

ASX and Media Release
14 August 2006

Results for the year ended 30 April 2006

Australian Pharmaceutical Industries Limited (API) today announced a net profit after tax of \$20.4 million for the year to 30 April 2006 (FY2005: \$34.8 million). The result was affected by one-off other expenses of \$17.2 million that are explained below.

Revenue from continuing operations increased from the prior year by 11% to \$2,582 million.

In line with the company's dividend policy, the directors have declared a fully franked final dividend of 3 cents per share payable on 8 September, taking the full year dividend payment to 9.25 cents (FY2005: 13.0 cents).

As advised earlier today, Mr Stephen Roche has been appointed Chief Executive Officer and Managing Director of the company following the resignation of Mr Jeff Sher.

One-off other expenses

This announcement of API's FY2006 results has been delayed by a month as, during final consolidation of the 30 April balance sheet, a number of significant items did not reconcile.

Over the previous three years, API had changed from two legacy IT systems to a fully integrated ERP system. The changeover was extremely complex; and, to minimise disruption, financial transactions were maintained on all three systems as each state's operations converted separately and progressively.

When an initial internal review failed to identify the discrepancies in the consolidation process, the company requested a trading halt on 12 July to provide time to clarify the issue before the results were announced on 14 July. In addition to the company's own resources, a specialist team was recruited including IT experts and Ernst & Young to assist the company.

It became clear that the problem would not be identified in two days, so the company requested a suspension in trading of its shares on the ASX. Subsequently, when it was realised that more time would be needed to finalise the 2006 accounts, an approach was made to ASIC and the ASX, and an extension was granted until 14 August. After advice from the company's auditors, on 11 August API requested a further extension to lodge the 2006 statutory accounts; this was granted by ASIC and the statutory accounts are now expected to be lodged on Thursday 17 August, with trading in API shares anticipated to recommence on or shortly after that date.

The board has been closely involved throughout and formed a sub-committee to oversee the matter. It also brought in a second, forensic team from Ernst & Young which, after a thorough review, verified the completeness and findings of the company's own process.

The complete reviews have confirmed that the discrepancies resulted from processes related to the redundant computer systems and that the unreconciled balances totalled \$17.2 million. The auditor will be providing a qualified opinion in relation to this issue as it has not been possible to determine whether these balances represent expenses or balance sheet items. The company has therefore taken the conservative approach and written off the unreconciled balance.

The reviews have confirmed that the new IT system is robust, the problem has not affected initial FY2007 financial reporting, and at this point in time there has been no evidence of fraud.

API chairman, Mr Peter Robinson, said: "We very much regret this situation and apologise to our shareholders and other stakeholders for the impact on the company's FY2006 earnings and final dividend and for the delay in announcing the year's results.

"The processes run by management and the board identified that API's financial processes, controls and resourcing in relation to the systems conversion have been inadequate. Steps have been taken to strengthen the company's financial management team, and this is now being fast-tracked. "

2006 performance and operational review

Revenue for continuing businesses of \$2.58 billion was up 11% on the prior year; while underlying EBITD of \$73 million, when excluding all one-off expenses in FY2005 and FY2006¹, was 3% ahead of FY2005 (\$70.9 m) and below the company's expectation given the full year contribution from New Price Retail (acquired in October 2004).

The Retail division made good progress with its strategic implementation and grew earnings. Pharmacy Distribution maintained its share of a highly competitive, low growth market and is confident of its longer term position despite a decline in margins. Consumer Brands was restored to positive earnings in the second half after a period of restructuring.

There was no net debt as at balance date. Debtors totalling \$200 million at 30 April were securitised, strengthening the balance sheet. Interest expense for the year was higher than expected due to working capital requirements. A priority will be increased focus on improved working capital management.

Acting on under-performing assets

During the year API made significant progress to act on under-performing assets and streamline the business to focus on its main strengths. Assets in lower margin,

lower value-added businesses were divested, and these included the dental and hospital wholesaling operations and Pro-Pharma, the New Zealand pharmaceutical wholesaling business.

Having completed these transactions the company now believes there are no significant divestments ahead.

¹ See table at end of release for full details on one-off expenses for underlying business calculations

Retail division

API's strategy to build its presence in the pharmacy, health & beauty and lifestyle retail segments continued successfully. Divisional revenue increased to \$520.9 million, up significantly on the prior year, primarily due to the full year contribution and growth of the New Price Retail business.

Revenue for the six months to 30 April 2006 was strong at \$301.8 million, up 20% on the prior corresponding period; Underlying EBITD for the same period was up by more than 25% to \$22.7 million compared to the prior corresponding period. The increases in comparable second half revenue and earnings were mainly the result of the expansion of the Priceline Pharmacy model, demand for which is growing quickly in the pharmacy industry. There are now 68 Priceline Pharmacies trading, with a further 35 in various stages of development.

Retail trading conditions have been competitive; however Priceline corporate stores have continued to trade well with a strong consumer offering. Price Attack has continued to grow its franchise base successfully, while House has competed well in the highly competitive homewares market. Private label product strategies across the company's retail brands have been a key component in their revenue growth.

The retail pharmacy groups including Soul Pattinson, Chemworld, Pharmacist Advice and API Healthcare were reinvigorated with new retail programs and formats which have stabilised the previous decline in membership.

API's strategy of using its retail capabilities to provide greater choice and services to independent pharmacies through its API Member program has been well received. The program was launched in December 2005 and is now used by more than 1,000 pharmacies.

API's retail model provides pharmacists with access to retail services for their individual needs. The full franchise model is gaining greater acceptance as a point of differentiation and provides a long-term approach to offset the competition from supermarkets.

Pharmacy Distribution division

Pharmacy distribution revenue for the year ending 30 April 2006, at \$2,020 million, was relatively flat compared to the prior year, reflecting low PBS growth and the increasing penetration of generics, which often by-pass the wholesale market. Underlying EBITD of \$50.0 million was down 21% compared to underlying EBITD of \$63.2 million in the previous corresponding period.

Marginal market share churn resulted in gains in South Australia, Victoria and Western Australia offset by a loss in New South Wales. An operational restructure affected performance during the year, however by the end of the period it had restored high service levels and increased productivity. It has established a platform that positions the company well for the start of the Community Service Obligation (CSO) requirements from 1 July 2006 as part of the Fourth Community Pharmacy Agreement.

Integrated retail service solutions, including through the API Member program referred to above, were improved and have successfully strengthened relationships with many pharmacies beyond traditional wholesale relationships.

The transition to the CSO system has been relatively smooth, with API taking the opportunity to simplify and strengthen its business offer to pharmacists. This unique approach to build loyalty is being actively pursued to build on the more than 400 agreements already signed with distribution customers.

Consumer Brands division

During FY2006, API centralised its consumer products manufacturing in New Zealand, relocating equipment to Auckland and extending the Auckland plant with a new state-of-the-art facility. The division achieved revenue for the year ending 30 April 2006 of \$40.8 million, up 19% on the previous corresponding period. The underlying results for the division resulted in a profit in the second half and a break-even position for the year, a significant improvement on the underlying \$12 million EBIT loss in the prior full year period.

The Consumer Brands division now includes manufacturing over the counter (OTC), health and beauty products, and manages contract manufacturing. It has a sales and marketing division and is also responsible for product development. API enhanced its range of private label products in FY2006 to provide an exclusive range of pharmacy health products to API pharmacists. API intends to review its intellectual property to focus on profitable opportunities, and expand sales and marketing capability into the Australian market through an outsourced field force.

Conclusion

Despite the retail division sales for May and June being approximately 13% up on last year, as reported in the media release on 28 July 2006, the performance of the business will be affected by the current retail trading conditions, the implementation of the CSO and the cost of resolving the accounting issue.

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1. Reported FY06 Profit

Year ended 30 April A\$m	FY06	FY05	% Change
Revenue	2,582	2,323	+11
EBITD	51.1	63.7	-20
Depreciation	(11.7)	(9.1)	
EBIT	39.4	54.6	-28
Profit from associates	0.3	-	
Net interest	(13.3)	(9.3)	
Pre tax profit	26.4	45.3	
Tax	(7.8)	(12.9)	
Profit after tax	18.6	32.4	
Contribution from discontinued businesses	1.7	2.4	
Reported NPAT	20.4	34.8	-41

**2. Underlying FY06 Profit Result –
adjusted for one-off Other Expenses and costs**

The following table shows the adjustments which have been made to reported NPAT of \$20.4 million to arrive at underlying performance:

Year ended 30 April A\$m	FY06	FY05	% Change
Revenue	2,582	2,323	+11
EBITD	73.0	70.9	+3
Depreciation	(11.7)	(9.1)	
EBIT	61.3	61.8	-1
Profit from associates	0.3	-	
Net interest	(13.3)	(9.3)	
Pre tax profit	48.3	52.5	-8
Tax	(14.2)	(15.0)	
Underlying profit after tax	34.1	37.6	-9
Contribution from discontinued businesses	1.7	2.4	
Underlying Net Profit	35.8	40.0	
One off Other Expenses (after tax)	(12.0)	-	
One-off costs (after tax)	(3.3)	(5.2)	
Reported NPAT	20.4	34.8	-41

3. Adjustments – Other Expenses and One-Off Costs (pre tax)

Year ended 30 April A\$m	FY06	FY05
Other Expenses	17.2	
One off costs:		
Kingsgrove plant closure		5.8
Retail pharmacy research/rollout	2.2	
Redundancy costs	1.4	1.5
IT system implementation	1.1	
TOTAL	21.9	7.3