ordinary shares for basic and adjusted earnings per share	50,975,037	49,989,015
Impact of share options	164,117	151,049
Weighted average number of ordinary shares for diluted and adjusted diluted earnings per share	51,139,154	50,140,064

12. INTANGIBLE FIXED ASSETS

	Goodwill £'000	Patent rights £'000	Total £'000
Cost			
At 1 July 2002	5,385	–	5,385
Adjustments to fair values and consideration (see note 4)	223	–	223
Additions	–	784	784
At 30 June 2003	5,608	784	6,392
Amortisation			
At 1 July 2002	101	–	101
Charge for the year	561	–	561
At 30 June 2003	662	–	662
Net book value			
At 30 June 2003	4,946	784	5,730
At 1 July 2002	5,284	–	5,284

Goodwill is being amortised over 10 years, being the Directors' estimate of the useful life.

During the year, the Group entered into an agreement with Bioenvision, a company based in the USA, to acquire the exclusive marketing and development rights of Trilostane for animal health applications in the USA and Canada. Trilostane is the active ingredient in the Group's branded product Vetoryl. The first stage payment of £784,000 including legal costs was made in 2003 and has been capitalised as a patent right. Depending upon certain milestones being achieved, the Group is committed to making two further payments. The second stage payment of US$750,000 becomes payable on the submission of a new animal drug application to the US Food and Drug Administration ("FDA") and the final payment of US$3,000,000 becomes payable on the FDA granting a marketing authorisation for Vetoryl. Once a marketing authorisation has been granted and the patent right can be applied commercially, the patent rights will begin to be amortised.

Notes to the Financial Statements continued

For the year ended 30 June 2003

13. TANGIBLE FIXED ASSETS

Group	Freehold Land £'000	Short Leasehold Land and Buildings £'000	Motor Vehicles £'000	Plant and Fixtures £'000	Total £'000
Cost					
At 1 July 2002	13	2,171	2,322	5,481	9,987
Additions	–	438	364	802	1,604
Disposals	–	(2)	(2,019)	(389)	(2,410)
Fair value adjustment (see note 4)	–	–	–	(94)	(94)
At 30 June 2003	13	2,607	667	5,800	9,087
Depreciation					
At 1 July 2002	–	223	1,004	2,436	3,663
Disposals	–	(2)	(993)	(389)	(1,384)
Charge for the year	–	138	430	680	1,248
Fair value adjustment (see note 4)	–	–	–	(12)	(12)
At 30 June 2003	–	359	441	2,715	3,515
Net book value at 30 June 2003	13	2,248	226	3,085	5,572
Net book value at 1 July 2002	13	1,948	1,318	3,045	6,324
Leased assets					
Net book value of assets held under finance leases:					
At 30 June 2003	–	–	118	122	240
At 1 July 2002	–	–	662	178	840

	2003 £'000	2002 £'000
Contracted Capital Commitments (tangible fixed assets)	202	649

14. FIXED ASSET INVESTMENTS

Company	Shares in Subsidiary Undertakings £'000
Cost and net book value	
At 1 July 2002	4,619
Acquisition of shares in subsidiary undertakings	20
Adjustment to purchase consideration (see note 4)	(31)
At 30 June 2003	4,608

A list of principal subsidiary undertakings is given in note 28.

Where subsidiaries are acquired for shares, or a combination of shares and cash, statutory merger relief has been applied and accordingly cost includes the nominal value of shares issued.

15. STOCKS

Group	2003 £'000	2002 £'000
Raw materials and consumables	1,385	1,619
Work in progress	435	72
Finished goods and goods for resale	15,476	17,611
	17,296	19,302

16. DEBTORS

	Group		Company	
	2003 £'000	2002 £'000	2003 £'000	2002 £'000
Trade debtors	26,765	24,550	–	–
Amounts owed by subsidiary undertakings	–	–	53,541	44,955
Group relief receivable	–	–	1,371	1,433
Deferred taxation	7	31	–	–
Other debtors	859	869	31	41
Prepayments and accrued income	370	372	61	11
	28,001	25,822	55,004	46,440

Notes to the Financial Statements continued

For the year ended 30 June 2003

17. CREDITORS

	Falling Due within One Year			
	Group		Company	
	2003	2002	2003	2002
	£'000	£'000	£'000	£'000
Bank loans and overdrafts	7,652	5,838	18,333	10,334
Unsecured loan stock	500	–	500	–
Hire purchase and finance leases	128	423	–	–
Trade creditors	29,224	31,709	–	–
Amounts due to subsidiary undertakings	–	–	20	2,018
Other creditors	226	253	–	–
Corporation tax	1,032	1,387	–	–
Other taxation and social security	1,463	678	–	–
Accruals and deferred income	793	770	118	258
Proposed dividend	1,402	1,387	1,402	1,387
	42,420	42,445	20,373	13,997

	Falling Due after more than One Year			
	Group		Company	
	2003	2002	2003	2002
	£'000	£'000	£'000	£'000
Bank loans	6,639	7,700	6,639	7,700
Unsecured loan stock	–	500	–	500
Hire purchase and finance leases	69	267	–	–
Other creditors	–	71	–	–
	6,708	8,538	6,639	8,200

The unsecured loan stock is payable on the earlier of 8 April 2004 or North Western Laboratories Limited and Cambridge Specialist Laboratory Services Limited achieving annual pre-tax profits of at least £400,000. Interest is charged at 1% below base rate.

18. BORROWINGS

	Group 2003 £'000	Group 2002 £'000	Company 2003 £'000	Company 2002 £'000
Borrowings due within one year				
Bank overdraft	5,698	2,110	16,379	6,606
Bank loan	1,954	3,728	1,954	3,728
Unsecured loan stock	500	–	500	–
	8,152	5,838	18,833	10,334
Borrowings due after more than one year				
Aggregate bank loan instalments repayable				
between one and two years	1,954	3,728	1,954	3,728
between two and five years	4,886	4,180	4,886	4,180
	6,840	7,908	6,840	7,908
Arrangement fees netted off	(201)	(208)	(201)	(208)
	6,639	7,700	6,639	7,700
Obligations under finance leases				
Due within one year	128	423	–	–
Due between one and two years	69	267	–	–
	197	690	–	–
Unsecured loan stock due between one and two years	–	500	–	500
Total borrowings	14,988	14,728	25,472	18,534

The bank overdraft of £5.698 million and term loan of £8.794 million from Bank of Scotland are secured by a fixed and floating charge on the assets of the Group. Interest is charged on the overdraft at 1% over base and on the term loan at 1.25% over LIBOR. The loan is repayable in semi-annual instalments of £977,000.

19. FINANCIAL INSTRUMENTS AND DERIVATIVES

An explanation of the Group's treasury policies and controls is set out in the Finance Director's Review on pages 10 and 11. As permitted by Financial Reporting Standard 13, short term debtors and creditors meeting the definition of a short term asset or liability are excluded from these disclosures.

a) Fair value of financial assets and liabilities

The Group's financial assets and liabilities are, with the exception of finance leases, at floating rates of interest and therefore their fair value and book value are equal. Finance leases are at various fixed rates of interest; however, the difference between book value and fair value is not material.

b) Interest rate risk profile as at 30 June 2003

i) Financial liabilities

Financial liabilities principally comprise the Group's borrowings of bank loans and overdrafts from the Bank of Scotland. These are secured by fixed and floating charges on the assets of the Group. All interest is payable at floating rates of 1–1.25% above LIBOR. The Group also has finance lease commitments of £197,000 (2002: £690,000) with a weighted average fixed interest rate of 7.9% (2002: 8%) over a weighted average term of 18 months (2002: 15 months).

19. FINANCIAL INSTRUMENTS AND DERIVATIVES continued

c) Foreign currency exposure profile

There were no material foreign currency monetary assets or liabilities that would give rise to gains or losses in the profit and loss account.

d) Maturity of borrowings

Details are shown in notes 17 and 18.

e) Maturity of facilities

At 30 June 2003 the Group had an undrawn committed revolving credit facility of £5 million maturing in 2005.

20. DEFERRED TAX

	Group
	£'000
At 1 July 2002 (included in debtors)	(31)
Transfer from profit and loss account	49
Fair value adjustment (see note 4)	(25)
At 30 June 2003 (included in debtors)	(7)

The amounts provided for deferred taxation at 30% (2002: 30%) are as follows:

	2003	2002
Group	£'000	£'000
Accelerated Capital allowances	20	89
Short term timing differences	(27)	(120)
Amounts included in debtors	(7)	(31)

21. CALLED UP SHARE CAPITAL

Issued share capital	Ordinary Shares of 1p each £'000	No.
At 1 July 2002	504	50,442,244
New shares issued	6	532,793
At 30 June 2003	510	50,975,037
Authorised share capital		
At 30 June 2003 and 30 June 2002	750	75,000,000

On 17 May 2003, 532,793 new ordinary shares of 1p were issued to the vendors of Anglian Pharma Plc and Anglian Pharma Manufacturing Limited in satisfaction of the deferred consideration arising on last year's acquisition of these companies (see note 4).

SHARE OPTIONS

Outstanding share options over ordinary shares of 1p at 30 June 2003 under the various Group Share Option Schemes are as follows:

	Exercise Period	Exercise Price per Share Pence	At 30 June 2002 Number	Exercised Number	Granted Number	Lapsed Number	At 30 June 2003 Number
Unapproved Share Option scheme							
14 September 2000	2003 – 2010	120	524,000	–	–	(53,000)	471,000
22 April 2002	2005 – 2012	153.5	399,000	–	–	(22,000)	377,000
11 April 2003	2006 – 2013	58.5	–	–	124,000	(3,000)	121,000
			923,000	–	124,000	(78,000)	969,000
SAYE scheme							
26 April 2001	2004 – 2006	158	178,124	–	–	(101,648)	76,476
9 April 2002	2005 – 2007	129	150,614	–	–	(82,554)	68,060
3 April 2003	2006 – 2008	39	–	–	1,034,938	—	1,034,938
			328,738	–	1,034,938	(184,202)	1,179,474
Total share options			1,251,738	–	1,158,938	(262,202)	2,148,474

Notes to the Financial Statements continued

For the year ended 30 June 2003

22. RESERVES

Group	Shares to be issued £'000	Share Premium Account £'000	Merger Reserve £'000	Profit and Loss Account £'000
At 1 July 2002	750	26,783	994	(23,282)
New shares issued	–	–	726	–
Decrease in shares to be issued	(750)	–	–	–
Retained profit for the year	–	–	–	1,740
At 30 June 2003	–	26,783	1,720	(21,542)

Shares to be issued reduced on the issue of new ordinary shares relating to the acquisition of Anglian Pharma Plc and Anglian Pharma Manufacturing Limited (see notes 4 and 21).

Company				
At 1 July 2002	5	26,783	–	1,570
Decrease in shares to be issued	(5)	–	–	–
Retained profit for the year	–	–	–	3,737
At 30 June 2003	–	26,783	–	5,307

23. GOODWILL

The cumulative amount of goodwill written off to reserves at 30 June 2003 was £30,184,000 (2002: £30,184,000).

24. RECONCILIATION OF OPERATING PROFIT TO OPERATING CASH FLOW

	2003 £'000	2002 £'000
Operating profit	7,101	8,478
Depreciation	1,248	1,289
Goodwill amortisation	561	101
Profit on disposal of tangible fixed assets	(100)	(43)
Decrease/(increase) in stocks	1,698	(2,223)
Increase in debtors	(2,197)	(601)
Decrease in creditors	(1,769)	(604)
Net cash inflow from operating activities	6,542	6,397

25. ANALYSIS OF NET DEBT

	At 1 July 2002 £'000	Cash Inflow/ (Outflow) £'000	Other Non-Cash Changes £'000	At 30 June 2003 £'000
Borrowings due after one year	(8,200)	–	1,561	(6,639)
Bank overdraft	(2,110)	(3,588)	—	(5,698)
Other borrowings due within one year	(3,728)	2,842	(1,568)	(2,454)
Finance leases	(690)	568	(75)	(197)
	(14,728)	(178)	(82)	(14,988)

Major non-cash transactions:

During the year the Group entered into finance lease arrangements in respect of assets with a total capital value at the inception of the leases of £75,000 (2002: £133,000) and finance leases with a total capital value of £nil (2002: £285,000) arising on the acquisitions of subsidiaries.

26. OTHER FINANCIAL COMMITMENTS

	2003		2002	
	Land and buildings £'000	Other assets £'000	Land and buildings £'000	Other assets £'000
At 30 June 2003 the Group has the following commitments payable within one year under operating leases expiring:				
Within one year	53	104	–	–
Between one and two years	–	111	9	–
Between two and five years	66	418	51	–
In five years or more	655	–	756	–
	774	633	816	–

The Company had no commitments under operating leases in either the current or prior year.

27. PENSIONS

The Group operates a defined contribution pension scheme for certain employees. The Group contributed between 4% and 12% of pensionable salaries which amounted to £281,000 (2002: £191,000) (see note 8).

28. SUBSIDIARY UNDERTAKINGS

The principal subsidiary undertakings of the Company, all of which are wholly owned, are:

Company	Country of Operation	Country of Incorporation	Principal Activity
Dechra Limited	UK	Great Britain	Wholesaler, marketer and manufacturer of pharmaceuticals; Wholesaler and marketer of veterinary products, instruments and equipment; Provider of veterinary laboratory services
National Veterinary Services Limited*	UK	Great Britain	Wholesale of veterinary products
Arnolds Veterinary Products Limited*	UK and Export	Great Britain	Marketer of veterinary pharmaceuticals, instruments and equipment
Dales Pharmaceuticals Limited*	UK	Great Britain	Manufacture of pharmaceuticals
Veneto Limited	UK	Great Britain	Holding Company
North Western Laboratories Limited*	UK	Great Britain	Veterinary Laboratory
Cambridge Specialist Laboratory Services Limited†	UK	Great Britain	Veterinary Laboratory
Anglian Pharma Manufacturing Limited‡	UK	Great Britain	Manufacture of pharmaceuticals
Anglian Pharma Limited*	UK	Great Britain	Holding Company

* 100% of ordinary share capital held by Veneto Limited. Voting preference shares held by Dechra Pharmaceuticals PLC Employee Benefit Trust.

† 100% of ordinary share capital held by North Western Laboratories Limited.

‡ 100% of ordinary share capital held by Anglian Pharma Limited.

Financial History

	2003 £'000	2002 £'000	2001 £'000	2000 £'000	1999 £'000
Profit and loss account					
Turnover	179,309	170,202	156,400	145,487	130,762
Operating profit before exceptional items and goodwill	8,162	8,773	8,234	7,505	6,033
Profit on ordinary activities before taxation	5,685	7,308	4,772	2,088	417
Profit after taxation	3,833	5,058	3,034	1,546	205
Dividends	(2,093)	(2,069)	(1,867)	–	–
Retained profit	1,740	2,989	1,167	1,546	205
Earnings per share – adjusted (pence)	9.39	10.59	9.29	6.05	1.61
Dividend per share (pence)	4.12	4.12	3.75	–	–
Average number of employees	615	500	454	408	367
Balance sheet					
Fixed assets	11,302	11,608	4,317	2,595	2,514
Working capital	11,157	8,869	5,157	1,580	5,823
Net debt	(14,988)	(14,728)	(8,464)	(31,994)	(37,669)
Shareholders' funds	7,471	5,749	1,010	(27,819)	(29,332)
Cash flow					
Cash flow from operating activities	6,542	6,397	3,453	12,036	5,424
Net interest paid	(1,384)	(1,126)	(7,712)	(3,662)	(3,348)
Tax paid	(2,066)	(2,155)	(1,195)	(252)	61
Capital expenditure	(1,224)	(2,704)	(1,771)	(859)	(183)
Acquisitions	32	(3,823)	(100)	(260)	(25)
Equity dividends paid	(2,078)	(1,927)	(622)	–	–
Financing	(3,410)	(765)	2,714	(2,473)	(1,388)
Changes in cash in period	(3,588)	(6,103)	(5,233)	4,530	541

The historical figures have been adjusted to reflect the adoption of FRS19 "Deferred Tax".

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