Developing **Pharmaceuticals**
Improving **Animal Health**

Annual Report and Accounts 2006

COMPANY REGN NO

3369634

Dechra
Pharmaceuticals PLC

Welcome
to Dechra

Our Strategy

To continue the development of our veterinary pharmaceutical portfolio and increase our pharmaceutical penetration into international markets.

Our Business

An emerging pharmaceutical business, focused on the veterinary market.

Contents

Pharmaceuticals

Dechra Veterinary Products
Marketing and development of licensed branded pharmaceuticals to the veterinary profession worldwide.

Arnolds Veterinary Products
UK market leading supplier of veterinary instruments and equipment, and suppliers of critical care fluids and equipment.

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

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Services

National Veterinary Services
UK market leader in the supply of pharmaceuticals and added value services to the veterinary profession, including management information systems and consumer and internet services.

NationWide Laboratories
Multi-disciplined independent commercial veterinary laboratory.

Cambridge Specialist Laboratory Services
Primary care and secondary referral specialist veterinary immunoassay laboratory.

Highlights

Revenue
£'000

up 10.6%

Dividend per share
pence

up 20.0%

Operating Profit
£'000

up 9.4%

Operating cash flow
£'000

up 3.3%

Chairman's Statement

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Improving **Animal Health**

I am pleased to report that we continue to make solid progress across the Group. This is reflected in the positive performance by our Pharmaceuticals and Services Divisions, both of which achieved strong revenue growth and improvements in profitability.

Overall, our strategic focus firmly remains the on-going development of the Group's own branded veterinary pharmaceutical portfolio for the world's companion animal markets.

Financial Highlights

These are the first full year results to be presented using International Financial Reporting Standards ("IFRS"). The comparative figures for the year ended 30 June 2005 have been restated accordingly.

Group revenue increased 10.6% from £210.3 million to £232.5 million.

Operating profit increased by 9.4% to £12.3 million (2005: £11.3 million) and profit before taxation rose 13.8% to £11.0 million (2005: £9.7 million).

Basic earnings per share was 14.71 pence, up 6.8% from the 13.77 pence achieved in 2005.

Cash flow continued to be strong with cash flow from operations being 114% of operating profit. As at 30 June 2006, the Group had net funds of £1.1 million compared to net debt of £4.9 million at 30 June 2005.

Interest cover was 9.7 times.

Capital expenditure during the year totalled £2.2 million which principally comprised IT upgrades at our distribution and manufacturing businesses and an expansion of capacity at our distribution business.

Further details on the financial results are contained in the Business Review.

Dividend

In line with our progressive dividend policy and our confidence in the business, the Directors are recommending a 23.7% increase in the final dividend to 4.33 pence per share (2005: 3.50 pence per share). This, together with the interim dividend of 1.91 pence per share (2005: 1.70 pence per share), makes a total dividend for the year of 6.24 pence per share (2005: 5.20 pence per share), a 20% increase.

Total dividend cover is 2.3 times profit after taxation.

The final dividend, which is subject to Shareholder approval at our Annual General Meeting to be held on Wednesday 18 October 2006, will be paid on 24 November 2006 to Shareholders on the Register at 27 October 2006.

People

On behalf of the Board and all our Shareholders, I warmly welcome all staff who joined us during the year and I would like to take this opportunity to thank all of our people for the tireless hard work, focus and commitment to the business.

Prospects

Current trading remains in line with management expectations and we continue to maintain confidence in the future. We have an increasing number of opportunities to market and exploit our own-developed branded veterinary products on a global basis, and also to further extend our strong position within our Services business.

Following the launch of Vetoryl® Capsules by our European Marketing Partner in France, Germany and the Benelux countries, we expect to see a reasonable contribution in 2007 towards revenues.

The clinical trial work required to obtain regulatory approval for Vetoryl® Capsules and Felimazole® Tablets in the USA is progressing in line with our expectations and these trials are expected to be completed prior to the end of 2007.

Michael Redmond
Chairman
5 September 2006

"Our protocols for Vetoryl® clinical trials within the USA have been approved by the FDA and trials have commenced in several dogs with new cases being identified daily. We anticipate completing the trials on schedule prior to the end of the 2007 calendar year"

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Pharmaceuticals PLC

Global Markets

90% of the world's companion animal market is in North America, Western Europe and Japan

The USA represents the largest companion animal market in the world, with around **70 million dogs and 80 million cats**

There are approximately **6.5 million dogs, 7 million cats and 1 million horses in the UK**

Japan has over **13 million dogs,** while Canada and Australia also represent sizeable companion animal markets

Directors' Business Review

Review of the Year

Developing **Pharmaceuticals**
Improving **Animal Health**

The Business and Its Markets

Dechra Pharmaceuticals PLC ("Dechra") comprises six businesses operating under two divisions, Pharmaceuticals and Services. Both divisions are focused on the veterinary market with a key area of specialisation being on companion animal products.

The Group's main focus is delivering organic growth from its two divisions; however, the key strategy to deliver medium to long-term growth is the development of our own branded veterinary pharmaceutical products for licensing internationally.

Dechra employs 698 people who operate out of 16 locations.

The veterinary market for companion animal products is dominated by North America, Western Europe and Japan. Key drivers within the companion animal market are the increasing medical and surgical capabilities of veterinary surgeons, increased life expectancy of pets and ultimately the consumer's passion for their animals.

The USA represents the biggest companion animal market in the world with the number of dogs and cats estimated at 70 million and 80 million respectively. American veterinarians are very advanced in their knowledge of small animal medicine, a key advantage when marketing specialised products such as Dechra's own brands. Sources indicate that Americans spend more per companion animal than any other nation.

Within the UK there are approximately 6.5 million dogs, 7 million cats and 1 million horses. The UK companion animal market is also considered to be highly advanced in terms of spend per animal and veterinarian competence. The UK veterinary market, including livestock products, has consistently outperformed the Retail Price Index ("RPI") over the past seven years.

The remainder of the EU, in terms of the number of animals, is potentially commensurate with the USA. Despite this, however, the market value is currently considerably less as the average spend on dogs and, particularly, cats is lower. The majority of pets do not have regular contact with a veterinary surgeon and with the exception of some major conurbations, small animal veterinary science is not as advanced. Japan represents a considerable market opportunity with over 13 million dogs. Other territories with sizeable companion animal markets are Canada and Australia.

Product Development

Strategy

Our product development is focused entirely on prescription only veterinary medicines for dogs, cats and horses, with our main area of specialisation being endocrinology. Most of our projects utilise existing pharmaceutical entities that are typically used within the human market, therefore the majority of product creation is development and not research based. There are a number of benefits to our strategy relative to traditional human and veterinary pharmaceutical R&D, which include:

- An identified, existing pharmaceutical product can often be brought to full licence for the veterinary market within five years;

Directors' Business Review

Review of the Year *continued*

Developing **Pharmaceuticals**
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- After minimal expenditure on early explorative project evaluation, an identified human pharmaceutical has a high probability of achieving a veterinary licence;
- Development projects have a high probability of success with relatively low cost; research-based projects are usually expensive with low probability of product success;
- Products developed for other species, i.e. food producing animals, take considerably longer to license as expensive food safety and toxicological studies are required;
- Clinical trials for veterinary medicines typically require a few hundred cases, while human trials demand several thousand.

Legislation

There are two pieces of EU legislation, which the Directors believe have been implemented to encourage development of specialised veterinary products for relatively small markets. Dechra considers this legislation to be favourable towards its strategy:

- "The Prescribing Cascade": The basic principles of this legislation are that the veterinary surgeon must prescribe a veterinary licensed product above any other alternative. Therefore, any products licensed specifically for animals must be used instead of a human ethical or generic product, irrespective of price;
- EU law gives a novel product ten years protection from generic competitors, irrespective of its patent status.

Licensing Authorities

Dechra considers one of the most unpredictable aspects of product licensing is the response time from the Regulatory Authorities globally. EU regulators provide definitive response times based on a number of working days, which can vary depending on the type of application. However, these time lines can be stopped intermittently if the assessor considers that parts of the application need further supporting information. The US Food and Drug Administration ("FDA") have recently introduced similar targets for novel products; however, whilst progress is being made, it will be a number of years before they meet statutory targets. Currently, there is an extensive backlog of applications for generic products for the American market, where the FDA have no obligations on response time. Other regulators, such as Canada and Japan, make no commitment to time lines and as a result the process can take several years.

Key Strengths

The Directors believe that the Group has exceptional skills and expertise that are relevant to delivering its strategy:

- The recognition of opportunities for specialised and niche pharmaceutical products for the veterinary market achieved from knowledge gained from the Group's strong UK market position;
- In-house formulation of products into preparations suitable for the target species;
- International experience and proven track record of regulatory and licence delivery;
- Successful design and management of international clinical field trials;
- Industry leading veterinary and commercial personnel throughout the Group.

Achievements

During the last five years we have licensed four specialist products, of which Vetoryl® Capsules and Felimazole® Tablets currently represent our biggest opportunities for international growth.

Vetoryl® is a novel and patented product for the treatment of Cushing's Disease (excess cortisol or hyperadrenocorticism) in dogs. It is the only licensed product within the EU and is the only recognised safe and efficacious product for the treatment of Cushing's Disease around the world. Launched in the UK on a provisional marketing authorisation in September 2001, Vetoryl® has been well received by veterinarians, with revenue now in excess of £2.9 million per year. It achieved mutual

Product Development
Dr Susan Longhofer, Product Development and Regulatory Affairs Director; Keith Collis, Regulatory Affairs Director

recognition for approval within Europe in 2005 and was recently launched within the key *European territories.*

Felimazole® is the first veterinary licensed product for the treatment of feline hyperthyroidism. Felimazole® received marketing approval in 2002 and has achieved revenues in *excess of £2.4 million in the financial year.* Felimazole® was launched into most major EU territories during the 2005 financial year.

Both Vetoryl® and Felimazole® have been granted an expedited review status by the FDA in the USA. The principal advantage to an expedited review is that there is a target 90-day response from submission of information (however, as previously indicated, the FDA are currently not meeting their targets).

To date, we have submitted the safety and UK based efficacy parts of the dossiers; in both instances clear guidance has been provided by the FDA on requirements for further USA-based clinical trial work. In the USA, the various sections of the dossier can be submitted independently, i.e. when one section is complete it can be sent for review as opposed to the whole application being made concurrently. We anticipate filing our manufacturing sections by the end of this 2006 calendar year and the efficacy sections, containing data from the USA-based clinical trials, during the 2007 calendar year.

Development Update

There have been a number of achievements within our development programme throughout the financial year:

- Vetoryl® Capsules have received approval for marketing in 19 major European territories. This is a major achievement for our Regulatory team and is now the third product we have successfully licensed throughout key European markets following the approval of Felimazole® last year and Hypercard in 2003;
- Our protocols for Vetoryl® clinical trials within the USA have been approved by the FDA and trials have commenced in several dogs with new cases being identified daily. We anticipate completing the trials on schedule prior to the end of *the 2007 calendar year;*
- Clinical trials for Felimazole® are also progressing well within the USA. A significant number of cats have now commenced the trial and, as with Vetoryl®, we anticipate the trials to be completed prior to the end of the 2007 calendar year;
- After twelve months' negotiations of both a technical and commercial nature, we have signed a marketing agreement for Vetoryl® in Japan with Kyoritsu Seiyaku ("KS"). KS are Japan's leading companion animal pharmaceutical supplier and have over sixty representatives marketing to veterinary practices. The Japanese Regulators will require clinical trials to be conducted in Japan. These will be the responsibility of KS and it is anticipated that it will be at least three years to gain approval in this significant territory;
- Complete dossiers have been submitted *for Vetoryl® to the Canadian and* Australian authorities. The complete Felimazole® dossier has been submitted in Canada. We estimate that the review process in these territories will take two to three years prior to marketing authorisations being approved;
- A new 10mg small dog Vetoryl® Capsule is at an advanced stage of development for all markets, with approval anticipated for Europe within the next twelve months. *The USA approval is expected to be* concurrent with the full application;
- Further investment has also been made into our pharmaceutical development laboratory in terms of equipment and people, as we continually strengthen our in-house product development formulation capabilities.

We currently have a number of other products under development; due to commercial sensitivity we believe it to be appropriate to treat the nature of these projects as confidential.

Directors' Business Review

Review of the Year *continued*

Developing **Pharmaceuticals**
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Case Study

After their elderly owners were no longer able to *look after them, lifelong companion corgis* Molly and Digger were found a new home with Anne Craghill and her family in 2000.

Shortly after Molly and Digger had settled into family life, Anne became concerned that all was not well with Molly — her water intake seemed excessive, she was constantly tired and her co-ordination and attention were far from perfect.

Following a visit to the local veterinary practice, initial blood tests suggested that Molly was hypothyroid and was immediately put on a thyroid supplement therapy. However, several months passed and with Molly showing no sign of improvement, further tests were undertaken that then confirmed that Molly had hyperadrenocorticism, also known as Cushing's disease, due to a pituitary tumour.

Molly was prescribed Vetoryl, Dechra's own developed drug which is licensed in the EU for the treatment of Cushing's disease.

Cushing's occurs when a dog produces excessive amounts of cortisol, which is an important hormone that affects the body's protein, carbohydrate and fat metabolism. When these levels are too high, it becomes harmful to the animal and has a damaging effect on the function of many organs and the body's metabolism. This can result in a number of serious conditions.

Vetoryl contains the active ingredient trilostane, which blocks the chemical reaction triggered in the body to stimulate the production of cortisol, and allows the dog to lead a near normal life. While there is no cure for Cushing's, the therapy helps to block further progress and damage by regulating the amount of cortisol in the body.

Thanks to Vetoryl, Molly's excessive drinking subsided and she became more energised; as Molly was improving, Anne began to become increasingly concerned with Digger.

Although the two corgis are unrelated, like Molly, Digger had begun to drink excessively. He had also become incontinent, started scavenging for food and when being groomed, was losing large chunks of hair — the vet suspected Cushing's disease once again.

Digger was also treated with Vetoryl therapy and soon after, his coat began to grow back and his other symptoms subsided.

Digger, now aged 10, has been treated with Vetoryl since October 2005 and Molly, aged 11, for three years — both corgis, despite maturity, are now healthy and happy dogs and have adapted well to the Vetoryl treatment without any side-effects.

Dechra Veterinary Products, as part of its education programme, runs continuing professional development seminars which give the veterinary profession the opportunity to keep abreast of new developments in veterinary science.

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"Due to the unique nature of Vetoryl® and Felimazole® the products will be sold on a technical basis, i.e. education of veterinary surgeons and opinion leaders which is achieved through technical marketing, sponsoring congress lectures, and through conducting regional educational roadshows"

Pharmaceuticals Division

Directors' Business Review

Review of the Year *continued*

Developing **Pharmaceuticals**
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DVP UK
Giles Coley, Managing Director; Chris Kingdon, Pharmaceutical Sales Director; Gwenda Bason, Pharmaceutical Marketing Director; Mark Sallin, Finance Director

Our Pharmaceuticals Division comprises Dechra Veterinary Products ("DVP UK"), Dechra Veterinary Products USA ("DVP USA"), Arnolds Veterinary Products ("Arnolds®") and Dales Pharmaceuticals ("Dales").

DVP UK

DVP UK, located in Shrewsbury, England, employs 30 people. This business markets and sells our own branded, licensed veterinary pharmaceuticals in the UK, and manages the relationships with our EU marketing partners. We have over 50 licences; however, there are 12 key brands which represent over 90% of DVP's revenue. We have three UK marketing agreements; with Virbac Corp. to market Soloxine within the UK and Ireland, with Biopure to market Oxyglobin in the EU, and with Peptech to market Ovuplant in the EU. Soloxine is used for the treatment of hypothyroidism in dogs and currently has UK sales of approximately £800,000 per year; this contract is due to expire in March 2007. Ovuplant is a seasonal equine fertility product, launched in the UK in Spring 2005; development has commenced to license the product within the rest of the EU. Felimazole® and Vetoryl®, together with Equipalazone®, the market leading equine non-steroidal anti-inflammatory drug, are marketed within the EU by various partners, the key territories being serviced by Janssen, Intervet and Orion.

As outlined in the Financial Review in this report, DVP had a very successful year. Felimazole® revenue increased by 34%, predominantly as a result of the introduction of the new 2.5mg product presentation which was launched last year. It is estimated that over 50,000 cats are now being treated with Felimazole® daily. Vetoryl's® market penetration has also increased with over 2,100 of the UK's 3,500 veterinary practices now prescribing Vetoryl®. The reduction in the pack size from a pot of 100 capsules to blister packs of 30 had a temporary depressive effect on UK revenue in the year as the number of capsules in the supply chain was reduced. This has now reversed out and solid growth is being delivered. The marketing department has been strengthened and restructured during the year with greater accountability being given to the marketing managers, with individual product categories being assigned to specific teams. Our business in Eire has been restructured and we have taken on direct sales responsibility with the appointment of a Business Development Manager for the territory. We have also strengthened our management team with the appointment of a European account manager to develop our relationship with our marketing partners and drive sales of our products within Europe.

"We currently have a number of other products under development; due to commercial sensitivity we believe it to be appropriate to treat the nature of these projects as confidential"

Directors' Business Review

Review of the Year continued

DVP USA
Mike Eldred, President; Chip Whitlow, Vice-President Sales & Marketing

Arnolds
Andrew Groom, Instruments Business Director; Becky Watkins, Marketing Co-ordinator; Kerry Boyd, Critical Care Marketing Manager

DVP US

This business, established in 2005 and located in Kansas City, Missouri, USA, currently has two employees. As outlined under Product Development, both Vetoryl® and Felimazole® are at an advanced stage of the licensing process, with full submissions being targeted to be completed by the end of 2007. The Directors consider that the US market represents the biggest single opportunity for our own international expansion. We believe that to gain full value from our products, the best route to market will be to create a Dechra brand within the USA. In order to achieve this, we currently market one minor product with the intention of establishing the Dechra brand, developing distributor relationships, creating a customer database and establishing accounting and logistics systems prior to the approval of our own key products. It is our intention to distribute our products through the existing network of veterinary suppliers within the USA, who also provide first line sales support. Our American function will be structured predominantly around marketing and technical support, with a team of up to 12 people being employed to coincide with the launch of our first major product. Due to the unique nature of Vetoryl® and Felimazole® the products will be sold on a technical basis, i.e. education of veterinary surgeons and opinion leaders which is achieved through technical marketing, sponsoring congress lectures, and through conducting regional educational roadshows. Pre-marketing has already commenced; the majority of world opinion leaders now understand and support the benefits of our products.

Arnolds®

Arnolds®, located in Shrewsbury, England, employing 23 people, is a well-established brand within the UK veterinary market and sells licensed critical care fluids, instruments, consumables and equipment to veterinary practices. Critical care products, branded Vetivex, drive the growth within Arnolds®. The revenue from instruments and surgery equipment is difficult to maintain given the low barriers to entry, cheap unregulated imports and the increasing number of small business entrants. The majority of products are branded "Arnolds"; however, we do have a number of important long-term marketing agreements which include 3M, B Braun and Portex (Smiths Medical).

Throughout the year we have continued to build on the Vetivex range of critical care fluids which were purchased from Gambro BCT in April 2005. We have increased market share by 4% to 37.5% on a moving annual total basis and revenue has now exceeded £1.2 million per annum. Many of our disposable products, which are associated with critical care, have also been branded Vetivex to leverage brand strength.

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Dales
Steve Dewar, Operations Director; Gareth Davies, Sales & Marketing Director; Kirsty Ireland, Finance Director; Mike Annice, Managing Director

Dales

Dales, located in Skipton, England, employing 129 people, is a fully Medicines and Healthcare Products Regulatory Agency ("MHRA") approved pharmaceutical manufacturer with multi-competence in both batch size and dose form. Dales manufactures the vast majority of our own branded licensed pharmaceutical products, which are marketed through DVP, but also derives approximately 50% of revenues from third party contract manufacturing, predominantly for human pharmaceutical companies. This is Dechra's only significant source of revenue not derived from the veterinary market. As major pharmaceutical companies continue to rationalise their manufacturing centres, our multiple scale production and specialisation (i.e. controlled drugs) capabilities allow us to maintain and write new contracts. The third party contracts make a significant contribution to the manufacturing overheads and, whilst many contracts are substantial, our relationships with key customers are important and new contracts are being written, contract manufacturing is not key to the Group's long-term growth prospects.

Throughout the year, we have continued to strengthen our technical department with further appointments being made within the Quality Assurance and Quality Control departments. We have successfully introduced a new Quality Management System, which provides the framework for anticipated future worldwide compliance requirements and is the basis for continual improvement. The improvement in the business has already been witnessed within the year as, despite these appointments, the overall headcount has reduced due to increased efficiency and investment in new equipment. The Dales management are at an advanced stage of implementing a new integrated IT system, which is expected to go live prior to the end of 2006.

Services Division

Directors' Business Review

Review of the Year *continued*

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NVS
Tony Scott, Operations Director; Caitrina Harrison, Sales & Marketing Director; Martin Riley, Managing Director; Dan Shipman, Finance Director; Colin Higham, Buying Director

Our Services Division comprises National Veterinary Services ("NVS®"), NationWide Laboratories ("NWL") and Cambridge Specialist Laboratory Services ("CSLS").

NVS®

NVS, located in Stoke-on-Trent, England, employing 453 people, is the UK market leader, as measured in terms of market share, in the supply and distribution of veterinary products to veterinary practices and other approved outlets.

NVS stocks a range of over 12,000 products including pharmaceuticals, pet products, consumables and accessories. NVS has also developed a range of IT solutions for veterinary practices which are branded "Vetcom®". Vetcom's principal objective is to collect orders and transmit electronically. Approximately 80% of NVS' orders arrive automatically with no human input required. This is considered to be a major advantage to our customers and also reduces our operating costs. With over 30,000 invoiced lines per working day, significant numbers of additional personnel would be required to handle this business manually. NVS distributes to 1,500 customers daily utilising its own fleet of vans and Heavy Goods Vehicles ("HGVs"). The centralised inventory in Stoke-on-Trent is picked and packed throughout the afternoon and evening and then distributed overnight to trunking depots by the HGVs on large trailers. Van drivers are then employed locally at these depots who distribute the goods to the customers. NVS operates on a Sunday until Thursday shift which allows customers to place orders up until 7.00 p.m. Monday to Thursday and any time over the weekend up to 11.00 a.m. on Sunday for a next working day delivery.

NVS services companion animal practices, livestock practices and agricultural merchants, with approximately 60% of sales being in favour of companion animal related products. As with other divisions within Dechra, NVS benefits from the solid growth in the veterinary market as outlined previously in this report.

The wholesale market in which NVS trades saw a major consolidation within the year with the acquisition of GenusXpress by Dunlops. There are now only two major full-line competitors to NVS within the mainland UK, the other business being Centaur Services.

NVS saw good growth within the year and gains in market share, which now stands at 44%.

NVS launched a new IT solution, Vpod, in March 2006, a hand-held, stand-alone, electronic, online ordering device. To date, 100 have been installed as veterinary practices recognise the benefits of this system to maintain optimum stock levels and the flexibility to place orders at any time of day.

Over the last five years, NVS has been investing in automation within the warehouse. This has continued during this financial year with an investment in excess of £700,000. This investment increases our capacity and provides improved operational efficiencies. The warehouse has been extended with a new 16,000 sq. ft. mezzanine floor and significant improvements and extensions have been made to the semi-automated picking circuit.

There have been two major management changes at NVS within the year. Martin Riley was appointed as Managing Director and Caitrina Harrison as Sales & Marketing Director.

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"The NVS warehouse has been extended with a new 16,000 sq. ft. mezzanine floor and significant improvements and extensions have been made to the semi-automated picking circuit"

"NVS saw good growth within the year and gains in market share, which now stands at 44%"

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Directors' Business Review

Review of the Year *continued*

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Laboratories
Tariq Shah, Sales & Marketing Manager; Jamie Whitwam, Food Microbiology and Business Development Manager; Dr Peter Graham, Managing Director

Laboratories

NWL is located in Poulton-le-Fylde, England and employs 44 people. It is a first referral veterinary laboratory, providing histology, pathology, haematology, chemistry and microbiology services to veterinary practices. Whilst a certain amount of simple chemistry is performed at veterinary practices, nearly all veterinary practices will outsource more advanced analytical tests, often requiring expert interpretation of results. We consider NWL to offer the highest level of service within this sector. We were the first veterinary laboratory to gain UKAS (United Kingdom Accreditation Service) approval. NWL also offers other services such as Allervet, a pet and equine allergy testing programme and Petscreen, a chemotherapy sensitivity test for small animal tumours.

CSLS, located in Sawston, England, employs 6 people. It operates as a first and second referral laboratory, with its key area of expertise being endocrinology. The second referral work, i.e. providing services for NWL and some of NWL's competitors, is mainly derived from specialisation in radio-immuno-assays. The business also provides precise assays which support the dosage regimes and patient monitoring of our key products, Vetoryl® Capsules and Felimazole® Tablets.

The laboratories management team, established over the last two years, has begun to realise benefits from the changes they have implemented. New account gains have been good and new services have been introduced. Allervet, a pet allergy testing programme introduced last year, has exceeded expectations. We are also starting to build on the microbiology laboratory at NWL by providing services for food quality testing. This is a potentially large market and offers good growth opportunities.

"After twelve months' negotiations of both a technical and commercial nature, we have signed a marketing agreement for Vetoryl® in Japan with Kyoritsu Seiyaku, Japan's leading companion animal pharmaceutical supplier"

Directors' Business Review

Financial Review

Developing **Pharmaceuticals**
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Key Performance Indicators

		2006 £'000	2005 £'000
Revenue	— pharmaceuticals	**23,252**	21,381
	— services	**215,556**	194,611
	— inter-division	**(6,337)**	(5,725)
		232,471	210,267
Operating profit before product and USA development cost		**13,950**	12,493
Product and USA development cost		**(1,638)**	(1,238)
Operating profit		**12,312**	11,255
Operating margin — Before product and USA development cost		**6.0%**	5.9%
— After product and USA development cost		**5.3%**	5.4%
Cash conversion rate		**114%**	120%
Gearing		**(4.7%)**	21.6%
Return on capital employed (pre-tax)		**34.9%**	34.0%
Revenue per employee		**336**	310
Inventory days		**38**	38
Receivables days		**42**	43

Financial Ratios

	2006	2005
Interest cover	**9.7 times**	7.2 times
Effective tax rate	**31.6%**	27.6%
Dividend cover	**2.3 times**	2.6 times

Review of Operating Performance

Group Performance

The Group achieved revenue growth of 10.6% for the year whilst operating profit grew by 9.4%. This was despite the start-up losses incurred by our US operation and a 30.9% increase in product development expenditure. Operating profit before these costs increased by 11.7% compared to last year.

The Group achieved a pre-tax profit of £11.0 million, an improvement of 13.8% compared to last year. Pre-tax profit before product development and USA costs increased by 15.9%.

The results are reviewed in more detail on a divisional basis below:

Pharmaceuticals Division

	2006 £'000	2005 £'000
Revenue		
Own branded pharmaceuticals	**12,316**	10,915
Instruments, consumables, critical care and equipment	**5,127**	4,436
Third party contract manufacturing	**5,809**	6,030
Total revenue	**23,252**	21,381
Operating profit	**4,868**	4,292

Revenue from own branded pharmaceuticals continued to show strong growth, achieving a 12.8% increase over the previous year. As already emphasised, the development of this area of the business is the key strategic driver to long-term growth.

Most of the increase this year came from our key products Vetoryl® Capsules and Felimazole® Tablets. Vetoryl® achieved global revenue of £2.90 million, a 35.9% increase on the £2.13 million achieved last year. Felimazole® generated global revenue of £2.41 million, a 34.1% increase over last year. During the year, Vetoryl® became our largest product measured by global revenue with increasing amounts being sold overseas. In May 2006, we made the first shipment to our European marketing partner following the approval of Vetoryl® within the European Union. We are also selling substantial amounts into the USA under the FDA waiver scheme for named patients.

Our USA operation commenced marketing one small product during the financial year. Although the revenue generated of £326,000 (US$589,000) was modest, we have managed to establish the Dechra brand within the USA and establish relationships with the key distributors that we will work with following the launch of Vetoryl® and Felimazole® into this market.

Revenue from instruments, consumables, critical care and equipment increased by 15.6% to £5.13 million. This was entirely due to the excellent performance of the Vetivex® range of critical care fluids that we acquired in April 2005. The revenue achieved was £1.25 million which, as already noted, was derived from a significant gain in market share. Revenue from other instruments and consumables continued to struggle in the face of low cost competitors and "grey market" imports.

Revenue from third party contract manufacturing fell slightly due to the timing of customer delivery requirements. However, continued efficiency improvements enabled our manufacturing operation to increase operating profit by 14.6% despite the lower revenue. The order book at 30 June 2006 was strong at £2.0 million and, subsequent to the year end, a significant new contract has been agreed.

Operating profit for the pharmaceuticals division increased by 13.4% to £4.9 million. This was even after a 30.9% increase in product development expense and the start-up losses incurred by our USA operation. Operating profits before these costs improved by 17.6% and reflects the higher margins achieved by our own branded pharmaceuticals and increased efficiency at our Dales manufacturing operation.

Services Division

	2006 £'000	2005 £'000
Revenue		
Veterinary wholesaling	**210,940**	190,634
Vetcom	**819**	785
Laboratories	**3,797**	3,192
Total revenue	**215,556**	194,611
Operating profit	**8,681**	7,973

Revenue from veterinary wholesaling increased by 10.7% to £210.9 million. This compared to market growth as measured by GfK, an independent market analyst, of 5.3% for the

Directors' Business Review

Financial Review *continued*

Developing **Pharmaceuticals**
Improving **Animal Health**

same period. Revenue was boosted by NVS gaining, towards the end of the 2005 financial year, a number of veterinary practice accounts who had joined together as a buying and marketing group. Other account gains were also made during the year.

Following the Competition Commission review of the veterinary market in 2003, the agricultural market was opened up to us. Revenue from sales to agricultural merchants reached nearly £2.6 million for the year, an increase of 17.1% over 2005.

Revenue from our various IT products, branded Vetcom, increased by 4.3%.

Our laboratories had an excellent year, achieving revenue growth of 19.0%. This reflected new veterinary practice account gains following a concerted sales and marketing effort and the introduction of new services such as Allervet, our pet and equine allergy testing programme.

The overall veterinary wholesaling market continues to be competitive with upward pressure on discounts allowed to our customers. We largely negated this by further operational efficiencies and improvement of our gross margin. The division did, however, see a small reduction in operating margin from 4.10% to 4.03%.

The Services Division has always been a strong cash generator and this provides the Group with the financial resources to invest in the development of our own branded pharmaceuticals.

Unallocated Central Costs

These costs comprise the charge in respect of share-based payments under IFRS2, Non-Executive Director fees and corporate legal, taxation and advisory fees.

Central costs for the year increased from £1.0 million to £1.24 million. The principal reason for the increase was a rise in the charge for share-based payments (including national insurance) from £398,000 to £515,000.

Return on Capital Employed ("ROCE")

A key focus of the Group has been to make efficient use of the capital that we employ. We measure ROCE by dividing profit before financing and taxation by average operating assets utilised during the year. Operating assets exclude cash and cash equivalents, borrowings, tax and deferred tax balances.

We were pleased to achieve a further increase in ROCE this year from 34.0% to 34.9%. This reflected the strong trading performance and the continued focus on working capital management.

Net Finance Expense

The net finance expense reduced by 18.4% to £1.27 million. This was due to the strong cash flow achieved during the year. The net finance expense was covered a healthy 9.7 times by operating profit (2005: 7.2 times).

Taxation

The effective tax rate this year was 31.6% compared to 27.6% last year. The rate this year was higher than the standard rate of 30% because of the losses of our USA subsidiary for which no tax asset has been recognised and expense items not deductible for tax purposes. A full reconciliation to the standard rate is shown in note 7 to the financial statements.

During the year, additional tax credits totalling £429,000 relating to share-based payments were recognised. However, under IFRS rules, these had to be taken directly to equity rather than credited to the income statement.

The 2005 tax rate was less than 30% due to tax relief on goodwill payments that had not been previously recognised.

Earnings Per Share and Dividend

Earnings per share increased by 6.8% over last year. The lower rate of growth when compared to pre-tax profit was due to the higher tax charge.

The Board is proposing a final dividend of 4.33p per share (2005: 3.50p) which, when added to the interim dividend of 1.91p (2005: 1.70p) already paid, gives a total dividend for the year of 6.24p (2005: 5.20p).

The 20% increase over last year reflects the strong cash flow performance of the Group and the Board's confidence in the future.

Dechra
Pharmaceuticals PLC

"Throughout the year we have continued to build on the Vetivex range of critical care fluids and have increased market share by 4% to 37.5% on a moving annual total basis and revenue has now exceeded £1.2 million per annum"

Directors' Business Review

Financial Review *continued*

Developing **Pharmaceuticals**
Improving **Animal Health**

Cash Flow

The Group aims to achieve a cash conversion rate of at least 100% (defined as cash generated from operations as a percentage of operating profit). This year, a cash conversion rate of 114% (2005: 120%) was achieved.

Total capital investment during the year was £2.16 million (2005: £2.43 million). The major items were upgrades to our IT systems at NVS and Dales and an expansion of our central warehouse capacity at NVS. This figure also includes £195,000 (2005: £321,000) of development costs that met the criteria for capitalisation.

Financial Position at the End of the Year

	2006 £'000	2005 £'000
Non-current assets		
Intangible assets	7,527	7,039
Property, plant & equipment	5,595	4,946
Deferred tax assets	445	406
	13,567	12,391
Working capital	11,774	12,127
Current tax liability	(2,505)	(2,057)
Net cash/(borrowings)	1,079	(4,859)
Net assets	23,915	17,602

The financial position at the end of the year was strong with equity shareholders' funds standing at £23.9 million. This compares with just £1 million at 30 June 2001, our first year end following the listing of our shares on the London Stock Exchange.

The increase in non-current assets is due to the investments detailed above whilst the reduction in working capital reflects further improvements in receivables days. During the year there was a drive to convert customers of our largest business, NVS, to pay by direct debit. It is pleasing to report that 1,250 accounts are now paying by this means.

The strong cash flow during the year converted net borrowings of £4.9 million at 30 June 2005 to net funds of £1.1 million at 30 June 2006. Shareholders will be aware that the working capital requirements of the Group vary both intra-month and during the course of the year, reaching their peak in the period December–February. The Group will therefore return to a net borrowings situation at the next reporting date of 31 December 2006.

Group Funding

The Group is funded by £28.2 million of called up share capital, a £17.2 million term loan from Bank of Scotland repayable in instalments ending in 2010 and various finance lease and hire purchase contracts.

The Group also has available a £5 million revolving credit facility committed until 2010 and a £4 million overdraft facility renewable annually to fund the Group's working capital requirements. These are only partially utilised at peak working capital points during the year.

Treasury Policy

The Group's treasury policy is set by the Board and monitored by the Group Finance Director.

The Company does not speculate on short-term interest rate or exchange rate movements.

The Group seeks to hedge for interest rate risk between 20% and 80% of its outstanding borrowings. Currently, £5.733 million of outstanding loans are subject to a floor and ceiling arrangement whereby the effects of fluctuations in LIBOR rate are limited to between 4.53% and 5.50%.

All finance leases and hire purchase contracts are at fixed rates.

Foreign exchange exposure is hedged naturally as far as possible by matching receipts and payments in the relevant foreign currency. To this end, the Group maintains Euro and US Dollar accounts. Unmatched foreign currency exposure is hedged by the Group Finance Director in accordance with Group policy.

No borrowings are denominated in foreign currencies.

Liquidity Management
The Group's cash position is monitored on a daily basis by the Group Finance Director. As noted above, 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 show in note 20 to the consolidated financial statements.

Risks and Uncertainties

Like every business, the Group faces risks and uncertainties in both its day-to-day operations and the achievement of its long-term strategic objectives. The Group has well-established procedures for identifying and controlling risk. Significant risks and procedures to control them are reviewed at Divisional Board Meetings on a monthly basis and by the Main Board on a quarterly basis.

The main potential risk areas identified by the Directors are as follows:

Regulatory
Like the human pharmaceutical industry, the veterinary industry is tightly regulated. Our major operational sites are required to be licensed either by the MHRA or the Home Office, and our products by the Veterinary Medicines Directorate ("VMD"). Inspections by these bodies are carried out regularly.

All of our new pharmaceutical products are required to be approved for sale by the relevant Regulatory Authority in each territory.

The main regulatory risks faced by the Group are:

- Failing to operate our businesses in accordance with their licences resulting in disruption to operations.
- Potential reclassification of major pharmaceutical products from prescription only to a lower category causing loss of revenue.
- Failure to satisfy the regulatory authorities on new product submissions causing product launches to be delayed or aborted.
- Changes to the law or adverse reactions causing threat to existing products.

Corporate Veterinary Practices
The growth of corporate veterinary practices has been a feature of the veterinary market over the last few years. Most corporates currently trade with NVS. The rise of corporate practices provides both opportunities and risks to the Group.

The opportunities arise when a corporate group acquires veterinary practices not currently trading with NVS. The risks arise from the potential increased buying power of corporates causing pressure on gross margin. Additionally, a payment default could cause a material impairment charge.

General Market Conditions
The overall veterinary market has shown robust growth for many years. However, there have in the past been periods when the market has suffered a significant slowdown. This can be caused by external "shocks" such as BSE or Foot & Mouth or general economic conditions. Our past experience has been that these slowdowns have been short term in nature. However, given the relatively high operational gearing of NVS, in particular, any future market slowdown could have a material effect on short-term profitability.

Summary of Risks
The Group has procedures in place to control and, as far as possible, mitigate against the above risk factors. It must be emphasized, however, that these procedures can only control rather than eliminate risk.

Directors and Senior Management

Executive Directors

Ian Page
Chief Executive
Aged 45, Ian joined the Group's principal trading subsidiary NVS at its formation in 1989. He was also part of the MBO in 1997. In 1998, he was appointed Managing Director at NVS. He joined the Board in 1997 and became Group 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 veterinary arena.

Simon Evans BCom, ACA
Group Finance Director
Aged 42, 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. He played a major role in the management buy-out of the Group from Lloyds Chemists in 1997 and its subsequent listing on the London Stock Exchange in 2000.

Ed Torr
Development Director
Aged 46, Ed joined NVS as Sales Director in 1997 and he was appointed Managing Director of Arnolds and Dales in 1998. He relinquished this role in 2003 to focus on his Main Board responsibilities, specifically the strategic development of the Group's licensed veterinary pharmaceutical portfolio in key international territories. Prior to joining the Group, he worked within the animal healthcare sector for a number of companies including ICI, Wellcome and Alfa Laval Agri.

Non-Executive Directors

Michael Redmond
Non-Executive Chairman
Aged 62, 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 also Executive Chairman at Synexus Clinical Research PLC. Michael is Chairman of the Nominations Committee.

Malcolm Diamond MBE
Senior Non-Executive Director
Aged 57, Malcolm joined the Board in August 2000 and is also Chairman of the Remuneration Committee. He is a Non-Executive Director at the Unicorn AIM VCT 11 Investment Fund, and a Senior Non-Executive Director at Centurion Electronics Group plc. His other directorships include Chairman at CWO Limited, Jacksons Fencing Limited and My Marketing Limited. In addition, Malcolm advises a number of private businesses on their strategic planning, management development programmes and marketing initiatives. Malcolm was previously Chief Executive at Trifast plc, a role he held for 18 years.

Neil Warner BA, FCA, MCT
Non-Executive Director
Aged 53, 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. He has also held senior positions in Balfour Beatty PLC (formerly BICC Group plc), Alcoa and PricewaterhouseCoopers. Neil is Chairman of the Audit Committee.

1
Pictured from left:
Neil Warner
Michael Redmond
Malcolm Diamond

2
Pictured from left:
Ed Torr
Ian Page
Simon Evans

1 2 3
4 5 6 7

Pictures:
1 Stephen Whitehouse
2 Peter Graham
3 Giles Coley
4 Susan Longhofer
5 Martin Riley
6 Mike Annice
7 Mike Eldred

Dechra
Pharmaceuticals PLC

Senior Management

Mike Annice BSc (Hons), MRPharmS
Managing Director, Dales Pharmaceuticals
Aged 46, 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 Technical Director at the time of the Group's MBO. Mike was appointed Managing Director at Dales in March 2002.

Giles Coley BSc
Managing Director, Arnolds Veterinary Products and Dechra Veterinary Products UK
Aged 44, Giles joined Arnolds in 1999 as Sales & Marketing Manager. He took over the role of Managing Director from Ed Torr in October 2003. Prior to this, Giles spent 14 years with Genus (formerly MMB) in various management roles in agricultural business consultancy. He holds a BSc in Agricultural Technology gained at Harper Adams University.

Mike Eldred BA, MBA
President, US Operations, Dechra Veterinary Products
Aged 36, Mike was appointed in November 2004 to head up the Group's sales and marketing drive in the United States. He has over 12 years' professional experience in the US animal health sector, having held senior positions in business development, sales and operations at Virbac Corporation, and international marketing and operational positions at Fort Dodge Animal Health. Mike began his career with Sanofi Animal Health where he managed the pharmaceutical and biological production planning activities.

Dr Peter Graham
BVMS, PhD, CertVR, DipECVCP, MRCVS
Managing Director of NationWide Laboratories and Cambridge Specialist Laboratory Services
Aged 38, Peter was appointed Managing Director of NationWide Laboratories and Cambridge Specialist Laboratory Services in 2003. Peter graduated from the University of Glasgow Vet School in 1989, where he remained as Small Animal House Physician and Research Scholar until 1995. During this period he was awarded the RCVS Certificate in Veterinary Radiology and a PhD on the Epidemiology and Management of Canine Diabetes Mellitus. He contributed to the initial commercialisation of biochemistry and endocrinology lab services at the University of Glasgow. Between 1995 and 2002, Peter was Assistant Professor at the world's largest specialist veterinary endocrinology laboratory in Michigan State University, USA, leading it as Section Chief from 2000. He was awarded Diplomate of the European College of Veterinary Clinical Pathologists in 2002.

Dr Susan Longhofer
DVM, MS, DipACVIM
Product Development and Regulatory Affairs Director
Aged 48, Susan joined the Group in June 2005. She has 17 years' industry experience in development and worldwide registration of animal health pharmaceuticals having worked for multinational corporations including Virbac Corporation, Heska Corporation and Merck Research Laboratories. Her veterinary degree is from Texas A&M University and her MS is from the University of Wisconsin, Madison. She was awarded Diplomate status in the American College of Veterinary Internal Medicine in 1992. She has a number of Academic and Professional Honours including membership on the Board of Directors of the American Heartworm Society and the Executive Council of the American Academy of Veterinary Pharmacology and Therapeutics.

Martin Riley
Managing Director, National Veterinary Services
Aged 42, Martin was appointed Managing Director of National Veterinary Services in 2005. A graduate of the Welsh Agricultural College in Aberystwyth, Martin has extensive knowledge of the animal healthcare and veterinary sectors. Before joining the Group, he previously held several senior positions over an 18 year period with the pharmaceutical manufacturer Merial Animal Health.

Company Secretary

Stephen Whitehouse, FCCA
Company Secretary
Aged 58, Stephen was appointed Company Secretary at the time of the Group's flotation in 2000. He joined Arnolds Veterinary Products in 1989 as Financial Controller and in 1992, he assumed the role of Financial Director at Arnolds, a position he held until 1994, when he became General Manager/Finance Director. Between 1996 and 1998, he also took on the responsibility as Managing Director. He was also a member of the MBO team in 1997. Prior to joining the Group, he worked for 12 years at GKN Sankey and 10 years at British Oxygen.

Directors' Report

The Directors present their Annual Report and Audited Financial Statements for the year ended 30 June 2006.

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 and financial position at 30 June 2006 are shown in the consolidated income statement on page 43 and balance sheet on page 44. The Directors recommend the payment of a final dividend of 4.33p per share which, if approved by shareholders, will be paid on 24 November 2006 to shareholders registered at 27 October 2006. An Interim Dividend of 1.91p per share was paid on 7 April 2006, making a total dividend for the year of 6.24p (2005: 5.20p). The total dividend payment is £3,231,000 (2005: £2,656,000).

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 on page 2 and the Directors' Business Review on pages 5 to 23.

Directors
The Directors who held office throughout the year were as follows:

M. Redmond (Chairman)
I.D. Page
S.D. Evans
E.T.W. Torr
M.M. Diamond
N.W. Warner

The interests of the Directors in the share capital of the Company are shown in the remuneration report on pages 34 to 39. During the year, no Director had a disclosable material interest in any contract or arrangement with the Company or any of its subsidiaries.

The Company's articles of association require one-third of the Company's Directors to retire by rotation at the annual general meeting and also if they have held office for more than thirty-six months since appointed or last elected.

S.D. Evans and M.M. Diamond retire by rotation and, being eligible, offer themselves for re-election. Biographical details of the Directors can be found on page 24 of this report and accounts.

Political and Charitable Contributions
The Group made no political or charitable contributions during the year.

Research and Development
The Group has a structured research and development programme with the aim of identifying and bringing to market new pharmaceutical products. Investment in research and development is seen as key to further strengthen the Company's competitive position.The expense on this activity for the year ended 30 June 2006 was £1,378,000 (2005: £1,053,000) and a further £195,000 less £60,000 amortisation (2005: £321,000 less £41,000 amortisation) was capitalised as development costs.

Employees
The Group has a policy of offering equal opportunities to employees at all levels in respect of conditions of work. Throughout the Group it is the intention of the Directors to provide possible employment opportunities and training for disabled people and employees who become disabled, having due regard to aptitude and abilities. Further details can be found in our Social, Ethical and Environmental Responsibilities Statement on page 40.

Suppliers
The Company does not follow any code of practice or standard regarding the payment of suppliers but seeks to agree the terms of payment with suppliers prior to the placing of business and it is the Company's policy to settle liabilities by the due date. At 30 June 2006, the Group had an average of 77 days (2005: 77 days) purchases outstanding in creditors. The Company had an average of Nil days (2005: Nil days) purchases outstanding in creditors.

Substantial Shareholdings
As at 17 August 2006, 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
Schroder Investment Management	5,883,851	11.32
Insight Investment	4,509,756	8.68
Legal & General Investment Management	3,964,880	7.63
Barclays Global Investors	3,415,806	6.57
Platinum Fund Managers	2,336,860	4.50
INVESCO Asset Management	2,129,532	4.10
Rathbones	1,937,992	3.73
OLIM	1,591,500	3.06

Audit Information
The Directors who held office at the date of the approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditors are unaware, and each Director has taken all the steps that he ought to have undertaken as a Director to make himself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

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

Directors' Indemnity Insurance
The Directors benefited from qualifying third party indemnity provisions in place during the financial year and at the date of this report.

Annual General Meeting
The 2006 Annual General Meeting of the Company will be held at 10.00 am on 18 October 2006. Notice of the meeting together with the Annual Report and financial statements are posted to shareholders not less 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 are disclosed at the meeting.

In addition to the adoption of the 2005/2006 report and accounts, resolutions dealing with the re-election of Directors and the resolution dealing with the approval of the Directors' remuneration report, there are five other matters which will be considered at the Annual General Meeting. These relate to the reappointment of KPMG Audit Plc as auditors, declaration of the final dividend, the ability for the Directors to unconditionally allot shares up to one-third of the Company's issued share capital plus share option schemes, the disapplication of pre-exemption rights in relation to the previous resolution and to empower the Company to buy back up to 5% of its issued share capital.

By order of the Board

Steve Whitehouse S.P. Whitehouse

S.P. Whitehouse
Company Secretary
Dechra Pharmaceuticals PLC
5 September 2006

Corporate Governance

Revised Combined Code

The Board recognises its accountability to shareholders and is committed to maintaining high standards of corporate governance. In the opinion of the Directors, the Company has complied throughout the period under review with Section 1 of the July 2003 FRC Combined Code on Corporate Governance (the Combined Code) in all aspects apart from the membership of Board Committees, the details of which are set out below.

Application of the principles of the Combined Code

The following report details how the Company has applied the principles of Section 1 of the Combined Code to its activities. Section 1 of the Combined Code sets out the main and supporting principles of good governance for companies, which is split into the sections detailed below.

Board of Directors

The details of the Board of Directors are shown on page 24 and in the Directors' Report on page 26. There is a clear division of responsibilities between the Chairman and Chief Executive. The Chairman is responsible for leadership of the Board, ensuring its effectiveness and setting its agenda. The Chief Executive is responsible for the management of the Company, implementing policies and strategies determined by the Board. The Board consists of the Non-Executive Chairman, two other Non-Executive Directors and three Executive Directors (including the Chief Executive). The Board considers M.M. Diamond to be the Senior Independent Director.

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 as a Non-Executive Director. In addition, no Non-Executive Director has previously been a senior manager of the Company, and has not participated in the Company's incentive bonus scheme or pension scheme.

M. Redmond was considered by the Board to be independent at the date of his appointment as Chairman.

On appointment, the Directors are required to seek election at the first AGM following appointment. 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.

Conduct of Board Meetings

The Board normally has eleven Board Meetings per annum including two meetings where the full year and half year results are dealt with. Strategy meetings are convened as required with a minimum of one meeting per year. In addition, the Board has three standing committees — the Audit, Remuneration and Nominations committees, the details of which are shown on page 29.

The Board has reserved to itself powers relating to matters that it considers significant to the Group's business, operational and financial risks. These include the approval of corporate policies, strategy, 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, Development 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.

Attendance at meetings was as follows:

Name	Board (11 meetings)	Audit (2 meetings)	Remuneration (3 meetings)	Nomination (1 meeting)
Michael Redmond	11	2	3	1
Malcolm Diamond	9	2	3	1
Neil Warner	10	2	3	1
Ian Page	11	N/A	N/A	N/A
Simon Evans	11	N/A	N/A	N/A
Ed Torr	10	N/A	N/A	N/A

Note: N/A denotes that the Director is not a member of this committee, but may attend by invitation of the committee.

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.

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.

The Board has developed a formal process of reviewing its own effectiveness and the effectiveness of the Board committees. This is based on a combination of written reviews by individual Directors, discussion with the Chairman and review by the Board as a whole. As part of this process the Board considers the performance of individual Directors. This process has been undertaken during the year.

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.

Board Committees

The Board has three standing committees — the Audit, Remuneration and Nominations Committees. The Board has reviewed membership of these committees and has confirmed its view that it is appropriate that all the Non-Executives should participate as members of these committees, so that they are fully involved in monitoring the governance issues affecting the Company, including Executive remuneration, succession planning and risk management. There is therefore no provision for fixed periods of membership of the committees nor is the Chairman of the Board excluded from membership as recommended by the Combined Code. The Board considers that the Chairman should continue his membership of the Audit and Remuneration Committees in that he has a wide experience and knowledge gained through his directorships with other companies.

The Board has delegated specific responsibilities to the committees, as described below. The terms of reference of the Audit, Remuneration and Nomination Committees are available on the Company's website and on request to the Company Secretary.

The Audit Committee

The Audit Committee comprises N.W. Warner (Chairman), M. Redmond, and M.M. Diamond. The activities of the Audit Committee are shown in the Audit Committee Report on pages 32 and 33.

The Audit Committee met twice during the year, the attendance record being shown in the table of attendance above.

The Remuneration Committee

The Remuneration Committee comprises M.M. Diamond (Chairman), M. Redmond, and N.W. Warner.

The Remuneration Committee met three times during the year, the attendance record being shown in the table of attendance above. The terms of reference for the Remuneration Committee include the following responsibilities:

- To develop the remuneration strategies that drive performance.
- To provide levels of reward which reflect that performance both for Executive Directors and designated senior managers.
- To approve terms and conditions, bonus schemes, pensions and related matters.

A report on the remuneration of Directors appears on pages 34 to 39.

The Nominations Committee

The Nominations Committee comprises M. Redmond (Chairman), M.M. Diamond, and N.W. Warner.

The Nominations Committee normally meets once a year. The terms of reference of the Nominations Committee include the following responsibilities:

- To oversee the plans for management succession.
- To recommend appointments to the Board.
- To evaluate the effectiveness of the Non-Executive Directors.
- To consider the structure, size and composition of the Board generally.

Internal Control

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

The Group has a well-established framework of internal financial and operational control for identifying, evaluating and managing the risks faced by the Group. This framework has been in place throughout the year under review, and has continued up to the date of approval of the annual report.

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 quarterly thorough review of relevant risk areas and systems of internal control. The review is structured by business area and key risk strategy and is based upon a summary of information prepared and reviewed by divisional management on an ongoing basis. The current review was prepared to 30 June 2006.

The Group'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 due to 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 for the period from 1 July 2005 to the date of approval of the financial statements which has included quarterly business risk reviews and quarterly internal control reporting.

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

External Audit

The external auditors are engaged to express an opinion on the Company's Annual Report and Accounts. They independently and objectively review management's reporting of the Group's consolidated results and financial position. In addition, they review the systems of internal control and the data contained in the Annual Report and Accounts to the level necessary for expressing their audit opinion.

Investor Relations

Relationships with shareholders receive high priority and a rolling programme of meetings between institutional shareholders and Executive Directors is held throughout the year. These meetings are in addition to the annual and interim results presentations and the Annual General Meeting and seek to foster mutual understanding of the Company's and shareholders' objectives. M. Redmond (Chairman) attended a number of the annual results presentations. 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 the Annual Report and financial statements, is posted to shareholders not fewer than 23 days prior to the date of the Annual General Meeting. The information 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 are disclosed at the Meeting.

At the Annual General Meeting there is an opportunity, following the formal business, for informal communications between investors and Directors.

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.

Audit Committee Report

Committee Membership

The members of the Audit Committee are currently:

Neil Warner (Chairman of the Audit Committee)
Michael Redmond (Chairman of the Company)
Malcolm Diamond (Senior Independant Director)

The Audit Committee considers that Neil Warner has recent and relevant financial experience gained through his position as Finance Director of Chloride Group PLC.

Attendance at the meetings by the Committee members is detailed within the Corporate Governance report on page 28.

Committee Meetings and Responsibilities

The Audit Committee met twice during the year ended 30 June 2006. The external auditors attend meetings of the Committee other than when their appointment or performance is being reviewed. The Chief Executive, Group Finance Director and other senior finance staff attend as appropriate.

The performance, cost and independence of the external auditors is reviewed annually by the Audit Committee, together with a review of the level of service provided by the external auditors to the Group.

The Audit Committee has discussions at least once a year with the auditors without management being present.

The scope of the year's audit is discussed in advance by the Audit Committee. Audit fees are reviewed and approved by the Audit Committee. Professional rules require rotation of the Group Audit Engagement Director. This has taken place during the period being reported on.

The annual appointment of the auditors by our shareholders at the Annual General Meeting is a fundamental safeguard but, beyond this, controls are in place to ensure that additional work performed by the auditors is appropriate and subject to proper review as discussed below.

The main responsibilities of the Audit Committee are set out in the written terms of reference and are:

- To monitor the integrity of the financial statements of the Company, reviewing the annual and interim reports in detail to ensure they present a balanced assessment of the Company's position and prospects which is understandable to shareholders and potential investors.
- To review the effectiveness of the Company's internal controls and risk management systems as described on page 30 and, in conjunction with the auditors, consider the accounting policies adopted by the Company.
- To review the Company's whistle-blowing arrangements.
- To oversee the relationship with the external auditors. The Committee makes recommendations to the Board on the appointment of the external auditors, approves their remuneration, monitors their independence and objectivity, and monitors the effectiveness of the audit process and sets the policy for non-audit work.
- To make recommendations to the Board on the requirement for an internal audit function.

Given the systems of internal control discussed on page 30, and due to the present size of the Group, the Audit Committee currently believes that an internal audit function is not required.

Auditor Independence

With respect to non-audit assignments undertaken by the external auditors, the Company has developed a policy to ensure that the provision of such services does not impair their independence or objectivity. When considering the use of the external auditors to undertake non-audit work, the Chief Executive and Group Finance Director do at all times give consideration to the provisions of the Smith report with regard to the preservation of independence.

The Chief Executive and the Group Finance Director have authority to commission the external auditors to undertake non-audit work where there is a specific project with a cost not exceeding £25,000 and total non-audit fees in any year do not exceed £80,000. This work has to be reported to the Audit Committee at the meeting where the Annual Report is considered. If the cost is expected to exceed the established levels then the prior approval of the Audit Committee is required before the work is commissioned. In all cases, other potential providers are adequately considered.

The external auditors annually confirm their policies on ensuring audit independence and provide the Committee with a report on their own audit quality procedures.

Effectiveness Review

During the year, the Committee reviewed its own effectiveness through a process led by the Committee Chairman. The results of the review were advised to the Committee and the Board.

Based on the Committee's review of the performance of the external auditors and on the planning and execution of the annual audit, the Committee has recommended to the Board that a resolution to reappoint KPMG Audit Plc be proposed at the forthcoming Annual General Meeting.

Neil W. Warner.

N.W. Warner
Chairman — Audit Committee
5 September 2006

Directors' Remuneration Report

This Report is presented in accordance with Schedule B of the Combined Code annexed to the listing rules of the FSA 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 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 attendance record of the members is shown on page 28.

During the year, the Remuneration Committee received advice from New Bridge Street Consultants LLP on executive remuneration, pensions and other benefits.

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 Incentive Plan and the Executive Bonus Scheme are performance related. Bonuses are non-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 of the Remuneration Committee, where considered appropriate, will consult the Company's principal shareholders regarding remuneration issues. This Remuneration Report 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 reviewed annually and is determined taking into account the responsibilities and performance of the individual, together with independently furnished information on rates for similar positions 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 38.

Benefits in kind

Executive Directors receive other benefits, including the use of a fully expensed car, medical cover and life insurance. This provides an overall package that is competitive with similar companies.

Pensions

The Company operates a Group Stakeholder personal pension scheme which has been effective since 1 July 2005. The previous pension scheme was closed on 25 July 2006, all contributions having been transferred to a S32a contract.

Share Option Schemes

The Company operates the Approved Share Option Scheme, the Unapproved Share Option Scheme together with a savings related share option scheme. Executive Directors are entitled to participate in the Company savings related share option ("SAYE") scheme and the Executive Incentive Plan discussed below. However, Executive Directors are not entitled to participate in either the Approved Share Option Scheme or the Unapproved Share Option Scheme. The table on page 39 provides an analysis of outstanding SAYE Directors' Share Options.

Executive Incentive Plan

Following its approval by shareholders at the Annual General Meeting on 23 October 2003, the Company operates the Executive Incentive Plan for Executive Directors and other key employees.

The Executive Incentive Plan aims to provide a clear link between the remuneration of Executive Directors and the creation of value for shareholders by rewarding Executive Directors for the Company's performance in terms of Total Shareholder Return ("TSR").

Under this plan, the Remuneration Committee makes awards to Senior Executives of shares in the Company, with vesting to individuals being subject to the achievement of performance targets. The first target is based on TSR over a three year measurement period (commencing at the beginning of the financial year in which the awards are made) expressed as an annual percentage return over that period. The TSR is calculated and compared to the TSR's of all other companies in the FTSE Small Cap Index for the entire measurement period. 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 over the measurement period, all of the shares over which an award had been made will vest.

If the TSR of the Company is ranked in the second quartile then the number of shares which will vest is determined by reference to a straight-line graph which ensures that 30% of the shares over which the award has been made will vest on the achievement of a TSR that places the Company at the bottom of the second quartile and all of the shares will vest on an achievement of a TSR that places the Company at the top of the second quartile.

If the TSR of the Company is ranked in the third or fourth quartile then none of the shares over which an award had been made will vest and the relevant participant will 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.

Initial awards granted under the Plan were made during the year ended 30 June 2004, the measurement period for these awards commencing on 1 July 2003 and ended on 30 June 2006. In accordance with the rules of the plan, awards granted since the initial award are limited to 50% of basic salary. The measurement period for the grants for this financial year commenced on 1 July 2005 and ends on 30 June 2008. The levels of grants made under the first three years of the scheme are shown on page 38.

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.

Executive bonuses for the year ended 30 June 2006 for the achievement of group performance targets are set out below.

	Bonus payable for achievement of 95% of profit target (% of Salary)
I.D. Page	30%
S.D. Evans	21%
E.T.W. Torr	21%

In addition, for I.D. Page an additional 20% will be payable on achievement of 105% of target. This bonus will be pro-rated on achievement of between 95% and 105% of target.

S.D. Evans and E.W. Torr will receive an additional 14% on achievement of 105% of target. This bonus will be pro-rated on achievement of between 95% and 105% of target.

Directors' Remuneration Report

Executive Directors' bonus payments for the forthcoming year will have a potential maximum of 60% of salary. The payable thresholds are as follows:

	Bonus payable for achievement of profit target (% salary)
Achievement of 95% of target	7%
Achievement of 97.5% of target	25%
Achievement of 100% of target	33%
Achievement of up to 105% of target	42%
Achievement of over 105% of target	50%

An additional 10% bonus will be payable on the achievement of personal objectives set by the Chairman for the Chief Executive, and by the achievement of personal objectives set by the Chief Executive for the Executive Directors.

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 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.

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

		Notice Period	
Name	Commencement	Director	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.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 a deduction at source of income tax and national insurance contributions).

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

Non-Executive Directors' compensation is confined to 12 months' remuneration.

Individual Directors' eligibility for the various elements of compensation is 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.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 2006 and their families in the share capital of Dechra Pharmaceuticals PLC were as follows:

Shareholdings	**Ordinary Shares 2006**	Ordinary Shares 2005
M. Redmond	**35,000**	35,000
I.D. Page	**592,167**	592,167
S.D. Evans	**669,131**	669,131
E.T.W. Torr	**343,832**	343,832
M.M. Diamond	**5,000**	5,000
N.W. Warner	**2,206**	2,206

Total Shareholder Return

The adjacent graph shows the total shareholder return performance of the Company over the past six 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.

The information shown relates to the six-year period since the Company's flotation on the London Stock Exchange in September 2000. Total shareholder return is the performance target for the Executive Incentive Plan.

Directors' Remuneration Report

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 2006 £'000**	Total 2005 £'000
Executive Directors					
I.D. Page (Chief Executive)	175	74	20	**269**	229
S.D. Evans	120	35	14	**169**	140
E.T.W. Torr	115	34	15	**164**	140
Non-Executive Directors					
M. Redmond (Chairman)	46	—	—	**46**	41
M.M. Diamond	26	—	—	**26**	24
N.W. Warner	24	—	—	**24**	21
	506	143	49	**698**	595

Executive Incentive Plan

Awards made under the Executive Incentive Plan are as follows:

	Initial share price at date of award pence	Award date	Exercise dates	Performance period	**2006 Number of shares**	2005 Number of shares	2004 Number of shares
I.D. Page	126	2003	2006–2007	2003–2006	**120,000**	120,000	120,000
	159.5	2004	2007–2008	2004–2007	**48,589**	48,589	
	251	2005	2008–2009	2005–2008	**34,861**		
S.D. Evans	126	2003	2006–2007	2003–2006	**80,000**	80,000	80,000
	159.5	2004	2007–2008	2004–2007	**33,096**	33,096	
	251	2005	2008–2009	2005–2008	**23,904**		
E.T.W. Torr	126	2003	2006–2007	2003–2006	**80,000**	80,000	80,000
	159.5	2004	2007–2008	2004–2007	**31,348**	31,348	
	251	2005	2008–2009	2005–2008	**22,908**		

The actual performance target in respect of the 2003 scheme has been calculated and confirms that Dechra Pharmaceuticals PLC Total Shareholder return for the three-year period to 30 June 2006 has resulted in a performance that places the Company in the top quartile of the FTSE small cap comparator group of companies for the measurement period. The full award for 2003 is therefore exercisable in accordance with the plan rules.

SAYE Scheme

Directors' entitlements under the SAYE Scheme are as follows:

	Award date	Market price at date of grant pence	Exercise price pence	Exercise dates	At 30 June 2005 number	Exercised number	Granted number	Lapsed number	**At 30 June 2006 number**
I.D. Page	3 April 2003	48	39	June 2008	42,115	—	—	—	**42,115**
S.D. Evans	15 October 2004	198	158	Jan 2008	7,641	—	—	—	**7,641**
E.T.W. Torr	15 October 2004	198	158	Jan 2008	3,056	—	—	—	**3,056**
	18 October 2005	255	204	Dec 2008	—	—	2,750	—	**2,750**
					52,812	—	2,750	—	**55,562**

The middle market price for the Company's shares on 30 June 2006 was 240p and the range of prices during the year was 210p to 267.25p.

Pension Entitlement

All Executive Directors were members of the Dechra Pharmaceutical PLC Group Stakeholder personal pension 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 2006 £000**	Contributions 2005 £000
I.D. Page	45	**21**	19
S.D. Evans	42	**14**	13
E.T.W. Torr	46	**14**	12
		49	44

Effectiveness Review

During the year, the Committee reviewed its effectiveness through a process led by the Committee Chairman. The findings were reported to the Committee and the Board.

By order of the Board

M.M. Diamond
Chairman Remuneration Committee
5 September 2006

Social, Ethical and Environmental Responsibilities

A responsible approach to our stakeholders and the wider community is seen by the Board to be fundamental to the Group. The conduct of the Group towards social, environmental, ethical and health and safety issues is recognised to have an impact on our reputation and the implementation of policies and systems continues.

The Board takes ultimate responsibility for corporate social responsibility (CSR) and continues to be committed to developing and implementing appropriate policies to create and maintain long-term value for shareholders. Sound business ethics help to minimise risk, ensure legal compliance and enhance company efficiency. The need to review and manage risks to the short and long-term value of the Company arising from CSR is recognised by the Board and it considers that it has received adequate information to review these risks and has not identified any risks to the business that could affect its future value.

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

The Group is a registered member of a compliance scheme in respect of the Waste Packaging Obligations Regulations and, in addition, all of the National Veterinary Services depots recycle waste cardboard back to UK paper mills, and waste polythene is also recycled back to UK recycling agents.

A fleet of low CO^2 emission diesel vehicles is maintained with these vehicles being replaced every three years via leasing agreements. In addition, a number of LPG powered vehicles are being used in and around the London area.

Our manufacturing unit continues to comply with and better effluent discharge standards into local water supplies, this being monitored by Yorkshire Water Authority. Standard operating procedures are in operation to ensure that contaminated waste is disposed of under strict controls. Exhaust air is fully filtered from the manufacturing unit before discharge. This unit continues its work towards ISO14001 status.

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

The Development Director is the nominated Director responsible for environmental policies.

Business Ethics
The Board expects all of the Group's business activities to be conducted in accordance with high standards of ethical conduct and full compliance with all applicable national and international legislation. This includes, in particular, the provision of a safe working environment including health and safety awareness, maintenance of fair and competitive employment practices, opposition to any bribery or corrupt business practices, treating suppliers on a fair basis to build long-term relationships to our mutual benefit, and being responsive for our customers' needs and providing a high standard of customer care.

A "whistle-blowing" policy is in place whereby employees may report, in confidence, any suspect wrongdoings within the business where they feel unable to discuss any such issue directly with local management. This policy is available to all employees via staff handbooks and the Dechra Pharmaceuticals web site.

Open and honest communication is positively encouraged between employees and management throughout the business.

Health and Safety Policy
Dechra Pharmaceutical 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. All of its sites are registered with the British Safety Council.

Each unit within the Group has an active Health and Safety Committee comprising representatives from both management and employees. The workforce nominates employee representatives. These committees meet on a regular basis to carry out a review of risk assessments and standard operating procedures as well as investigating any concerns raised by individual employees. Each site has the requisite number of employees trained in Health and Safety legislation.

A full health and safety report is presented at Divisional Board Meetings on a regular basis in the presence of Executive Directors. These reports are summarised for subsequent review by the Board.

A transport risk review committee has been established to assess risks related to the vehicle fleet and establish control procedures. This includes a quarterly licence check of all individuals who are able to drive company vehicles, an investigation into all accidents and a disciplinary procedure for speeding offences. It is proposed to introduce driver assessments during the coming year. This committee meets six times a year and issues raised by this committee are included at Health and Safety meetings.

The Finance Director is the nominated Director responsible for Health and Safety policy.

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. The manufacturing site is registered with "Investors in People" and operates a Works Council.

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 from disabled people, where they adequately fulfil the requirements of the role.

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 has encouraged employees to share in the growth of the Company through eligibility to participate in the SAYE share option scheme.

Statement of Directors' Responsibilities in respect of the Annual Report and the Financial Statements

The Directors are responsible for preparing the Annual Report and the Group and Parent Company financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and Parent Company financial statements for each financial year. Under that law they are required to prepare the Group financial statements in accordance with IFRSs as adopted by the EU and have elected to prepare the Parent Company financial statements in accordance with UK Accounting Standards.

The Group financial statements are required by law and IFRSs as adopted by the EU to present fairly the financial position and the performance of the Group; the Companies Act 1985 provides in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation.

The Parent Company financial statements are required by law to give a true and fair view of the state of affairs of the Parent Company.

In preparing each of the Group and Parent Company 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;
- for the Group financial statements, state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- for the Parent Company financial statements, state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the Parent Company financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the Parent Company will continue in business.

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Parent Company and enable them to ensure that its 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. Under applicable law and regulations, the Directors are also responsible for preparing a Directors' Report, Directors' Remuneration Report and Corporate Governance Statement that comply with that law and those regulations.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Independent Auditors' Report to the Members of Dechra Pharmaceuticals PLC

We have audited the Group and Parent Company financial statements (the "financial statements") of Dechra Pharmaceuticals PLC for the year ended 30 June 2006 which comprise the Consolidated Income Statement, the Consolidated and Parent Company Balance Sheets, the Consolidated Statement of Cash Flows, the Consolidated Statement of Changes in Shareholders' Equity and the related notes. These financial statements have been prepared under the accounting policies set out therein. 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' responsibilities for preparing the Annual Report and the Group financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU, and for preparing the Parent Company financial statements and the Directors' Remuneration Report in accordance with applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities on page 41.

Our responsibility is to audit the financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

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 and, as regards the Group financial statements, Article 4 of the IAS Regulation. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements. The information given in the Directors' Report includes that specific information presented in the Directors' Business Review that is cross-referenced from the Business Review and Future Developments section of the Directors' Report. We also report to you if, in our opinion, 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 other transactions is not disclosed.

We review whether the Corporate Governance Statement reflects the Company's compliance with the nine provisions of the 2003 FRC Combined Code specified for our review by the Listing Rules of the Financial Services Authority, 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 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. Our responsibilities do not extend to any other information.

Basis of audit opinion
We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) 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 and Company'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 Group financial statements give a true and fair view, in accordance with IFRSs as adopted by the EU, of the state of the Group's affairs as at 30 June 2006 and of its profit for the year then ended;
- the Parent Company financial statements give a true and fair view, in accordance with UK Generally Accepted Accounting Practice, of the state of the Parent Company's affairs as at 30 June 2006;
- 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 and, as regards the Group financial statements, Article 4 of the IAS Regulation; and
- the information given in the Directors' Report is consistent with the financial statements.

KPMG Audit Plc

KPMG Audit Plc
Chartered Accountants
Registered Auditor
5 September 2006

2 Cornwall Street
Birmingham
B3 2DL

Consolidated Income Statement

For the year ended 30 June 2006

	Note	Year ended 30 June **2006** £'000	2005 £'000
Revenue	2	**232,471**	210,267
Cost of sales		**(199,205)**	(180,550)
Gross profit		**33,266**	29,717
Distribution costs		**(10,309)**	(9,073)
Administrative expenses		**(10,645)**	(9,389)
Operating profit	2	**12,312**	11,255
Finance income	3	**725**	355
Finance expense	4	**(1,993)**	(1,909)
Profit before taxation	5	**11,044**	9,701
Income tax expense	7	**(3,487)**	(2,674)
Profit for the year attributable to equity holders of the parent		**7,557**	7,027
Earnings per share (pence)			
Basic	9	**14.71p**	13.77p
Diluted	9	**14.36p**	13.54p
Dividend per share (interim paid and final proposed for the year)	8	**6.24p**	5.20p

Consolidated Balance Sheet

At 30 June 2006

	Note	As at 30 June 2006 £'000	2005 £'000
ASSETS			
Non-current assets			
Intangible assets	10	**7,527**	7,039
Property, plant and equipment	11	**5,595**	4,946
Deferred tax assets	13	**445**	406
Total non-current assets		**13,567**	12,391
Current assets			
Inventories	14	**21,957**	20,390
Trade and other receivables	15	**35,347**	33,708
Cash and cash equivalents	16	**19,738**	13,924
Total current assets		**77,042**	68,022
Total assets		**90,609**	80,413
LIABILITIES			
Current liabilities			
Borrowings	19	**(3,417)**	(1,502)
Trade and other payables	17	**(45,530)**	(41,971)
Current tax liabilities	18	**(2,505)**	(2,057)
Total current liabilities		**(51,452)**	(45,530)
Non-current liabilities			
Borrowings	19	**(15,242)**	(17,281)
Total non-current liabilities		**(15,242)**	(17,281)
Total liabilities		**(66,694)**	(62,811)
Net assets		**23,915**	17,602
EQUITY			
Issued share capital	21	**519**	511
Share premium account		**27,693**	26,953
Hedging reserve		**(71)**	—
Merger reserve		**1,720**	1,720
Retained earnings		**(5,946)**	(11,582)
Total equity attributable to equity holders of the parent		**23,915**	17,602

The financial statements were approved by the Board of Directors on 5 September 2006 and are signed on its behalf by:

I.D. Page Director

S D Evans

S.D. Evans Director

Consolidated Statement of Changes in Shareholders' Equity

For the year ended 30 June 2006

Year ended 30 June 2005	Issued *share* capital £'000	Share *premium* account £'000	Hedging reserve £'000	Merger reserve £'000	Retained earnings £'000	Total £'000
At 1 July 2004	510	26,784	—	1,720	(17,012)	12,002
Profit for the period being total recognised income and expense for the period	—	—	—	—	7,027	7,027
Dividends paid	—	—	—	—	(2,473)	(2,473)
Share-based payments including deferred tax	—	—	—	—	876	876
Shares issued	1	169	—	—	—	170
At 30 June 2005	511	26,953	—	1,720	(11,582)	17,602
Year ended 30 June 2006						
At 1 July 2005 as previously stated	511	26,953	—	1,720	(11,582)	17,602
Impact of adoption of IAS32 and IAS39 on 1 July 2005 (see note 1(g))	—	—	(71)	—	—	(71)
At 1 July 2005 — restated	511	26,953	(71)	1,720	(11,582)	17,531
Profit for the period being total recognised income and expense for the period	—	—	—	—	7,557	7,557
Dividends paid	—	—	—	—	(2,777)	(2,777)
Share-based payments including current and deferred tax	—	—	—	—	856	856
Shares issued	8	740	—	—	—	748
At 30 June 2006	**519**	**27,693**	**(71)**	**1,720**	**(5,946)**	**23,915**

Consolidated Statement of Cash Flows

For the year ended 30 June 2006

	Year ended 30 June	
	2006	2005
	£'000	£'000
Cash flows from operating activities		
Profit for the period	**7,557**	7,027
Adjustments for:		
Depreciation	**886**	902
Amortisation	**136**	74
Gain on sale of property, plant and equipment	**(23)**	(42)
Finance income	**(725)**	(355)
Finance expense	**1,993**	1,909
Equity-settled share-based payment expenses	**427**	488
Income tax expense	**3,487**	2,674
Operating cash flow before changes in working capital	**13,738**	12,677
Increase in inventories	**(1,567)**	(3,411)
Increase in trade and other receivables	**(1,736)**	(787)
Increase in trade and other payables	**3,562**	5,070
Cash generated from operations	**13,997**	13,549
Interest paid	**(1,890)**	(2,022)
Income taxes paid	**(2,618)**	(1,996)
Net cash from operating activities	**9,489**	9,531
Cash flows from investing activities		
Proceeds from sale of property, plant and equipment	**23**	140
Interest received	**672**	355
Purchase of property, plant and equipment	**(1,320)**	(644)
Capitalised development expenditure	**(195)**	(321)
Purchase of other intangible fixed assets	**—**	(1,100)
Net cash from investing activities	**(820)**	(1,570)
Cash flows from financing activities		
Proceeds from the issue of share capital	**780**	138
New borrowings	**705**	13,160
Repayment of borrowings	**(1,582)**	(1,538)
Dividends paid	**(2,777)**	(2,473)
Net cash from financing activities	**(2,874)**	9,287
Net increase in cash and cash equivalents	**5,795**	17,248
Cash and cash equivalents at start of period	**13,924**	(3,324)
Cash and cash equivalents at end of period	**19,719**	13,924
Shown as:		
Cash and cash equivalents	**19,738**	13,924
Bank overdraft	**(19)**	—
	19,719	13,924

Reconciliation of net cash to movement in net borrowings

		Year ended 30 June	
		2006	2005
	Note	**£'000**	£'000
Net increase in cash and cash equivalents		**5,795**	17,248
Repayment of borrowings		**1,582**	1,538
New borrowings		**(705)**	(13,160)
New finance leases		**(649)**	(438)
Other non-cash changes		**(85)**	63
Movement in net borrowings in the period		**5,938**	5,251
Net borrowings at start of period		**(4,859)**	(10,110)
Net cash/(borrowings) at end of period	23	**1,079**	(4,859)

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

1. Accounting Policies

Dechra Pharmaceuticals PLC is a company domiciled in the United Kingdom. The consolidated financial statements of the Group for the year ended 30 June 2006 comprise the Company and its subsidiaries.

(a) Statement of Compliance

The consolidated financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union and with those parts of the Companies Act 1985 applicable to companies reporting under IFRS ("adopted IFRS"). The Company has elected to prepare its Parent company financial statements in accordance with UK GAAP and are separately presented on pages 73 to 82.

The accounting policies set out below have, unless otherwise stated, been applied consistently to all periods presented in these Group financial statements and in preparing an opening IFRS balance sheet at 1 July 2004 for the purposes of the transition to adopted IFRSs. The principal exemption is that, as more fully explained below, financial instruments accounting is determined on a different basis in 2006 and 2005 due to the transitional provisions of IAS32 and IAS39.

Reconciliations of the income statement, balance sheet and net equity from previously reported UK GAAP to IFRS are shown in note 27.

The Group's significant accounting policies are listed below:

(b) First Time Adoption

The Group has applied IFRS1 'First time adoption of International Financial Reporting Standards' in its initial application of IFRS. The Group is required to select appropriate accounting policies under IFRS and, subject to a few exemptions detailed below, apply them retrospectively to its financial statements such that all comparative information is presented on the same basis. Accordingly this necessitates the restatement of the balance sheet at 1 July 2004, the date of transition (this being the date of the beginning of the earliest financial year for which full comparative information is required) as well as at 30 June 2005.

IFRS1 permits certain exemptions to the full retrospective restatement. The exemptions that have been adopted by the Group are as follows:

Business combinations — business combinations made prior to 1 July 2004 have not been restated in accordance with IFRS3 'Business Combinations'.

Share-based payments — IFRS2 'Share-based payments' has only been applied to awards of share options granted after 7 November 2002 which had not vested by 1 January 2005.

Financial instruments — IAS32 'Financial Instruments: Disclosure and Presentation' and IAS39 'Financial Instruments: Recognition and Measurement' have been adopted prospectively from 1 July 2005 with no restatement of comparative information which continues to be presented in accordance with UK GAAP.

(c) Basis of Preparation

The financial statements are presented in Sterling, rounded to the nearest thousand. They are prepared on the historical cost basis except for derivative financial instruments that are stated at fair value.

The preparation of financial statements in conformity with adopted IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

The restated financial information for the transition to IFRS at 1 July 2004 and the year ended 30 June 2005 and the adoption of IAS32 and IAS39 at 1 July 2005 has been prepared in accordance with adopted IFRS and consistently in accordance with the accounting policies as set out below.

IFRS7 'Financial Instruments Disclosure' has not yet been applied. IFRS7 is applicable to years commencing on or after 1 January 2007 and was available for early application but has not yet been applied by the Group in these financial statements.

The application of IFRS7 in the year to 30 June 2006 would not have affected the income statement or balance sheet as the standard is concerned only with disclosure. The Group plans to adopt it in the year to 30 June 2008.

(d) Basis of Consolidation

(i) Subsidiaries

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

1. Accounting Policies continued

(ii) Transactions Eliminated on Consolidation

Intra-group balances and any unrealised gains and losses or income and expenses arising from intra-group transactions are eliminated in preparing the consolidated financial statements.

(e) Foreign Currency Transactions

Transactions in foreign currencies are translated at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to Sterling at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to Sterling at the foreign exchange rates ruling at the dates the fair value was determined.

(f) Derivative Financial Instruments (applicable to 30 June 2005)

All financial assets and liabilities are carried at cost (amortised as appropriate) less, in the case of financial assets, provisions for permanent diminution in value.

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 FRS13 "derivatives and other financial instrument disclosures" as detailed in note 20.

(g) Derivative Financial Instruments (applicable from 1 July 2005)

The Group uses derivative financial instruments to manage its exposure to foreign exchange and interest rate risks. In accordance with its treasury policy, the Group does not hold or issue derivative financial instruments for speculative purposes. However, derivatives that do not qualify for hedge accounting are accounted for as trading instruments.

On adoption of IAS32 and IAS39, the comparative financial statements have not been restated. As permitted under IFRS1 'First time adoption of International Financial Reporting Standards' the comparative statements continue to hedge account under UK GAAP. On 1 July 2005, the fair values of derivatives used for hedging were included in a hedging reserve. The corresponding adjustments were to decrease trade and other receivables by £58,000, increase trade and other payables by £44,000 and increase the deferred tax asset by £31,000. As the Group has not adopted hedge accounting under IAS39 from 1 July 2005 the hedging reserve is frozen and will only be released to the income statement when the related forecast transactions occur.

Derivative financial instruments are recognised initially at fair value. Subsequent to initial recognition, derivative financial instruments are stated at fair value. The gain or loss on remeasurement to fair value is recognised immediately in the income statement.

The fair value of interest rate swaps, floors and ceilings is the estimated amount that the Group would receive or pay to terminate the instrument at the balance sheet date. The fair value of forward exchange contracts and options is their quoted market price at the balance sheet date, being the present value of the quoted forward price.

(h) Property, Plant and Equipment

(i) Owned Assets

Items of property, plant and equipment are stated at cost less accumulated depreciation (see below) and impairment losses (see accounting policy m).

(ii) Leased Assets

Leases under the terms of which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Assets acquired by finance leases are stated at an amount equal to the lower of their fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation and impairment losses.

(iii) Subsequent Costs

The Group recognises in the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied with the item will flow to the Group and the cost of the item can be measured reliably. All other costs are recognised in the income statement as an expense as incurred.

(iv) Depreciation

Depreciation is charged to the income statement on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. Land is not depreciated. Assets in the course of construction are not depreciated until the date the assets become available for use. The estimated useful lives are as follows:

• short leasehold buildings	period of lease
• plant and fixtures	10%–33⅓%
• motor vehicles	25%

The residual value, if not insignificant, is reassessed annually.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

1. Accounting Policies continued

(i) Intangible Assets

(i) Goodwill

All business combinations are accounted for by applying the purchase method. Goodwill represents amounts arising on acquisition of subsidiaries, associates and joint ventures. In respect of business acquisitions that have occurred since 1 July 2004, goodwill represents the difference between the cost of the acquisition and the fair value of the net identifiable assets acquired.

In respect of acquisitions prior to this date, goodwill is included on the basis of its deemed cost, which represents the amount recorded under previous GAAP. The classification and accounting treatment of business combinations that occurred prior to 1 July 2004 has not been reconsidered in preparing the Group's opening IFRS balance sheet at 1 July 2004.

Goodwill is stated at cost less any accumulated impairment losses. Goodwill is not amortised but is allocated to cash generating units and is tested annually for impairment.

(ii) Research and Development Costs

Expenditure on research activities, undertaken with the prospect of gaining new scientific or technical knowledge and understanding, is recognised in the income statement as an expense is incurred.

The Group is also engaged in development activity with a view to bringing new pharmaceutical products to market. Internally generated costs of development are capitalised in the balance sheet unless those costs cannot be measured reliably or it is not probable that future economic benefits will flow to the Group, in which case the relevant costs are expensed to the income statement as incurred. Due to the strict regulatory process involved, there is inherent uncertainty as to the technical feasibility of development projects often until regulatory approval is achieved, with the possibility of failure even at a late stage. The Group considers that this uncertainty means that the criteria for capitalisation are not met unless it is highly probable that regulatory approval will be achieved and the project is commercially viable.

Where development costs are capitalised, the expenditure includes the cost of materials, direct labour and an appropriate proportion of overheads.

Capitalised development expenditure is stated at cost less accumulated amortisation and impairment losses.

(iii) Other Intangible Assets

Other intangible assets that are acquired by the Group are stated at cost less accumulated amortisation and impairment losses. Expenditure on internally generated goodwill and other intangibles is recognised in the income statement as an expense is incurred.

(iv) Subsequent Expenditure

Subsequent expenditure on capitalised intangible assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

(v) Amortisation

Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of intangible assets unless such lives are indefinite. Goodwill and intangible assets with an indefinite useful life are systematically tested for impairment at each balance sheet date. Other intangible assets are amortised from the date that they are available for use. The estimated useful lives are as follows:

● software	5 years
● capitalised development costs	5–10 years
● patent rights	Period of patent
● marketing authorisations	Indefinite life
● product rights	Period of product rights

(j) Trade and Other Receivables

Trade and other receivables are stated at their amortised cost.

(k) Inventories

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

The cost of inventories is based on the first-in, first-out principle and includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of overheads based on normal operating capacity.

1. Accounting Policies continued

(l) Cash and Cash Equivalents

Cash and cash equivalents comprise cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

(m) Impairment

The carrying amounts of the Group's assets, other than inventories and deferred tax assets, are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated.

The recoverable amount of assets is the greater of their net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

For goodwill, assets that have an indefinite useful life and intangible assets that are not yet available for use, the recoverable amount is estimated at each balance sheet date and, in the case of goodwill, at the date of transition to IFRS.

An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement.

Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the cash-generating units (group of units), and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

An impairment loss in respect of goodwill is not reversed.

In respect of other assets, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(n) Dividends

Dividends are recognised in the period in which they are approved by the Company's shareholders or, in the case of an interim dividend, when the dividend is paid.

(o) Interest-Bearing Borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis.

(p) Employee Benefits

(i) Pensions

The Company operates a Group stakeholder personal pension scheme for certain employees. Obligations for contributions are recognised as an expense in the income statement as incurred.

(ii) Share-Based Payment Transactions

The Group operates a number of equity-settled share-based payment programmes that allow employees to acquire shares of the Company. The Group also operates a Long Term Incentive Plan for Directors and Senior Executives.

The fair value of shares or options granted is recognised as an employee expense on a straight-line basis in the income statement with a corresponding movement in equity. The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the shares or options (the vesting period). The fair value of the shares or options granted is measured using a valuation model taking into account the terms and conditions upon which the shares or options were granted. The amount recognised as an expense in the income statement is adjusted to take into account an estimate of the number of shares or options that are expected to vest together with an adjustment to reflect the number of shares or options that actually do vest except where forfeiture is only due to market-based conditions not being achieved.

The fair value of grants under the Long Term Incentive Plan has been determined using the Monte Carlo simulation model.

The fair values of options granted under all other share option schemes have been determined using the Black-Scholes option pricing model.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

1. Accounting Policies continued

(q) Trade and Other Payables

Trade and other payables are stated at their amortised cost.

(r) Revenue

(i) Goods Sold

Revenue from the sale of goods is recognised in the income statement when the significant risks and rewards of ownership have been transferred to the buyer. This is normally when the buyer takes delivery of the goods. Appropriate provision is made, based on past experience, for the possible return of goods and discounts given to customers.

(ii) Milestone Payments

Milestone payments received from the granting of distribution and marketing rights for products are recognised in the income statement over the period in which the Company fulfils all of its obligations relating to such payments.

(s) Expenses

(i) Operating Lease Payments

Payments made under operating leases are recognised in the income statement on a straight-line basis over the term of the lease. Lease incentives received are recognised in the income statement evenly over the period of the lease, as an integral part of the total lease expense.

(ii) Finance Lease Payments

Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability.

(iii) Net Financing Costs

Net financing costs comprise interest payable on borrowings, interest receivable on funds invested, foreign exchange gains and losses, and gains and losses on hedging instruments that are recognised in the income statement (see accounting policy g).

Interest income is recognised in the income statement as it accrues. The interest expense component of finance lease payments is recognised in the income statement using the effective interest rate method.

(t) Income Tax

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method and represents the tax payable or recoverable on most temporary differences which arise between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes (the tax base). Temporary differences are not provided on: goodwill that is not deductible for tax purposes, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit and do not arise from a business combination; and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates expected to apply in the period in which the liability is settled or the asset is realised and is based upon tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is not probable that the related tax benefit will be realised against future taxable profits. The carrying amounts of deferred tax assets are reviewed at each balance sheet date.

(u) Segment Reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

(v) Operating Profit and Operating Cash Flow

Operating profit and operating cash flow is stated before investment income and finance costs.

2. Segmental Analysis

The Group's primary reporting segment is business divisions which correspond with the way the operating businesses are organised and managed within the Group and its secondary segment is geographical origin.

Segment results, assets and liabilities comprise those items directly attributable to particular segments as well as items which can reasonably be allocated to those segments. Inter-segment transactions are entered into applying normal commercial terms that would be available to third parties.

Unallocated items comprise mainly corporate assets, expenses, loans and borrowings together with the elimination of inter-segment transactions.

The composition of the segments is detailed in the Directors' Business Review section of this report.

The following table analyses revenue and operating profit accordingly:

Business Segment

	Pharmaceuticals		Services		Unallocated		Total	
	2006 £'000	2005 £'000	**2006 £'000**	2005 £'000	**2006 £'000**	2005 £'000	**2006 £'000**	2005 £'000
Revenue								
External customers	**17,001**	15,783	**215,470**	194,484	**—**	—	**232,471**	210,267
Inter-segment	**6,251**	5,598	**86**	127	**(6,337)**	(5,725)	**—**	—
Total revenue	**23,252**	21,381	**215,556**	194,611	**(6,337)**	(5,725)	**232,471**	210,267
Operating profit	**4,868**	4,292	**8,681**	7,973	**(1,237)**	(1,010)	**12,312**	11,255
Finance income							**725**	355
Finance expense							**(1,993)**	(1,909)
Profit before taxation							**11,044**	9,701
Income tax expense							**(3,487)**	(2,674)
Profit for the year							**7,557**	7,027
Assets								
Intangible assets	**5,104**	4,630	**2,423**	2,409	**—**	—	**7,527**	7,039
Property, plant and equipment	**3,571**	3,590	**2,024**	1,356	**—**	—	**5,595**	4,946
Other assets	**11,071**	9,460	**64,235**	57,058	**2,181**	1,910	**77,487**	68,428
Total assets	**19,746**	17,680	**68,682**	60,823	**2,181**	1,910	**90,609**	80,413
Liabilities								
Borrowings	**(508)**	(33)	**(1,056)**	(340)	**(17,095)**	(18,410)	**(18,659)**	(18,783)
Other liabilities	**(3,026)**	(3,842)	**(41,965)**	(37,964)	**(3,044)**	(2,222)	**(48,035)**	(44,028)
Total liabilities	**(3,534)**	(3,875)	**(43,021)**	(38,304)	**(20,139)**	(20,632)	**(66,694)**	(62,811)
Net assets/(liabilities)	**16,212**	13,805	**25,661**	22,519	**(17,958)**	(18,722)	**23,915**	17,602
Other Segment Items								
Capital expenditure								
— intangible assets	**552**	1,421	**72**	288	**—**	—	**624**	1,709
— property, plant and equipment	**469**	341	**1,066**	381	**—**	—	**1,535**	722
Total capital expenditure	**1,021**	1,762	**1,138**	669	**—**	—	**2,159**	2,431
Share-based payments charge	**—**	—	**—**	—	**515**	398	**515**	398
Depreciation and amortisation	**566**	490	**456**	486	**—**	—	**1,022**	976

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

2. Segmental Analysis continued

Geographical Segment

In presenting information on the basis of geographical segments, IAS14 'Segment Reporting' requires segment revenues to be based on the geographical location of customers. In this respect, £228,191,000 arises from customers in the UK (2005: £207,173,000) and £4,280,000 from customers in the rest of the world (2005: £3,094,000). The table below gives additional information in respect of segment revenue and segment operating profit, based on the geographical location of the business unit supplying the goods or services. Segment assets and capital expenditure are based on the geographical location of the assets and expenditure. Activities in the UK comprise all operating segments. Overseas operations comprise pharmaceuticals only.

	UK		USA		Unallocated		Total	
	2006 £'000	2005 £'000	**2006 £'000**	2005 £'000	**2006 £'000**	2005 £'000	**2006 £'000**	2005 £'000
Revenue by geographical origin	**232,145**	210,267	**326**	—	**—**	—	**232,471**	210,267
Operating profit by geographical origin	**13,809**	12,450	**(260)**	(185)	**(1,237)**	(1,010)	**12,312**	11,255
Total assets	**88,190**	78,453	**238**	50	**2,181**	1,910	**90,609**	80,413
Capital expenditure								
— intangible assets	**624**	1,709	**—**	—	**—**	—	**624**	1,709
— property, plant and equipment	**1,532**	709	**3**	13	**—**	—	**1,535**	722
Total capital expenditure	**2,156**	2,418	**3**	13	**—**	—	**2,159**	2,431

3. Finance Income

	2006 £'000	2005 £'000
Bank interest receivable	**627**	355
Other interest receivable	**52**	—
Fair value gains on derivative financial instruments	**46**	—
Total finance income	**725**	355

4. Finance Expense

	2006 £'000	2005 £'000
Bank loans and overdrafts	**1,913**	1,877
Finance charges payable on finance leases and hire purchase contracts	**64**	32
Fair value losses on derivative financial instruments	**16**	—
Total finance expense	**1,993**	1,909

5. Profit before Taxation

The following items have been included in arriving at profit before taxation:

	2006 £'000	2005 £'000
Cost of inventories recognised as an expense	**197,127**	178,933
Impairment of inventories included in above figure	**83**	521
Depreciation of property, plant and equipment		
— owned assets	**802**	807
— under finance leases	**84**	95
Amortisation of intangible assets	**136**	74
(Profit) on disposal of property, plant and equipment	**(23)**	(42)
Impairment of receivables	**455**	767
Operating lease rentals payable	**2,042**	1,776
Research and development expenditure as incurred	**1,378**	1,053
Auditors' remuneration for audit services (including £60,000 (2005: £31,000) in respect of the Parent Company)	**99**	89
Auditors' remuneration for other services	**137**	111
Analysis of total fees paid to the auditors:		
Audit services	**99**	89
Further assurance services	**28**	8
Tax compliance services	**53**	36
Tax advisory services	**56**	48
Other services	**—**	19
	236	200

6. Employees

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

	2006 Number	2005 Number
Manufacturing	**132**	146
Distribution	**364**	344
Administration	**195**	189
	691	679

The costs incurred in respect of these employees were:

	2006 £'000	2005 £'000
Wages and salaries	**12,895**	11,081
Social security costs	**1,171**	997
Other pension costs	**338**	281
Share-based payments charge (see note 22)	**515**	398
	14,919	12,757

Related party transactions — the remuneration of key management was as follows:

	2006 £'000	2005 £'000
Wages and salaries (including benefits in kind)	**1,176**	914
Social security costs	**151**	117
Other pension costs	**85**	75
Share-based payments charge	**384**	283
	1,796	1,389

Key management comprises Executive Directors, the Product Development and Regulatory Affairs Director and the Divisional Managing Directors.

Details of the remuneration, shareholdings, share options and pension contributions of the Executive Directors are included in the Remuneration Report on pages 34 to 39.

The Group operates a stakeholder personal pension scheme for certain employees. The Group contributed between 4% and 12% of pensionable salaries which amounted to £338,000 (2005: £281,000).

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

7. Income Tax Expense

		2006 £'000	2005 £'000
Current tax	— charge for current year	**3,491**	3,001
	— adjustment in respect of prior years	**(58)**	(233)
Total current tax expense		**3,433**	2,768
Deferred tax	— origination and reversal of temporary differences	**4**	(37)
	— adjustment in respect of prior years	**50**	(57)
Total deferred tax expense		**54**	(94)
Total income tax expense in the income statement		**3,487**	2,674

All taxation is in the United Kingdom.

The tax on the Group's profit before tax differs from the standard rate of UK corporation tax of 30% (2005: 30%). The differences are explained below:

	2006 £'000	2005 £'000
Profit before taxation	**11,044**	9,701
Tax at 30%	**3,313**	2,910
Effect of:		
— depreciation on assets not eligible for tax allowances	**27**	22
— disallowable expenses	**33**	2
— overseas trading losses	**78**	30
— under-recovery of deferred tax on share-based payments	**44**	—
— adjustments in respect of prior years	**(8)**	(290)
Total income tax expense	**3,487**	2,674

Additional current tax credits of £367,000 (2005: £nil) and deferred tax credits of £62,000 (2005: £388,000) have been recognised directly in equity.

8. Dividends

	2006 £'000	2005 £'000
Final dividend paid in respect of prior year but not recognised as a liability in that year 3.50p per share (2005: 3.15p)	**1,794**	1,606
Interim dividend paid 1.91p per share (2005: 1.70p)	**983**	867
Total dividend 5.41p per share (2005: 4.85p) recognised as distributions to equity holders in the period	**2,777**	2,473
Proposed final dividend for the year ended 30 June 2006 4.33p per share (2005: 3.50p)	**2,248**	1,789
Total dividend paid and proposed for the year ended 30 June 2006 6.24p per share (2005: 5.20p)	**3,231**	2,656

In accordance with IAS10 'Events After the Balance Sheet Date', the proposed final dividend for the year ended 30 June 2006 has not been accrued for in these financial statements. It will be shown as a deduction from equity in the financial statements for the year ending 30 June 2007.

The proposed final dividend for the year ended 30 June 2005 is shown as a deduction from equity in the year ended 30 June 2006.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

11. Property, Plant and Equipment

	Freehold land £'000	Short leasehold buildings £'000	Motor vehicles £'000	Plant and fixtures £'000	Total £'000
Cost					
At 1 July 2004	13	2,627	596	5,960	9,196
Additions	—	60	—	662	722
Disposals	—	(243)	(58)	(315)	(616)
At 30 June 2005 and 1 July 2005	13	2,444	538	6,307	9,302
Additions	—	157	—	1,378	1,535
Disposals	—	—	(105)	(185)	(290)
At 30 June 2006	**13**	**2,601**	**433**	**7,500**	**10,547**
Depreciation					
At 1 July 2004	—	511	541	2,920	3,972
Charge for the year	—	147	54	701	902
Disposals	—	(243)	(58)	(217)	(518)
At 30 June 2005 and 1 July 2005	—	415	537	3,404	4,356
Charge for the year	—	135	1	750	886
Disposals	—	—	(105)	(185)	(290)
At 30 June 2006	**—**	**550**	**433**	**3,969**	**4,952**
Net book value					
At 30 June 2006	**13**	**2,051**	**—**	**3,531**	**5,595**
At 30 June 2005 and 1 July 2005	13	2,029	1	2,903	4,946
At 1 July 2004	13	2,116	55	3,040	5,224
Net book value of assets held under finance leases					
At 30 June 2006	**—**	**77**	**—**	**1,028**	**1,105**
At 30 June 2005 and 1 July 2005	—	—	—	224	224
At 1 July 2004	—	—	32	149	181

	2006 £'000	2005 £'000
Assets in the course of construction included above	**1,444**	269
Contracted capital commitments	**823**	379

12. Impairment Reviews

Goodwill, indefinite life assets and intangible assets not yet available for use are tested for impairment annually, or more frequently if there are indications that amounts might be impaired. The impairment test involves determining the recoverable amounts of the relevant cash-generating unit, which corresponds to the higher of the fair value less costs to sell or its value in use. Value in use calculations have been performed using the methods and assumptions detailed below:

(a) Goodwill

The carrying amount of goodwill shown in note 10 comprises £2,154,000 (2005: £2,154,000) relating to the acquisition of North Western Laboratories Limited and £2,231,000 (2005: £2,231,000) relating to the acquisition of Anglian Pharma plc. For the purpose of annual impairment reviews the goodwill relating to North Western Laboratories has been allocated to the Laboratories cash-generating unit whilst the goodwill relating to Anglian Pharma plc has been allocated to the Dales Pharmaceuticals cash-generating unit. The recoverable amount of both units is based on value in use calculations. The value in use of each of these cash-generating units has been determined by discounting projected future cash flows by a pre-tax discount rate of 11.6%, being the Directors' estimate of the weighted average cost of capital of the Company.

Projected future cash flows have been derived from the annual budget for the year ending 30 June 2007 extrapolated over a 10 year period applying a growth rate of 5% per annum up to year five. No growth in revenues are assumed beyond year five.

In both cases, the value in use is significantly higher than the carrying amount and no impairment provision is therefore required.

(b) Indefinite Life Assets

As disclosed in note 10, the Directors consider that the Vetivex® marketing authorisations with a carrying amount of £822,000 have an indefinite life. Their value in use has been determined by discounting projected future cash flows by a pre-tax discount rate of 11.6%, being the Directors' estimate of the weighted average cost of capital of the Company. Projected future cash flows have been derived from the annual budget for the year ending 30 June 2007 extrapolated over a 10 year period applying a growth rate of 5% per annum up to year five. No growth in revenues are assumed beyond year five.

The value in use is significantly higher than the carrying amount and no impairment provision is therefore required.

(c) Intangible Assets not yet available for use

The Group is developing an intangible asset in respect of authorisation to market our product Vetoryl® in the USA. This intangible asset will only be available for use once marketing authorisation is received from the FDA.

The carrying amount in respect of this intangible asset is as follows:

	2006 £'000	2005 £'000
Payment to acquire patent rights to Trilostane (the active ingredient of Vetoryl®)	**789**	789
Subsequent development costs	**323**	128
	1,112	917

Value in use has been determined by discounting the projected cash flows by a pre-tax discount rate of 16.6%. The higher discount rate reflects the uncertainty of the timing of future cash flows. Projected cash flows have been determined from a detailed marketing plan covering a five year period from product launch extrapolated up to 30 June 2016. No growth in revenues is assumed after the fifth year following launch. The marketing plan uses data on the market size and market penetration taking into account our experience in launching Vetoryl® in other territories.

Based upon the above calculation, the value in use is significantly higher than the carrying amount and no impairment provision is required.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

13. Deferred Taxes

(a) Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
	2006 £'000	2005 £'000	**2006 £'000**	2005 £'000	**2006 £'000**	2005 £'000
Intangible assets	**—**	—	**(193)**	(153)	**(193)**	(153)
Property, plant and equipment	**—**	—	**(311)**	(272)	**(311)**	(272)
Inventories	**—**	—	**—**	—	**—**	—
Receivables	**98**	45	**—**	—	**98**	45
Cash and cash equivalents	**—**	—	**—**	—	**—**	—
Borrowings	**—**	—	**—**	—	**—**	—
Payables	**38**	103	**—**	—	**38**	103
Current tax liabilities	**—**	—	**—**	—	**—**	—
Share-based payments	**813**	683	**—**	—	**813**	683
	949	831	**(504)**	(425)	**445**	406

On the basis that all deferred income taxes relate to the UK and that there is a legally enforceable right to offset current tax liabilities against current tax assets, deferred income tax assets and liabilities have been offset.

(b) Unrecognised deferred tax assets

	2006 £'000	2005 £'000
Tax losses	**108**	30

No deferred tax asset has been recognised in respect of the losses incurred by the Company's USA subsidiary due to the uncertainty of achieving taxable profits in the USA against which the losses can be offset.

(c) Movement in temporary differences during the year

	Balance at 1 July 2004 £'000	Recognised in income £'000	Recognised in equity £'000	Balance at 30 June 2005 £'000
Intangible assets	(69)	(84)	—	(153)
Property, plant and equipment	(296)	24	—	(272)
Inventories	—	—	—	—
Receivables	24	21	—	45
Cash and cash equivalents	—	—	—	—
Borrowings	—	—	—	—
Payables	61	42	—	103
Current tax liabilities	—	—	—	—
Share-based payments	204	91	388	683
	(76)	94	388	406

	Balance at 1 July 2005 £'000	Adoption of IAS39 £'000	Recognised in income £'000	Recognised in equity £'000	**Balance at 30 June 2006 £'000**
Intangible assets	(153)	—	(40)	—	**(193)**
Property, plant and equipment	(272)	—	(39)	—	**(311)**
Inventories	—	—	—	—	**—**
Receivables	45	17	36	—	**98**
Cash and cash equivalents	—	—	—	—	**—**
Borrowings	—	—	—	—	**—**
Payables	103	14	(79)	—	**38**
Current tax liabilities	—	—	—	—	**—**
Share-based payments	683	—	68	62	**813**
	406	31	(54)	62	**445**

14. Inventories

	2006 £'000	2005 £'000
Raw materials and consumables	1,443	1,021
Work in progress	117	694
Finished goods and goods for resale	20,397	18,675
	21,957	20,390

15. Trade and Other Receivables

	2006 £'000	2005 £'000
Trade receivables	33,476	31,778
Other receivables	1,073	1,112
Prepayments and accrued income	798	818
	35,347	33,708

Trade receivables are stated after an impairment provision of £2,035,000 (2005: £1,761,000).

16. Cash and Cash Equivalents

	2006 £'000	2005 £'000
Cash at bank and in hand	4,552	3,857
Short-term deposits	15,186	10,067
	19,738	13,924

The short-term deposits are repayable on demand.

17. *Trade and Other Payables*

	2006 £'000	2005 £'000
Trade payables	41,988	38,175
Other payables	491	313
Other taxation and social security	1,373	1,650
Accruals and deferred income	1,678	1,833
	45,530	41,971

18. Current Tax Liabilities

	2006 £'000	2005 £'000
Corporation tax payable	2,505	2,057

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

19. Borrowings

	2006 **£'000**	2005 £'000
Current liabilities		
Bank loans and overdrafts	**3,019**	1,400
Finance lease obligations	**398**	102
	3,417	1,502
Non-current liabilities		
Bank loans	**14,200**	17,200
Finance lease obligations	**1,147**	271
Arrangement fees netted off	**(105)**	(190)
	15,242	17,281
Total borrowings	**18,659**	18,783

At the year end, the Group had the following unutilised borrowing facilities:

	2006 **£'000**	2005 £'000
Revolving credit facility	**5,000**	5,000
Bank overdraft facility	**4,000**	4,000
	9,000	9,000

The term loan from Bank of Scotland is secured by a fixed and floating charge on the assets of the Group. Interest is charged at 1.25% over LIBOR. The loan is repayable in instalments up to 30 June 2010.

The overdraft facility is renewable annually whilst the revolving credit facility is committed until 30 June 2010.

The maturity of the bank loans and overdrafts is as follows:

	2006 **£'000**	2005 £'000
Payable:		
Within one year	**3,019**	1,400
Between one and two years	**4,000**	3,000
Between two and five years	**10,200**	14,200
	17,219	18,600

The minimum lease payments and the present value of minimum lease payments payable under finance lease obligations are:

	Minimum Lease Payments		Present Value of Minimum Lease Payments	
	2006 **£'000**	2005 £'000	**2006** **£'000**	2005 £'000
Within one year	**503**	130	**398**	102
Between one and two years	**444**	151	**375**	125
Between two and five years	**835**	161	**772**	146
Total minimum lease payments	**1,782**	442	**1,545**	373
Future finance charges	**(237)**	(69)	**—**	—
Present value of lease obligations	**1,545**	373	**1,545**	373

Further information on the interest profile of borrowings is shown in note 20.

20. Financial Instruments

The Group adopted IAS32, 'Financial Instruments: Disclosure and Presentation' and IAS39, 'Financial Instruments: Recognition and Measurement' with effect from 1 July 2005. As allowed by the transitional provisions, comparative information for the year ended 30 June 2005 is presented under UK GAAP.

The Group's financial instruments comprise cash deposits, bank loans and overdrafts, finance lease obligations, derivatives used for hedging purposes and trade receivables and payables.

Treasury Policy

Treasury policy is set by the Board and monitored by the Group Finance Director. The Group does not speculate on short-term interest or exchange rate movements. Derivatives are used only to hedge underlying commercial positions and are not used for speculative or trading purposes.

Financial Risk Management

(i) Interest rate risk

All cash deposits and bank loans and overdrafts bear interest at floating rates linked to base rate or LIBOR and are consequently exposed to cash flow and interest rate risk.

The Group seeks to hedge interest rate risk on between 20% and 80% of outstanding bank loans. By way of a separate derivative financial instrument, £5,733,000 of outstanding loans are subject to a floor and ceiling arrangement whereby the Group's exposure to fluctuations in LIBOR are limited to a minimum rate of 4.53% and a maximum rate of 5.50%. All finance leases and hire purchase contracts are at fixed rates determined at the inception of the contract.

Sensitivity — a 1% increase in interest rates would reduce Group profit before taxation by £158,000.

(ii) Foreign exchange risk

Foreign exchange exposure is hedged naturally as far as possible by matching receipts and payments in the relevant foreign currency. The Group maintains Euro and US Dollar bank accounts for this purpose. Unmatched foreign currency exposure is hedged at the discretion of the Group Finance Director within the parameters set by the Board. Hedging instruments allowed to be used are forward contracts and options to purchase the relevant foreign currency.

No borrowings are denominated in foreign currencies.

(iii) Credit risk

Cash is only deposited with highly rated UK-based banks.

The Group offers trade credit to customers in the normal course of business. Trade and bank references are obtained prior to extending credit.

Insurance is held in respect of overseas receivables.

(iv) Concentration of credit risk

The Group sells to a large number of customers and, with the exception of corporate veterinary practices and veterinary wholesalers, credit risk is not highly concentrated. The largest customer accounted for approximately 3.0% of gross trade receivables at 30 June 2006.

(v) Liquidity risk

Liquidity risk is the risk that the Group will not have sufficient funds to meet liabilities. Cash forecasts identifying the liquidity requirements of the Group are produced quarterly. These are reviewed to ensure sufficient financial headroom exists for at least a 12 month period.

The Group's undrawn borrowing facilities at 30 June 2006 are detailed in note 19.

Maturity of Financial Instruments

The maturity of financial instruments excluding short-term receivables and payables are shown in notes 16 and 19.

Interest Rate Profile

The following table shows the effective interest rate at the balance sheet date of interest-bearing financial assets and liabilities and the period in which they reprice or mature.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

20. Financial Instruments continued

2006

	Carrying Value £'000	Effective Interest Rate %	Period to re-pricing or maturity within 3 months £'000	1–2 years £'000	2–3 years £'000	3–4 years £'000	4–5 years £'000
Financial assets							
— bank deposits (a)	15,186	4.0	15,186	—	—	—	—
Financial liabilities							
— bank loans (b)	(17,114)	6.0	(17,114)	—	—	—	—
— finance leases (c)	(1,545)	7.3	—	(62)	(3)	(787)	(693)
	(18,659)						

(a) Floating rate at 0.5% below base rate.

(b) Floating rate at 1.25% above LIBOR.

(c) Various fixed interest rates with a weighted average rate of 7.3%.

Foreign Currency Profile

At 30 June 2006, the Group had no material financial assets or liabilities denominated in foreign currencies.

Derivatives

The Group held the following derivatives at 30 June 2006:

	Carrying Value £'000	Gross amount hedged £'000
Interest rate floor and ceiling	2	5,733

Although used for the purpose of hedging interest rate risk, this derivative has been designated as held for trading financial instrument for the purposes of IAS39, with changes in fair value being taken through the income statement. The instrument matures on 31 December 2007. All loans held by the Group are measured at amortised cost.

Fair Values of Financial Instruments

The following table summarises the carrying values and fair values of financial assets and liabilities.

	2006 Carrying Value £'000	2006 Fair Value £'000	2005 Carrying Value £'000	2005 Fair Value £'000
Financial assets				
Cash and cash equivalents (a)	19,738	19,738	13,924	13,924
Trade receivables (a)	33,476	33,476	31,778	31,778
Derivatives (c)	2	2	77	19
	53,216	53,216	45,779	45,721
Financial liabilities				
Bank loans (a)	(17,114)	(17,114)	(18,410)	(18,410)
Finance leases (b)	(1,545)	(1,583)	(373)	(400)
Trade payables (a)	(41,988)	(41,988)	(38,175)	(38,175)
Derivatives (c)	—	—	—	(44)
	(60,647)	(60,685)	(56,958)	(57,029)

(a) Due to the nature and/or short-term maturity of these financial instruments, carrying values approximate to fair values.

(b) The fair values of these financial instruments are based upon discounted cash flows, using discount rates based upon the Group's cost of borrowing at the balance sheet date.

(c) The fair values of these financial instruments are based upon the amount that the Group would receive or pay to terminate the instrument at the balance sheet date, being the market price of the instrument.

20. Financial Instruments continued

2005 Financial Instruments Disclosure

An explanation of the Group's treasury policies and controls is set out on pages 22 and 23. 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, the floor and ceiling arrangement (see (b) below) and the currency option (see below), 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.

At 30 June 2005 the Group had a foreign currency swap option for $3.00 million to exchange sterling for US dollars at any time before 31 December 2005. Its book value at 30 June 2005 was £77,000 whilst the fair value was £19,000.

(b) Interest rate risk profile of financial liabilities as at 30 June 2005

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 £373,000 with a weighted average fixed interest rate of 8.9% over a weighted average term of 45 months.

During the year, the Group entered into an interest rate floor and ceiling arrangement which effectively fixes the LIBOR rate to within the range 4.53%–5.50% over one-third of the Group's bank borrowings (£6.2 million at 30 June 2005).

This arrangement expires on 31 December 2007. At 30 June 2005, the book value was £nil whilst the fair value was (£44,000).

(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 note 19.

(e) Maturity of facilities

At 30 June 2005 the Group had an undrawn committed revolving credit facility of £5 million maturing in between two to five years and an overdraft facility of £4 million which is renewable annually.

21. Share Capital

	Ordinary shares of 1p each			
	2006		2005	
	£'000	**No.**	£'000	No.
Authorised	**750**	**75,000,000**	750	75,000,000
Issued at start of year	**511**	**51,120,964**	510	50,977,857
New shares issued	**8**	**794,038**	1	143,107
At end of year	**519**	**51,915,002**	511	51,120,964

During the year, 794,038 new ordinary shares of 1p (2005: 143,107 new ordinary shares of 1p) were issued following the exercise of options under the Unapproved and SAYE Share Options Schemes. The consideration received was £748,000 (2005: £170,000). The holders of ordinary shares are entitled to receive dividends as declared or approved at General Meetings from time to time and are entitled to one vote per share at meetings of the Company.

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

22. Share-based Payments

During the year, the Company operated the Unapproved Share Option Scheme, the Approved Share Option Scheme, the Executive Incentive Plan and the Save As You Earn ("SAYE") Share Option Scheme as described below:

Unapproved and Approved Share Option Schemes

Under these Schemes, options are granted to certain executives and employees of the Group (excluding Executive Directors) to purchase shares in the Company at a price fixed at the average market value over the three days prior to the date of grant. For the options to vest, there must be an increase in earnings per share of at least 12% above the growth in the UK Retail Price Index (RPI) over a three year period. Once vested, options must be exercised within 10 years of the date of grant.

Executive Incentive Plan

Under this plan Executive Directors and selected Senior Executives are awarded shares in the Company subject to a Total Shareholder Return ("TSR") target.

The TSR target measures the Company's TSR performance against the FTSE Small Cap Index over a three year measurement period (commencing at the beginning of the financial year in which the awards are made). 100% of the shares vest if the Company achieves an upper quartile performance, 30% of the shares vest at median performance and awards vest on a straight-line basis for performance in between. No shares vest if performance is below median.

In addition, awards will only vest if, in the opinion of the Remuneration Committee, the performance of the Company has been satisfactory.

SAYE Option Scheme

This Scheme is open to all UK employees. Participants save a fixed amount of up to £250 per month for either three or five years and are then able to use these savings to buy shares in the Company at a price fixed at a 20% discount to the market value at the start of the saving period. The SAYE options must ordinarily be exercised within six months of the completion of the relevant savings period. The exercise of these options is not subject to any performance criteria.

Outstanding awards and the movement during the year are shown below:

Year ended 30 June 2006

	Exercise period	Exercise price per share Pence	At 1 July 2005 Number	Exercised Number	Granted Number	Lapsed Number	At 30 June 2006 Number
Unapproved Share Option Scheme							
14 September 2000	2003–2010	120	343,000	(210,000)	—	(2,000)	**131,000**
22 April 2002	2005–2012	153.5	317,000	(229,500)	—	—	**87,500**
11 April 2003	2006–2013	58.5	99,500	(17,000)	—	—	**82,500**
			759,500	(456,500)	—	(2,000)	**301,000**
Approved Share Option Scheme							
2 April 2004	2007–2014	134.5	137,000	—	—	(14,000)	**123,000**
3 December 2004	2007–2014	180	30,000	—	—	—	**30,000**
5 April 2005	2008–2015	202.5	179,000	—	—	(8,000)	**171,000**
15 March 2006	2009–2016	252	—	—	177,000	(2,000)	**175,000**
			346,000	—	177,000	(24,000)	**499,000**
Executive Incentive Plan							
5 December 2003	2006–2007	—	505,000	—	—	—	**505,000**
9 October 2004	2007–2008	—	210,739	—	—	(28,213)	**182,526**
3 October 2005	2008–2009	—	—	—	205,141	—	**205,141**
			715,739	—	205,141	(28,213)	**892,667**
SAYE Option Scheme							
26 April 2001	2004–2006	158	29,896	—	—	(1,708)	**28,188**
9 April 2002	2005–2007	129	29,078	(1,766)	—	(14,742)	**12,570**
3 April 2003	2006–2008	39	873,523	(335,772)	—	(41,358)	**496,393**
15 October 2004	2007–2009	124	142,619	—	—	(13,492)	**129,127**
18 October 2005	2008–2010	204	—	—	111,078	(12,748)	**98,330**
			1,075,116	(337,538)	111,078	(84,048)	**764,608**
Total			**2,896,355**	**(794,038)**	**493,219**	**(138,261)**	**2,457,275**
Weighted average exercise price			74.6p	94.2p	136.3p	89.0p	**79.9p**

22. Share-based Payments continued

Year ended 30 June 2005

	Exercise period	Exercise price per share Pence	At 1 July 2004 Number	Exercised Number	Granted Number	Lapsed Number	At 30 June 2005 Number
Unapproved Share Option Scheme							
14 September 2000	2003–2010	120	433,000	(78,000)	—	(12,000)	343,000
22 April 2002	2005–2012	153.5	352,500	(17,500)	—	(18,000)	317,000
11 April 2003	2006–2013	58.5	105,000	—	—	(5,500)	99,500
			890,500	(95,500)	—	(35,500)	759,500
Approved Share Option Scheme							
2 April 2004	2007–2014	134.5	143,000	—	—	(6,000)	137,000
3 December 2004	2007–2014	180	—	—	30,000	—	30,000
5 April 2005	2008–2015	202.5	—	—	181,000	(2,000)	179,000
			143,000	—	211,000	(8,000)	346,000
Executive Incentive Plan							
5 December 2003	2006–2007	—	505,000	—	—	—	505,000
9 October 2004	2007–2008	—	—	—	210,739	—	210,739
			505,000	—	210,739	—	715,739
SAYE Option Scheme							
26 April 2001	2004–2006	158	73,297	(13,978)	—	(29,423)	29,896
9 April 2002	2005–2007	129	59,387	(16,662)	—	(13,647)	29,078
3 April 2003	2006–2008	39	985,279	(16,967)	—	(94,789)	873,523
15 October 2004	2007–2009	124	—	—	144,147	(1,528)	142,619
			1,117,963	(47,607)	144,147	(139,387)	1,075,116
Total			**2,656,463**	**(143,107)**	**565,886**	**(182,887)**	**2,896,355**
Weighted average exercise price			71.3p	119.2p	105.9p	89.8p	74.6p

For options exercised during the year, the weighted average market price at the date of exercise was 241p (2005: 194p). The weighted average remaining contractual lives of options outstanding at the balance sheet date was 3.5 years (2005: 4 years).

As allowed by the transitional provisions of IFRS1 and IFRS2, included above are options over shares that have not been recognised in accordance with IFRS2 as the options were granted before 7 November 2002.

The fair values for shares granted under the Unapproved, Approved and SAYE Option Schemes have been calculated using the Black-Scholes Option Pricing Model. The fair value of shares awarded under the Executive Incentive Plan have been calculated using a Monte Carlo Simulation Model which takes into account the market-based performance conditions attaching to those shares:

The assumptions used in calculating fair value are as follows:

Executive Incentive Plan			
Date of grant	3/10/05	9/10/04	5/12/03
Number of shares awarded	205,141	210,739	505,000
Share price at date of grant	251p	164p	123p
Exercise price	Nil	Nil	Nil
Expected life	3 years	3 years	3 years
Risk-free rate	4.21%	4.69%	4.57%
Volatility	36%	36%	36%
Dividend yield	2.07%	2.95%	3.27%
Fair value per share	169p	105p	78p

Unapproved and Approved Share Option Schemes					
Date of grant	15/3/06	5/4/05	3/12/04	2/4/04	11/4/03
Number of shares awarded	177,000	181,000	30,000	147,000	124,000
Share price at date of grant	252p	212p	179.32p	136p	59p
Exercise price	252p	202.5p	180p	134.5p	58.5p
Expected life	5 years	5 years	5 years	5 years	5 years
Risk-free rate	4.32%	4.61%	4.53%	4.76%	4.12%
Volatility	36%	36%	36%	36%	36%
Dividend yield	2.15%	2.40%	2.61%	3.19%	7.04%
Fair value per share	79p	69p	54p	40p	11p

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

22. Share-based Payments continued

Save as You Earn Option Scheme

Date of grant	18/10/05	15/10/04	3/4/03
Number of shares awarded	111,078	144,147	1,034,938
Share price at date of grant	255p	160p	54p
Exercise price	204p	124p	39p
Expected life			
— three year scheme	3.25 years	3.25 years	3.25 years
— five year scheme	5.25 years	5.25 years	5.25 years
Risk-free rate			
— three year scheme	4.25%	4.56%	3.78%
— five year scheme	4.31%	4.64%	4.14%
Volatility	36%	36%	36%
Dividend yield	2.04%	2.92%	7.63%
Fair value per share			
— three year scheme	88p	55p	14p
— five year scheme	101p	61p	14p

National Insurance contributions are payable by the Company in respect of some of the share-based payments. These contributions are payable on the date of exercise based on the intrinsic value of the share-based payments and are therefore treated as cash-settled awards. The Group had an accrual at 30 June 2006 of £241,000 (2005: £181,000), of which £49,000 (2005: £56,000) related to vested options.

The total charge to the Income Statement in respect of share-based payments was:

	2006 £'000	2005 £'000
Equity-settled share-based transactions	**427**	273
Cash-settled share-based transactions	**88**	125
	515	398

The above charge to the Income Statement was included within administrative expenses.

23. Analysis of Net Cash/(Borrowings)

	As at 30.06.06 £'000	As at 30.06.05 £'000
Bank loans and overdraft	**(17,114)**	(18,410)
Finance leases and hire purchase contracts	**(1,545)**	(373)
Cash and cash equivalents	**19,738**	13,924
Net cash/(borrowings)	**1,079**	(4,859)

24. Operating Leases

At the balance sheet date the Group had outstanding commitments for future minimum rentals payable under non-cancellable operating leases as follows:

	2006 £'000	2005 £'000
Within one year	**1,912**	1,716
Between one and five years	**4,626**	4,058
In five years or more	**4,535**	4,919
	11,073	10,693

25. Contingent Asset/Liability

Dechra Limited, a subsidiary of Dechra Pharmaceuticals PLC, is in dispute with Vet Tec Systems Limited ("Vet Tec") where each party is alleging breach of contract on the part of the other.

Vet Tec provide the veterinary practice management software marketed by the Group under the brand "Vetcom Open". Neither party has, as yet, commenced legal proceedings and the amount and timing of any asset or liability from this dispute is currently uncertain.

No amounts have been included in the financial statements in respect of this dispute.

26. Critical Accounting Judgements and Key Sources of Estimation Uncertainty

Critical Judgements in applying the Group's Accounting Policies

In the process of applying the Group's accounting policies as described in note 1, the Directors have made the following judgements that have the most significant effect on the amounts recognised in the Financial Statements.

Intangible Asset — Vetoryl® USA

As described in note 12, the Group is carrying a total amount of £1,112,000 in respect of Vetoryl® USA. Recoverability of this amount is dependent upon obtaining FDA approval to market Vetoryl® in the USA. Based upon positive discussions with the FDA (evidenced by the product being granted expedited review status) and the obtaining of marketing approval in the European Union, the Directors concluded that the obtaining of marketing authorisation in the USA is highly likely and that the criteria for recognising an intangible asset have been met.

Key Sources of Estimation Uncertainty

The key sources of estimation uncertainty which may cause a material adjustment to the carrying amount of assets and liabilities are discussed below:

Impairment of Goodwill and Indefinite Life Intangible Assets

The Group determines whether goodwill and indefinite life assets are impaired at least on an annual basis. This requires an estimation of the value-in-use of the cash-generating units to which they are allocated. Estimating the value-in-use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. Further detail on the assumptions used in determining value-in-use calculations is provided in note 12.

Impairment of Receivables

The Group has estimated impairment of receivables by assessing recoverability of amounts due on a customer by customer basis. As described in note 20, credit risk is not highly concentrated with the exception of Corporate Veterinary Practices and Veterinary Wholesalers. If the receivables due from one of these large customers proved to be irrecoverable then an additional impairment provision may be required.

27. Explanation of Transition to IFRS

As stated in Note 1, these are the Group's first consolidated financial statements prepared in accordance with adopted IFRSs. Consistent accounting policies set out in note 1 have been applied in preparing comparative information for the year ended 30 June 2005 and the preparation of the opening IFRS balance sheet at 1 July 2004 (the Group's date of transition).

In preparing its opening balance sheet and comparative information for the year ended 30 June 2005 the Group has adjusted amounts reported previously in financial statements prepared in accordance with UK GAAP.

The adjustments from the conversion to IFRS had no impact upon the cash flows of the Group although there are a number of presentational differences under IFRS.

An explanation of the principal changes in accounting policies and how the transition from UK GAAP to IFRS has affected the Group's income statement, balance sheet and net equity is summarised below.

(a) IFRS Reconciliation of Income Statement Comparatives

		Year ended 30 June 2005		
	Notes	Published UK GAAP £'000	IFRS adjustments £'000	**Restated under IFRS £'000**
Revenue	a	208,197	2,070	**210,267**
Cost of sales	a	(178,480)	(2,070)	**(180,550)**
Gross profit		29,717	—	**29,717**
Operating expenses	b, c, d, e	(19,305)	843	**(18,462)**
Operating profit		10,412	843	**11,255**
Finance income		355	—	**355**
Finance expense		(1,909)	—	**(1,909)**
Profit before taxation		8,858	843	**9,701**
Income tax expense	f	(2,590)	(84)	**(2,674)**
Profit attributable to equity holders of the parent		6,268	759	**7,027**
Earnings per share (pence)				
Basic		12.28p	1.49p	**13.77p**
Diluted		12.08p	1.46p	**13.54p**

Notes to the Consolidated Financial Statements

For the year ended 30 June 2006

27. Explanation of Transition to IFRS continued

(b) IFRS Reconciliation of Balance Sheet Comparatives

	Notes	1 July 2004 Published UK GAAP £'000	1 July 2004 IFRS adjustments £'000	1 July 2004 IFRS £'000	30 June 2005 Published UK GAAP £'000	30 June 2005 IFRS adjustments £'000	30 June 2005 Restated under IFRS £'000
Non-current assets							
Intangible assets							
— goodwill	a	4,385	—	**4,385**	3,821	564	**4,385**
— software	b	—	—	**—**	—	255	**255**
— other intangibles	c	789	230	**1,019**	1,889	510	**2,399**
Property plant and equipment	b	5,224	—	**5,224**	5,201	(255)	**4,946**
Deferred taxes	d	—	—	**—**	—	406	**406**
Total non-current assets		10,398	230	**10,628**	10,911	1,480	**12,391**
Current assets							
Inventories		16,979	—	**16,979**	20,390	—	**20,390**
Trade and other receivables		32,889	—	**32,889**	33,708	—	**33,708**
Deferred taxes	d	—	—	**—**	4	(4)	**—**
Cash and cash equivalents		—	—	**—**	13,924	—	**13,924**
Total current assets		49,868	—	**49,868**	68,026	(4)	**68,022**
Total assets		60,266	230	**60,496**	78,937	1,476	**80,413**
Current liabilities							
Borrowings		(5,347)	—	**(5,347)**	(1,502)	—	**(1,502)**
Trade and other payables	e	(36,944)	(89)	**(37,033)**	(41,826)	(145)	**(41,971)**
Current tax liabilities		(1,275)	—	**(1,275)**	(2,057)	—	**(2,057)**
Proposed dividend	f	(1,606)	1,606	**—**	(1,789)	1,789	**—**
Total current liabilities		(45,172)	1,517	**(43,655)**	(47,174)	1,644	**(45,530)**
Non-current liabilities							
Borrowings		(4,763)	—	**(4,763)**	(17,281)	—	**(17,281)**
Provisions		—	—	**—**	—	—	**—**
Deferred taxes	d	(174)	98	**(76)**	—	—	**—**
Total non-current liabilities		(4,937)	98	**(4,839)**	(17,281)	—	**(17,281)**
Total liabilities		(50,109)	1,615	**(48,494)**	(64,455)	1,644	**(62,811)**
Net assets		10,157	1,845	**12,002**	14,482	3,120	**17,602**
Equity							
Called up share capital		510	—	**510**	511	—	**511**
Share premium account		26,784	—	**26,784**	26,953	—	**26,953**
Merger reserve		1,720	—	**1,720**	1,720	—	**1,720**
Retained earnings	g	(18,857)	1,845	**(17,012)**	(14,702)	3,120	**(11,582)**
Total equity attributable to equity holders of the parent		10,157	1,845	**12,002**	14,482	3,120	**17,602**

(c) Reconciliation of Equity

	1 July 2004 £'000	30 June 2005 £'000
Equity under UK GAAP	10,157	14,482
Write-back of proposed dividend	1,606	1,789
Deferred tax	98	402
Lease incentive	(89)	(145)
Capitalisation of development costs	230	510
Write-back of goodwill amortisation	—	564
Equity under IFRS	12,002	17,602

Explanatory notes to the UK GAAP to IFRS Reconciliations

Income Statement

a. Under IAS18 'Revenue' certain items, such as the sale of trading data to suppliers, have been reclassified to revenue from cost of sales. There is no impact on profit, earnings per share or net assets.

b. Under UK GAAP, goodwill was amortised over its estimated useful life. Under IFRS3 'Business Combinations', goodwill is not amortised but is subject to annual impairment review. This has resulted in a credit to the income statement of £564,000 for the year ended 30 June 2005.

c. Under UK GAAP the accounting policy of the Group was, in general, to write off all development expenditure to the income statement as incurred. Under IAS38 'Intangible Assets' development expenditure meeting the required criteria must be capitalised. This has resulted in a credit to the income statement of £280,000 for the year ended 30 June 2005.

d. Under IFRS2 'Share-based Payments', the cost of employee share options recognised in the income statement is based upon the excess of the fair value of the option over the exercise price at the date of grant. Under UK GAAP, the cost recognised was generally the intrinsic value being the difference in exercise price and market price at the date of grant of the option.

The change in method of calculation has resulted in a net credit of £55,000 in respect of the year ended 30 June 2005.

e. Under UK GAAP, the benefit of lease incentives received (in the form of rent-free periods) was spread over the period until the rent reverts to market rates. Under IAS17 'Leases', the benefit must be spread over the entire lease period. This change has resulted in an additional charge to the income statement of £56,000 for the year ended 30 June 2005.

f. The income tax expense has been adjusted to reflect the tax effect of the above adjustments.

Balance Sheet

a. The increase in goodwill reflects the write-back of amortisation previously charged under UK GAAP.

b. Under IAS38 'Intangible Assets', software costs that are not an integral part of the related hardware are classed as intangible assets. They have therefore been reclassified from property, plant and equipment. There is no impact on the income statement or net assets.

c. The increase in other intangible assets represents capitalised development costs under IAS38 'Intangible Assets'.

d. The calculation of deferred tax under IAS12 'Income Taxes' can be different from UK GAAP, under which deferred tax is calculated based upon income statement timing differences. The principal reason for the increase in the deferred tax asset is that deferred tax in respect of share-based payments is calculated by reference to a figure which differs from the charge for such payments in the income statement. Deferred tax in respect of share-based payments charged directly to the income statement is also taken to the income statement but any excess tax relief over this amount is taken directly to equity.

e. The increase in trade and other payables represents the balance of lease incentives received that are being spread over the remaining lease periods.

f. Under IAS10 'Events After the Balance Sheet Date' dividends are recognised when they are paid or approved by the shareholders. This generally results in a later recognition in the financial statements than under UK GAAP.

g. The increase in retained earnings at 30 June 2005 is made up as follows:
   - net adjustments to the income statement of £759,000
   - reduction to credit to equity in respect of share-based payments of (£55,000)
   - capitalised development costs at 1 July 2004 of £230,000
   - increase in lease incentives carried forward at 1 July 2004 of (£89,000)
   - de-recognition of the final dividend of £1,789,000
   - credit to deferred tax recognised directly in equity of £486,000

Financial History

	2006* £'000	2005* £'000	2004† £'000	2003† £'000	2002† £'000
Income statement					
Revenue	**232,471**	210,267	186,843	179,309	170,202
Operating profit before exceptional items and goodwill amortisation	**12,312**	11,255	9,184	8,162	8,773
Profit before taxation	**11,044**	9,701	7,369	5,685	7,308
Profit after taxation	**7,557**	7,027	5,081	3,833	5,058
Earnings per share — basic (pence)	**14.71**	13.77	9.97	7.52	10.12
— adjusted (pence)	**14.71**	13.77	11.28	9.39	10.59
Dividend per share (pence)	**6.24**	5.20	4.70	4.12	4.12
Average number of employees	**691**	679	643	615	500
Balance sheet					
Non-current assets	**13,567**	12,391	10,398	11,302	11,608
Working capital	**11,774**	12,127	11,318	12,189	10,256
Current tax liabilities	**(2,505)**	(2,057)	(1,275)	(1,032)	(1,387)
Deferred tax liabilities	**—**	—	(174)	—	—
Net cash/(debt)	**1,079**	(4,859)	(10,110)	(14,988)	(14,728)
Shareholders' funds	**23,915**	17,602	10,157	7,471	5,749
Cash flow					
Cash flow from operating activities	**13,997**	13,549	10,576	6,542	6,397
Net interest paid	**(1,218)**	(1,667)	(1,012)	(1,384)	(1,126)
Tax paid	**(2,618)**	(1,996)	(1,864)	(2,066)	(2,155)
Capital expenditure	**(1,492)**	(1,925)	(546)	(1,224)	(2,704)
Acquisitions	**—**	—	—	32	(3,823)
Equity dividends paid	**(2,777)**	(2,473)	(2,192)	(2,078)	(1,927)
Financing	**(97)**	11,760	(2,588)	(3,410)	(765)
Changes in cash in period	**5,795**	17,248	2,374	(3,588)	(6,103)

* Reported under IFRS

† Reported under UK GAAP

Dechra
Pharmaceuticals PLC

Company Financial Statements

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Company Balance Sheet

At 30 June 2006

	Note	2006 £'000	2005 restated* £'000
Fixed assets			
Investments	iii	**53,408**	53,408
		53,408	53,408
Current assets			
Debtors	iv	**43,536**	41,471
Cash at bank and in hand		**1,638**	1,345
		45,174	42,816
Creditors: amounts falling due within one year	v	**(52,090)**	(48,331)
Net current liabilities		**(6,916)**	(5,515)
Total assets less current liabilities		**46,492**	47,893
Creditors: amounts falling due after more than one year	v	**(14,095)**	(17,010)
Net assets		**32,397**	30,883
Capital and reserves			
Called up share capital	ix	**519**	511
Share premium account	x	**27,693**	26,953
Hedging reserve	x	**(71)**	—
Profit and loss account	x	**4,256**	3,419
Total equity shareholders' funds		**32,397**	30,883

* The comparatives have been restated for the adoption of FRS20 and FRS21 by the Company (see note xi).

The financial statements were approved by the Board of Directors on 5 September 2006 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 2006

	2006 £'000	2005 £'000
At start of year as previously stated	33,111	32,655
Prior year adjustments (see note xi)	(2,228)	(2,394)
At start of year as restated	30,883	30,261
Impact of adoption of FRS26 on 1 July 2005 (see note i)	(71)	—
At 1 July 2005 as restated	30,812	30,261
Profit for the financial year	3,187	2,437
Share-based payments charge	427	488
Dividends paid	(2,777)	(2,473)
New shares issued	748	170
At end of year	32,397	30,883

Accounting Policies

(i) Principal Accounting Policies of the Company

Accounting Principles

The Company Balance Sheet has been prepared under the historical cost convention except for derivatives which are stated at fair value in accordance with applicable UK accounting standards and the Companies Act 1985.

The Company has adopted FRS20, share-based payments, FRS21 (IAS10), Events After the Balance Sheet Date and from 1 July 2005, FRS25 (IAS32), Financial Instruments: Disclosure and Presentation, FRS26 (IAS39), Financial Instruments: Measurement and FRS28 Corresponding Amounts in these financial statements. The adoption of these standards represents a change in accounting policy and accordingly the comparative figures have been restated where required. Details of the effect of the change in policy are given in note xi.

Basis of Preparation

No Profit and Loss Account is presented for the Company as permitted by Section 230(3) of the Companies Act 1985. The profit dealt with in the accounts of the Company was £3,187,000 (2005: £2,437,000).

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.

Derivative Financial Instruments (applicable to 30 June 2005)

All financial assets and liabilities are carried at cost (amortised as appropriate) less, in the case of financial assets, provisions for permanent diminution in value.

Derivative Financial Instruments (applicable from 1 July 2005)

The Company uses derivative financial instruments to manage its exposure to foreign exchange and interest rate risks. In accordance with its treasury policy, the Company does not hold or issue derivative financial instruments for speculative purposes. However, derivatives that do not qualify for hedge accounting are accounted for as trading instruments.

On adoption of FRS25 and FRS26, the comparative financial statements have not been restated. As permitted, the comparative statements continue to hedge account under UK GAAP. On 1 July 2005, the fair values of derivatives used for hedging were included in a hedging reserve. The corresponding adjustments were to decrease trades and other receivables by £58,000, increase trade and other payables by £44,000 and increase the deferred tax asset by £31,000. As the Company has not adopted hedge accounting under FRS26 from 1 July 2005 the hedging reserve is frozen and will only be released to the profit and loss account when the related forecast transactions occur.

Derivative financial instruments are recognised initially at fair value. Subsequent to initial recognition, derivative financial instruments are stated at fair value. The gain or loss on remeasurement to fair value is recognised immediately in the profit and loss account.

The fair value of interest rate swaps, floors and ceilings, is the estimated amount that the Group would receive or pay to terminate the instrument at the balance sheet date. The fair value of forward exchange contracts and options is their quoted market price at the balance sheet date, being the present value of the quoted forward price.

Cash Flow Statement

As the ultimate holding company of the Dechra Pharmaceuticals PLC Group, the Company has relied upon the exemption in FRSI (Revised) not to present a cash flow statement as part of its financial statements.

Dividends

Dividends are recognised in the period in which they are approved by the Company's shareholders or, in the case of an interim dividend, when the dividend is paid.

Dividends receivable from subsidiaries are recognised when either received in cash or applied to reduce a creditor balance with the subsidiary.

Interest-Bearing Borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis.

Employee Benefits

(i) Pensions

The Company operates a Group stakeholder personal pension scheme for certain employees. Obligations for contributions are recognised as an expense in the profit and loss account as incurred.

(ii) Share-Based Payment Transactions

The Company operates a number of equity-settled share-based payment programmes that allow employees to acquire shares of the Company. The Company also operates a Long Term Incentive Plan for Directors and Senior Executives.

The fair value of shares or options granted is recognised as an employee expense on a straight line basis in the income statement with a corresponding movement in equity. The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the shares or options (the vesting period). The fair value of the shares or options granted is measured using a valuation model, taking into account the terms and conditions upon which the shares or options were granted. The amount recognised as an expense in the profit and loss account is adjusted to take into account an estimate of the number of shares or options that are expected to vest together with an adjustment to reflect the number of shares or options that actually do vest except where forfeiture is only due to market-based conditions not being achieved.

The fair value of grants under the Long Term Incentive Plan has been determined using the Monte Carlo simulation model.

The fair values of options granted under all other share option schemes have been determined using the Black-Scholes option pricing model.

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".

Financial Guarantee Contracts

The Company has not adopted amendments to FRS26 in relation to financial guarantee contracts which will apply for periods commencing on or after 1 January 2006.

Where the Company enters into financial guarantee contracts to guarantee the indebtedness of other companies within its group, the Company considers these to be insurance arrangements, and accounts for them as such. In this respect, the Company treats the guarantee contract as a contingent liability until such time as it becomes probable that the Company will be required to make a payment under the guarantee.

The Company does not expect the amendments to have any impact on the financial statements for the period commencing 1 July 2006.

Notes to the Financial Statements

For the year ended 30 June 2006

(ii) Directors and Employees

Total emoluments of Directors (including pension contributions) amounted to £698,000 (2005: £595,000). Information relating to Directors' emoluments, share options and pension entitlements is set out in the Directors' Remuneration Report on pages 34 to 39.

Including Directors, the average number of staff employed during the year solely in an administrative function was 8 (2005: 3). The costs incurred in respect of these employees were:

	2006 £'000	2005 £'000
Wages and salaries	601	151
Social security costs	77	14
Other pension costs	61	14
Share-based payment charge	173	165
	912	344

(iii) Fixed Asset Investments

	Shares in Subsidiary Undertakings £'000
Cost and net book value	
At 1 July 2005 and 30 June 2006	53,408

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

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.

(iv) Debtors

	2006 £'000	2005 restated* £'000
Amounts owed by subsidiary undertakings	42,403	40,433
Group relief receivable	775	537
Deferred taxation (see note viii)	260	200
Other debtors	11	191
Prepayments and accrued income	87	110
	43,536	41,471

Included in debtors are amounts of £260,000 (2005: £200,000) due after more than one year.

* The comparatives have been restated for the adoption of FRS20 and FRS21 by the Company (see note xi).

(v) Creditors

	Falling due within one year	
	2006	2005 restated*
	£'000	£'000
Bank loans (see note vi)	**3,000**	1,400
Amounts due to subsidiary undertakings	**48,551**	46,624
Other creditors	**8**	8
Other taxation and social security	**60**	23
Accruals and deferred income	**471**	276
	52,090	48,331

In accordance with FRS21, Events after the Balance Sheet Date, the proposed final dividend for the year ended 30 June 2006 of 4.33p per share has not been accrued for in these financial statements. It will be shown in the financial statements for the year ending 30 June 2007. The total cost of the proposed final dividend is £2,248,000.

	Falling due after more than one year	
	2006	2005
	£'000	£'000
Bank loans (see note vi)	**14,095**	17,010

(vi) Borrowings

	2006	2005
	£'000	£'000
Borrowings due within one year		
Bank loan	**3,000**	1,400
	3,000	1,400
Borrowings due after more than one year		
Aggregate bank loan instalments repayable		
between one and two years	**4,000**	3,000
between two and five years	**10,200**	14,200
	14,200	17,200
Arrangement fees netted off	**(105)**	(190)
	14,095	17,010
Total borrowings	**17,095**	18,410

The term loan from Bank of Scotland is secured by a fixed and floating charge on the assets of the Group. Interest is charged at 1.25% over LIBOR.

The Company guarantees certain borrowings of other Group companies, which at 30 June 2006 amounted to £1,239,000 (2005: £nil).

* The comparatives have been restated for the adoption of FRS20 and FRS21 by the Company (see note xi).

Notes to the Financial Statements

For the year ended 30 June 2006

(vii) Financial Instruments

	2006 £'000	2005 £'000
Changes in fair value credited to profit and loss	**30**	—

Details of valuation techniques and fair values of each category of financial instruments are given in note 20 to the Consolidated Financial Statements in the section headed 'Fair values of Financial Instruments'.

(viii) Deferred Tax

	£'000 restated*
At 1 July 2005 (included in debtors)	(217)
Prior year adjustment	17
As restated	(200)
Adoption of FRS 26 on 1 July 2005	(31)
Transfer to profit and loss account	(29)
At 30 June 2006 (included in debtors)	**(260)**

The amounts provided for deferred taxation at 30% (2005: 30%) are as follows:

	2006 £'000	2005 £'000
Short term timing differences	**(260)**	(217)
Total	**(260)**	(217)

(ix) Called up Share Capital

	Ordinary Shares of 1p each	
Issued share capital	£'000	No.
At 1 July 2005	511	51,120,964
New shares issued	8	794,038
At 30 June 2006	**519**	**51,915,002**
Authorised share capital At 30 June 2006 and 30 June 2005	750	75,000,000

During the year, 794,038 new ordinary shares of 1p were issued following the exercise of options under the Unapproved and SAYE share option schemes. The consideration received was £748,000 (2005: £170,000).

Share Options

Details of outstanding share options over ordinary shares of 1p at 30 June 2006 under the various Group share option schemes are shown in note 22 to the Consolidated Financial Statements.

* The comparatives have been restated for the adoption of FRS20 and FRS21 by the Company (see note xi).

(x) Reserves

	Share premium account £'000	Hedging reserve £'000	Profit and loss account £'000
At 1 July 2005 as previously stated	26,953	—	5,647
Prior year adjustment (see note xi)	—	—	(2,228)
As restated	26,953	—	3,419
Adoption of FRS26 on 1 July 2005	—	(71)	—
At 30 July 2005 as restated	26.953	(71)	3,419
New shares issued	740	—	—
Profit for the financial year	—	—	3,187
Dividend (see note 8 to Consolidated Financial Statements)	—	—	(2,777)
Share-based payments charge	—	—	427
At 30 June 2006	**27,693**	**(71)**	**4,256**

(xi) Changes in Accounting Policy

The Company has adopted the following standards FRS20, Share-Based Payments, FRS21, Events After the Balance Sheet Date, and, with effect from 1 July 2005, FRS25, Financial Instruments: Disclosure and Presentation, and FRS26, Financial Instruments: Measurement.

Under previous UK GAAP, the cost of granting employee share options recognised in the income statement was the intrinsic value of the option being the difference in exercise price and market price at the date of grant of the option. Options issued under Save As You Earn ("SAYE") schemes were exempt from this requirement. Previously the Company has recognised a charge to the Profit and Loss Account only in respect of the Long Term Incentive Plan.

Under FRS20 'Share-Based Payments', the cost recognised in the income statement is based upon the excess of the fair value of the option over the exercise price at the date of grant.

Although this results in an additional charge in respect of the Company's Approved, Unapproved and SAYE share option schemes, there is a reduction in the charge in respect of the Long Term Incentive Plan. The net result is a credit of £55,000 for the year ended 30 June 2005.

There is no impact on net assets or distributable reserves as a result of this adjustment which is taken directly to equity.

An additional deferred tax charge of £17,000 has been made to reflect the tax effect of the above adjustment.

Under FRS21 'Events After the Balance Sheet Date' final dividends are generally recognised in the subsequent accounting period to which they would have been recognised under previous UK GAAP. At 30 June 2005, the final dividend for 2005 of £1,789,000 (2004: £1,606,000) has been added back to net assets as part of distributable reserves and appears as a deduction from equity in the year ended 30 June 2006.

Similarly, dividends receivable from subsidiaries are generally recognised in the subsequent accounting period to which they would have been recognised under previous UK GAAP. At 30 June 2005, dividends of £4,000,000 (2004: £4,000,000) have been deducted from net assets as part of distributable reserves and are included within profit for the year in the year ended 30 June 2006.

The Company adopted FRS25 and FRS26 with effect from 1 July 2005. In accordance with the transitional provisions of these standards, the comparative financial statements for 2005 have not been restated.

Notes to the Financial Statements

For the year ended 30 June 2006

(xii) 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
Dechra Investments Limited	UK	Great Britain	Holding company
National Veterinary Services Limited*	UK	Great Britain	Non-trading
Arnolds Veterinary Products Limited*	UK	Great Britain	Non-trading
Dales Pharmaceuticals Limited*	UK	Great Britain	Non-trading
Veneto Limited	UK	Great Britain	Holding company
North Western Laboratories Limited	UK	Great Britain	Non-trading
Cambridge Specialist Laboratory Services Limited†	UK	Great Britain	Non-trading
Anglian Pharma Manufacturing Limited‡	UK	Great Britain	Non-trading
Anglian Pharma Limited	UK	Great Britain	Holding company
Dechra Veterinary Products LLC	USA	USA	Distributor of veterinary products

* 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 Dechra Investments Limited.

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

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

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