GLAXOSMITHKLINE

2013 Results Review

Sir Andrew Witty

Hello. I would like to welcome you to the 2013 Results Review for GlaxoSmithKline. It gives me great pleasure to take this opportunity to talk you through some of the achievements and deliveries for last year and also importantly lay out our priorities and areas of focus for 2014.

2013 is a year I am very proud of at GSK. We were able to deliver right at the top of our earnings guidance range that we issued a year ago based on sales growth, helped along by the extraordinary delivery of our R&D portfolio.

GSK strategy is delivering

During the year we continued to build on the strategy and the foundations that we laid out six years ago consistently and resolutely focussed on building an organisation which is sustainable for the long-term, focussed on organic sales growth, looking for areas of diversified sales growth within our portfolios, making sure we take advantage of every opportunity that our Vaccine, Consumer and Pharmaceuticals businesses gives us, a business focussed on truly modernising the way in which research and development is done in the pharmaceutical sector.

We began that journey six years ago and we have continued resolutely to focus on what we believe are the right ways to drive innovation, creativity but at a good economic return, recognising that this just can't be a place where endless amounts of money can be invested. We believe we have made significant progress on that agenda.

We have also continued to be focussed on how we can simplify and streamline our business. By definition as a global company operating over in 100 companies we are bound to be complex but we can choose to be simpler in some key parts of our organisation and by doing that we can focus our attentions on what is really important; improving our interface with customers, getting our customer service levels right and making sure we improve returns to shareholders.

So our strategy remains absolutely as it has been for the last several years and I believe in 2013 we have seen some good evidence of really positive steps forward in the direction of travel that we want to see.

I am more convinced than ever today that the strategy we have laid out is right also for what has become an increasingly dynamic and changing environment. It is important that as we face different challenges in different parts of the world from different countries, different payers, that we have that breadth of presence so that from within the overall portfolio of our businesses we can deliver the growth and the earnings that our shareholders are looking for.

The environment we are in in my view has never been more challenging than it is today. On the one hand there is opportunity everywhere because of the fundamental demographics of the world, greater demands for healthcare, greater demands for higher quality healthcare, but all contrasted against a tough economic background of the last five or six years amplifying payer anxieties.

It is important that we modernise the way in which we offer our products into the marketplace. It is important that we modernise the value for money proposition that we as a pharmaceutical company can give and that's a key part of our overall strategic stance, to make sure that yes, we can discover new medicines, yes we can commercialise those medicines but we do that in step with the environment in which we now operate.

Our delivery for shareholders I believe is a very straightforward proposition; to grow our sales, to drive leverage through control of our cost base, to spin off more cash which is then dedicated primarily to go back to the shareholder, and I am delighted again that this year we are able to announce a further increase in our dividend to 78 pence per share, up another 5% on top of the £1.5 billion of share buy-back during 2013, meaning that once again during this year alone we have given back to our shareholders over £5 billion through the share buy-back and the dividend.

6 new product approvals support GSK businesses

Now if I look at the performance of the businesses over the last year or so, it also becomes clear the shape of how GSK is evolving. Again, we are a large company and it really boils down to a company focussed on three globally leading businesses. Then we have two challenger businesses, businesses that we have been investing in in our pipeline, which now have new products and give us the chance to increase our competitive position.

Those businesses together shown on this slide represent 70% of the company, by far the majority of the company, essentially committed to these five business areas and these business areas delivered last year 4% sales growth. So 70% of the company growing at 4% at constant exchange rates.

Now within these five businesses there are three absolutely established global leadership positions; our Respiratory business, our Vaccine business and of course our Consumer business, each one of which characterised by deep global presence, very deep portfolios and significant continuous innovation.

I will touch a little more in particular on Respiratory in a few moments, but just to say something about Vaccines. Over the last several years with the launch of *Cervarix, Synflorix, Rotarix* and particularly in 2013 with the launch of the new quadrivalent flu vaccines in America, we have seen innovation combined with our global footprint allow us to drive forward and really establish a number one global leadership position in vaccines. That's something we are committed to continuing to do and there are exciting opportunities coming forward in the next two years alone as we continue to see more data from our MAGE-A3 programme, we look forward to the results of our zoster vaccine programme and we are also starting to move programmes such as *PRAME* into late stage development.

Our Vaccine business supported by an extraordinary capital base gives us great confidence for future opportunity.

In the Consumer business we have seen some very important changes to that portfolio and I will touch more on that in just a couple of minutes.

If we think about these challenger areas of HIV and oncology, these are both areas that GSK has been strong in the past or present in the past, but over the last few years we have not been global leaders but we have been working hard to refresh our pipeline and our new product opportunity.

So we come into 2014 with great optimism here, built on the delivery of new products. Of the six new products which we had approved last year, three land into these two areas; MEK and BRAF for oncology and of course dolutegravir for HIV, all three launched, all three successfully launched, and all three giving us new impetus and energy within these businesses.

So our focus as we look forward over the next two or three years is to continue to look for ways in which we can continue to strengthen our opportunities here. Now in the past we have done that in HIV in some creative, unusual ways through the creation of the ViiV partnerships with Pfizer and Shionogi, and we will continue to look for those sorts of opportunities to make sure that when we have high quality new product entries that we don't lose time, don't lose opportunity building a market position.

During 2013 we also announced the creation of the Established Products Group. That accounts for about 16% of turnover during the year. Why did we do this? It gave us a chance to focus on how we can streamline that portfolio, reduce a number of SKUs in that portfolio, provide a more efficient service support to that portfolio and where necessary divest parts of that portfolio, and you saw during 2013 some significant steps in that direction, particularly with the divestment of *Arixtra* and *Fraxiparine*.

We will continue to look for those opportunities. This is a part of the business where we believe it adds value for the company, but where we want to focus on efficiency and ensuring that if there are opportunities for value creation through divestment we will certainly explore them fully.

New respiratory portfolio provides platform for maintained market leadership to 2020 and beyond

Now I would like to move on to give you a little bit more detail of Respiratory. Now Respiratory has been an absolute bedrock of this company for the last 40 years and we continue to believe it will be a bedrock for the next ten, 20, 30 years. Why do we believe that?

First of all our established products within the Respiratory business, the *Ventolin*s, the *Flovents* and of course *Advair* remain in their own rights market leaders in many countries across the world. While they have been around for many years, in many cases they remain unchallenged and unsurpassed in what they are able to bring to patients.

That gives us a tremendous platform to build with confidence. It also gives us a deep expertise in an understanding of respiratory disease and particularly inhaled respiratory medicine.

That has proven to be a differentiating factor in the last three or four years. Over that three or four years we have heard numerous putative competitors who had great plans to enter this category, whether they be generic or whether they be branded but with almost no exception, all of those competitors have run into significant technical challenges in trying to develop inhaled medicines.

It is an extraordinarily difficult thing to do. It is an extraordinarily challenging scientific proposition and it doesn't get any easier when you move into the factories. This is an area where for 40, 50 years GSK has been an innovator and a leader. It is our expectation, and it's my expectation that we will remain the leader in the respiratory marketplace well into the next decade, and the reason I believe that is because of the extraordinary strength of our pipeline.

During 2013 alone we had two new medicines approved in the US, one of which is already launched, so *Breo* the first once a day, ICS-LABA combination and *Anoro*, the first double bronchodilator registered in the US.

But in addition to those two, we have seven more respiratory programmes in advanced development and they are shown on this slide. Importantly, for all of those inhaled medicines they are all built on the same *Ellipta* technology, the same device technology. It gives us a chance not to just innovate the medicine, but also the device. That we believe has the potential to give patient benefit and of course efficiency for the organisation.

Good early progress in *Breo Ellipta* launch

If we move now to look specifically at *Breo*, our first new product launch from this pipeline, I am very pleased with the initial reaction from the marketplace is very good, and the recognition of physicians of the benefits of the product are encouraging. The challenge that we want to focus on and we understood would be there, is the coverage from insurance companies, particularly in the Medicare Part D which is important for COPD. Things are very different now from four or five years ago even, and it takes time to build this coverage, but I am delighted with the progress we have been making. After just a few weeks we already have 25% of patients who are covered by Medicare Part D now entitled to access to *Breo*, and over two-thirds of those people who are under commercial insurance plans.

The key really now to the uptake of the product is to make sure we continue to build that coverage during the rest of the year. I am very, very encouraged by the numbers of prescriptions which are being written. Today some of those aren't making it all the way through to a filled prescription because the coverage isn't there, and that's what we're going to focus on over the next few weeks and months. Early signs for *Breo* are very encouraging.

Rapid market share gains for *Mekinist* and *Tafinlar*

I want to touch on the oncology marketplace. Over the last year or two as we brought *Tykerb, Votrient* and now particularly our MEK and BRAF inhibitors to the V600 melanoma patients, we have started to see some really material innovation and the performance of this category has improved significantly. Now we are still a small player within the global oncology marketplace and we need to think hard about how we can continue to accelerate the contribution of our medicines into this category, but I did want to just take a minute to reflect on just how successful these launches have really been.

Already we have 60% market share of total prescriptions in this category. The most recent data tells us we have almost 70% market share of new prescriptions. That's a remarkable performance. We have done that with a very small organisation and really driven by the differentiated quality of these medicines.

We remain extremely optimistic for MEK and BRAF but we also recognise this is an area of great innovation which is why we continue to explore further opportunities for these products, for example in adjuvant melanoma setting and also explore partnerships with other companies who are developing, for example, immuno-oncolytics and perhaps look at sequencing and combination opportunities going forward.

Rapid market share gains for *Tivicay*

Let me move to another area of innovation for the company - HIV, the ViiV business. We created the ViiV business four years ago with a real focus to make sure that if we could we would develop a true breakthrough medicine in the shape of dolutegravir, *Tivicay*. *Tivicay* was launched in the middle of last year and has been an extraordinarily successful product launch.

You can see from this slide, very strong coverage for this medicine, very good access. You see very, very strong uptake in the product, already 8% market share of that dynamic marketplace.

This is shaping up to be one of the best HIV product launches of recent years. I am very proud of the performance of ViiV and of course we are excited because dolutegravir is the first of several new opportunities as we think forward into combination products and we also think forward into super long-acting integrase inhibitors which have potential utility in both the developed and of course the developing world.

So for us HIV and ViiV in particular has delivered exactly what we hoped. We have gone across the bridge from our old portfolio to the new, and we are now in a situation where our innovation can really help us drive forward competitively.

Pipeline opportunity is significant for GSK

If we think about the overall performance then of R&D over the last few years, it has really been I think tremendous. If you look since 2009, GSK has achieved 17 US FDA approvals for NCEs, NMEs and vaccines. That is significantly more than any other company. That volume really reflects the changes we have made in GSK, the creation of a Discovery Performance Unit to energise our researchers, the leaning of the whole organisational process to ensure that we invest money in the best highest prospect research projects, and to make sure that we don't waste time in that process, that we get things to patients as quickly and as safely as we possibly can.

If we look on this slide, in 2013 alone six major approvals in the US, really an unparalleled performance and the majority of those medicines and molecules discovered inside GSK laboratories.

Now lots of people talk about lots of numbers in R&D. I have chosen only to show the new molecular entities. What does that really mean? It means a new chemical entity or a new vaccine or the combination of two medicines into a single new product. It does not include any line extensions, it doesn't include any tweaks or twists or incremental steps of innovation. If I showed you the list of all the programmes in GSK with all of the line extensions, we would be into huge numbers but the reason to show this, the 40, the six, the ten, is that this is really substantial innovation; new step forwards in a variety of key diseases.

The combination of all of this progress has really been characterised if you will by the continued improvement in the rate of return for our R&D business. We have just re-run the numbers again and we believe based on the pipeline we have today, particularly helped by the number of programmes now at the very late stage or even at the approval stage the risk profile has diminished for many of our products. That has lifted our rate of return again to 13%. As you know, our long-term goal is 14% and we are well on the way to that and I am proud that we are I think still the only company that has the discipline to hold ourselves accountable to that performance for shareholders in terms of delivering value for money.

I just wanted to touch briefly on two of the emergent areas of the earlier part of the pipeline. As you know, I am not one of those people who is going to stand up and talk about lots of Phase I projects in detail. By definition they are high-risk and lots of them will fail. In fact, if they are not failing you are probably not trying to be innovative enough, but I did want to just share a little bit of where some of the early science in GSK is now maturing into development programmes in areas where there is significant unmet medical need and where we are beginning to see in a complementary way to those five businesses I described earlier on, continued growth of potential portfolio.

Emerging portfolios in Immuno-inflammation and Cardiovascular & Metabolic

They really fall into two areas; immunoinflammation and cardiovascular metabolic and you can see from this slide a whole raft of different areas, very innovative, great new science, particularly in the immuno-inflammation field, I think we have in epigenetics and in some of the other pattern recognition programmes really global leadership positions in that science understanding which we believe can drive forward portfolios of products in the future.

If I look at the cardiovascular metabolic area, we are excited about the short-term prospects for albiglutide in Type 2 diabetes, and I remain very optimistic and excited about the potential for our Lp-PLA2 programme led by darapladib with many other follow-ups behind, where we continue to see evidence which convinces us that this is an opportunity for the company.

We are also very excited about the PHI programme with its lead indication in anaemia but with subsequent number of exploratory programmes in other indications.

£4.7bn Consumer business growing across all categories and all regions

I would like to touch on Consumer, an important part of our organisation. Now, part of our organisation where we have worked hard over the last five years to again bring focus, and if we look at Consumer today, essentially it is four key platforms within our global Consumer business: a wellness business, a traditional OTC, cough and cold respiratory-type of business; a nutrition business, really driven by our Indian nutritional *Horlicks* business; oral care led by *Sensodyne*, a real blockbuster of consumer products; and skin health, helped particularly by the acquisition of Stiefel just a few years ago.

These four platforms is where we are really investing to achieve and sustain category leadership. I am particularly pleased with the performance of this business in its globalisation. It is a business which really helps us to establish our Emerging Markets position in many situations.

We continue to look for opportunities to further enhance this business in particular through organic innovation, and over 2014, we expect up to 30 unique points of innovation to be brought to these four platforms. It is that type of innovation, leveraging our R&D base which gives us we believe points of differentiation.

You will have also seen, though, to get to this focus, we have made some tough decisions on how to streamline the business. We have divested the non-core tail, and we have also most recently divested the *Lucozade* and *Ribena* business. In both cases, they were good deals for shareholders, value-creating, but what they also allowed us to do was to get to where we really wanted to be in terms of a true focused, high quality, global Consumer Healthcare business.

Portfolio Optimisation to enhance growth, profitability and cash generation

That kind of change of structure of the business, being open-minded to divest when it makes sense, is a part of the way we are thinking about optimising our portfolio, and it doesn't just apply to Consumer. You saw last year the *Fraxiparine/Arixtra* business was divested, we exited *Vesicare* earlier. At the same time, we have been building up our presence in other businesses which we believe are going to be high growth opportunities in the future. Right now, we are exploring how we can build up our Indian pharmaceuticals' shareholding in that business. Last year, we lifted our stake in our Indian Consumer business. We have done other transactions, for example, acquiring HGS, all of those to take a greater share of the positive economics that we believe exist there.

We have used acquisitions very sparingly to achieve scale. In Emerging Markets it was important in those early days to achieve more scale, through Stiefel to really enhance our Dermatology business, but acquisitions are not really a core strategy for GSK. They are there for a purpose, they have to meet the challenge of beating the share buyback in terms of value creation, and as a result, they are not really a core part of the strategy. Why? Because we believe focusing on really the organic growth, fixing R&D, deploying our capital efficiently, those are the ways to absolutely maximise shareholder return over the long term.

2014 Priorities

So, as we think about 2014, the priorities for the company I think are very, very clear. This slide really summarises those ones which we believe if we can execute well during this year, we will continue to be able to deliver a significant return for shareholders.

As a company, we want to build a position which is focused on innovation and access. Access means making sure we are working hard to have a modern view of the world, to recognise that large numbers of the world, the majority of the world, do not live in the rich west, but they do have an aspiration for healthcare, and we need to make sure we have a strategy and a policy framework which addresses that. We believe the best way to do that is to be the world's most efficient and effective R&D organisation, to be a great innovator, and to then have a capability and a mindset which allows us to challenge our business model, the way we interact with customers, the way we think about pricing, to maximise access around the world. We think that's how we build a long term position, a capability. Those are fundamental, but to do that, we need to be great, not just at R&D delivery, we need to be great at launches, at execution of that commercial capability. I think the evidence of 2013 is extremely encouraging, and I believe during the next few months in 2014, as we see the *Breo* position build, we will continue to see very reassuring signals, but it is an area of focus for us. Our Emerging Markets are an important platform for us. We need to make sure that we stay in step with the rapidly evolving needs and demands of our customers and the governments with whom we want to partner.

Our Consumer business needs to deliver innovation to really win and prosper. We are in a good place for that, but it's an area we want to make sure we deliver on during the year. The Vaccine business has an extraordinary platform with its capital base and global footprint. The continued innovation, this year I hope through MAGE-A3 results, through the Zoster data over the next year or so, will give us further opportunity to strengthen an already significant position.

Our industry leading position with the way in which we work with GAVI and the Global Fund, the Gates Foundation, to help deliver vaccines to the poorer countries in the world, will also be a key part of that business. And of course, during this year, the company will file for the approval of the world's first potential vaccine for malaria, an extraordinary achievement, and potentially an extraordinary contribution to human health in some of the poorest countries in the world.

We will stay focused on improving R&D returns. Everything that I have described in these few minutes about what R&D has done, has been done with a flat or falling budget in pharmaceutical R&D. I believe that really challenges the dogma that you have to invest more and more and more to deliver creative, innovative R&D. I think we have been able to show that with discipline, with focus and empowering our organisations, we can in fact recreate an energised R&D organisation without having to spend more and more money. Of course, that is what is helping contribute to that increasing rate of return.

All of this, if we get our positioning right in the big world, if we get our focus and strategies right within the company, all of this will improve our performance. If we do that, our commitment with that cashflow we produce is to return it to our shareholders.

Thank you very much for your attention.

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GLAXOSMITHKLINE

2013 Results Review

Simon Dingemans

As those of you who have followed us for some time will know, our strategy has very consistently focussed on building a more balanced business by reinforcing the strengths of our three key Pharma, Vaccines and Consumer businesses across different geographies as well as improving our R&D productivity and flow of new products.

Our financial architecture is designed to ensure we are driving the returns out of that more sustainable growth by ensuring we continue to simplify our business, allocate our resources more efficiently and flexibly and build leverage across the P&L to drive earnings per share faster than sales and in turn convert more of those earnings into cash that we can either reinvest in the business or return to shareholders wherever the returns look most attractive.

Our financial performance in 2013 highlights the progress we have made against these objectives with delivery of sales and earnings growth at the upper end of the guidance range we gave at the start of the year, despite a number of unexpected headwinds, including the ongoing investigation by the Chinese authorities.

This delivery reflects the better balance of the group today and the broader range of growth drivers now contributing to the top line.

It also demonstrates the improving flexibility and efficiency of our cost base that allowed us to absorb those headwinds while still protecting the investments we need to make behind our growth markets and new product launches.

Our improved responsiveness also positions us well for 2014, even though we have a number of uncertainties to manage during the year as we launch an unprecedented number of new products at the same time as we are facing potential competition to a number of older products, particularly *Lovaza.*

Our guidance for 2014 reflects this mix of factors and is why we have indicated a range around our expected EPS growth of 4-8% on turnover growth of around 2%, both on a constant currency basis.

I should remind you that the guidance is given on a base for 2013 adjusted for divestments completed during last year. Clearly any disposals will distort the reported numbers and so to avoid confusion we will be providing guidance on an ex-divestment basis going forward, consistent with how we look at the group on an ongoing basis.

The disposals made last year all achieved good prices and released significant resources for reinvestment behind the core business as well as supporting the ongoing programme of returns to shareholders. The benefits of the disposals are also clear in the improved performance of the Consumer and Pharma businesses.

We will continue to look at ways of sharpening the group's strategic focus where we can realise attractive values.

Headline results

If we turn to the core results for 2013, you can see that turnover grew 1% at constant currency rates, in line with our guidance.

We also worked the P&L to deliver leverage resulting in EPS growth that outpaced sales growth. Our core EPS grew 4%, again in constant currencies.

As expected, we saw greater leverage in 2013 from the bottom half of the P&L on the back of continued financial efficiencies but the top half of the P&L is far from static with strong delivery from our ongoing restructuring programmes and around £400 million of incremental cost savings released relative to 2012. In particular, a lot more flexibility is now emerging in our cost base that is allowing us to reallocate rather than have to add resource to get behind the current launches.

Although the launches are off to a good start, they are still at a relatively early stage and we are going to need to continue to invest in 2014 to build the strongest market positions that we can for these important new products. As a result, in the short term the greater degree of leverage is still likely to come from the bottom half of the P&L until the new products begin to contribute more materially.

Lastly, on cash flow for the year net cash from operations excluding legal was up 5% versus last year. Free cash flow on the same basis was up slightly less at 2% reflecting the ongoing restructuring and capex investments we are making. We still generated just under £4.8 billion and contributed to the significant cash returns we made to shareholders through the dividend and ongoing buy-back programme.

2013 Sales growth

The slide lays out for you very clearly the breadth of contributions across the business that delivered the overall reported growth of 1% in constant currency.

Divestments made during 2012, including Vesicare and the OTC tail reduced reported sales by £338 million and impacted overall top line growth by 2%.

Looking at the US, the business reported its first full year of growth since 2006. Respiratory grew 7%, with the benefit of better pricing, particularly during the first half of the year and some help from wholesaler and retailer stocking patterns, particularly in the fourth quarter.

Oncology grew 17% with *Votrient* and *Promacta* growing strongly and we have now launched *Mekinist* and *Tafinlar.* Vaccines grew 17% in the US, benefitting from some competitor supply issues but also the successful launch of our quadrivalent flu vaccine.

Europe was flat on last year. This represents a considerably better performance compared to 2012 when sales were down 7%. Europe is a good example of where our restructuring and refocusing is really paying off. Following the wave of austerity measures in recent years, we restructured the business materially and took a lot of above country overhead out and reduced the headcount but, most importantly, we also reallocated a lot of our sales force effort behind the franchises that really count in Europe, including Respiratory, Vaccines, Oncology and *Avodart/Duodart*.

In 2014 we are expecting continued competitive pressure on our respiratory business in Europe including the launch of additional non-substitutable generics in some markets. So far this is in line with what we expected.

Japan continues to also make progress with strong Pharma growth, up 9% offset by a setback in the Vaccines business following the suspension of the Government's recommendation for HPV vaccinations during the second half. Respiratory was a particularly strong contributor, up 9% and we have just launched *Relvar* in Japan.

I know the outlook for Emerging Markets has been subject to quite a lot of debate over the last several months but for us they remain a very important part of the strategy. We have invested heavily here and are comfortable with the footprint we have built. Even though they may have slowed a little, mid to high single digit growth is still very attractive for us.

Events in China in the second half clearly impacted our reported Emerging Markets performance. For the year, our China Pharma and Vaccines business was down £125 million, a decline of 18%.

But overall, compared to the similar chart I showed you last year when Europe and Viiv were down and the US was flat, you can now see a much more even performance building across the company during 2013.

Further Strengthening of business mix

Looking at our turnover for 2013 in a little more detail, over the last couple of years in addition to expanding our geographical footprint, we have put more focus into strengthening our Vaccines and Consumer businesses.

This has created a more resilient company and helped deliver the stronger performance we have seen in 2013.

We have made some bolt-ons but also, importantly, we have made a number of divestments leaving 70% of the company now focussed around those businesses where we already have leadership positions or where we see particular opportunities to grow in the future.

For the remainder of the business we are now moving around 16% of our sales into our new Established Products portfolio which comprises over 50 brands and £3.9 billion of sales after stripping out the recent divestments to Aspen. We have set up this separate unit to bring greater focus on how we optimise value and in particular profit and cash from this group of products. Where we can realise more attractive value than our own efforts, we will also consider further divestments.

Going forward we will show the performance of this unit separately within our results and we will provide further details of restatements during Q1.

GSK financial architecture ensuring focus on returns

As I said earlier, we continue to utilise our financial architecture to make sure that we are driving the returns from the growth we are creating by building leverage across the P&L, driving earnings per share faster than sales and converting more of those earnings to cash.

Most importantly our financial architecture is helping us to allocate our resources and our capital more effectively.

Operating profit margin breakdown

Looking to our operating margin, excluding currency which I have already touched on, the operating margin was down approximately half of a percentage point. This primarily reflected the impact of the upward pressure we were expecting on the cost of sales.

Higher royalty receipts and reduced R&D expenditure helped offset some of this pressure but not all of it, despite encouraging early delivery from the manufacturing elements of our major change restructuring programme.

On royalties, we benefited from a true-up in Q1 in 2013. Without this and with the expiration of some agreements in 2014, I expect royalties in 2014 will likely be somewhat lower than last year and come in around £300 million.

R&D continue to control costs well and have benefited in 2013 from additional efficiency gains in their platform and infrastructure spend, but also in tight management of trial expense. Some is phasing and the ending of a number of large trials, but the R&D team have also made significant progress in reducing trial costs by more efficient design, use of technology and a better mix of internal and external resource. Overall, we expect to be able to maintain total R&D expense, broadly stable, at around £3.5 billion in 2014, despite substantial activity around our new products, and a significant number of Phase III starts and ongoing programmes.

COGS

Looking at the Cost of Goods, as we expected the year has seen a material drag from the unwind of the costs of volume under recoveries deferred from 2012 which are now largely done, but also restructuring benefits to 2012 that did not repeat.

However, our ongoing restructuring programmes are continuing to contribute, particularly through more effective integration of the supply chains for each of our three businesses. While this programme will take some time to ramp up, we expect to be delivering further significant annual savings to our manufacturing costs within the next couple of years. This will help offset inflation and other upward pressures, including the impact of lower recoveries from the initial volumes of our launch products. Overall, these benefits should contribute to an improving cost of goods margin over time as volumes of the pipeline products build. Remember also, that we will be paying royalties on a number of new products, including *Breo* and *Anoro*, which will be recorded in the cost of sales.

In the past few years, mix has also been a significant drag to COGS, but in 2013 we did better at managing the mix effect with stronger price realisation offsetting the negative impact of growth from our lower margin businesses. A return to the growth in the US will also help here in the future.

SG&A

Our restructuring programmes are also making an impact to the SG&A level, creating greater flexibility to reallocate and redirect selling and other resource to where we can generate the best returns. This has been particularly important as we have put in place the teams we need to launch the new products we now have approved.

We are leveraging our sales better as well, and largely offsetting our investment requirements with the benefits of our ongoing and structural restructuring initiatives. As a result, we held SG&A flat in percentage terms last year, but also broadly flat in absolute terms.

As the new launches build, we expect that the greater flexibility and restructuring benefits we are delivering will allow us to hold our growth in SG&A behind sales, creating leverage in the P&L as the pipeline contributes more meaningful revenues and delivering on our target to improve operating margins over time.

Continued delivery of restructuring benefits

So, why are we confident in that objective? Mainly because of the significance and scale of the restructuring programmes we are undertaking across our cost base.

Some of the supply chain initiatives I have already covered, but there are particular benefits from globalising our procurement and centralising our distribution, logistics and warehousing that are already contributing materially. New technology benefits are longer term, but are already being built into the production plans for our new products.

Equally significant is the continuing simplification of our operating structure. We are well advanced in rolling out new IT platforms, centralising our functional support and shared service capability as well as strengthening our procurement teams that have already delivered very significant value in standardising the many services we buy and improving the rates we pay as a result.

Almost every area of the company has been impacted by these programmes and cumulatively our major change programmes and OE programmes have delivered to date about £3 billion of annual cost savings.

On top of this, in 2012 we began a separate initiative designed to reshape and reduce our long term operating expenses and liabilities, and in 2013 we delivered a reduction of approximately £280 million in our long-term employment costs through restructuring of our post-employment medical benefits. This compares to 2012 when we delivered £395 million in savings when we restructured our pension obligations.

In 2014, we are working on additional initiatives that we expect to deliver upfront benefits of around £200 million. These have been factored into our guidance, but most likely will not arise until the fourth quarter.

Further financial efficiency gains

We made significant further financial efficiency gains in 2013, and we will continue to target this area to contribute leverage across the bottom half of the P&L. We have taken advantage of an era of low interest rates to lock in much more attractive long-term funding, but without losing flexibility, recognising that we are likely to continue to make divestments and need to be able to manage the short end of our debt maturities.

Overall, we have reduced net funding costs by over 3% since 2010, while maintaining our targeted credit rating of A1/P1, which is a central part of our funding strategy.

Over the last few years, our core tax rate has also come down, and I expect further improvements. We are currently expecting a core rate of 22% in 2014. And, we expect further benefits to come in future years as we start to benefit from the patent box.

On the share buyback, in 2013 we purchased £1.5 billion of our shares, and as we announced when we started the programme in 2011, we are looking for a sustainable position. The dividend is our first commitment, and we shall use share buybacks to manage the balance sheet as long as we see good value.

The pattern we have established is to start the year with a range and work with that during the course of the year, so again, for 2014, we are signalling that we expect to purchase between £1 and £2 billion of shares.

Continued strong cash generation

Turning to cash flow, the business remains highly cash generative and we continue to focus on improving conversion of earnings into cash, and this is a big focus for me. My philosophy on working capital in particular has been steady sustainable progress, and we have made good progress on receivables and payables; now we need the supply chains to deliver on the inventory.

We have integrated our inventory programmes and given the manufacturing businesses end-to-end ownership of inventory to increase our focus on this priority.

In 2012 we reduced working capital by £400 million. We have been able to maintain these savings and deliver an additional £46 million of savings despite renewed growth in many of our businesses and the need to start building inventory behind our new launches.

The improvements to inventory management over the next several years are likely to be more about limiting cash outflows than net cash inflows.

In monitoring our progress, you should also note that the working capital days we have reported over this year and last were distorted by the impact of the disposals and a number of intangible write-offs. Stripping these out, we still improved overall working capital by approximately ten days during 2013.

Cashflow was also impacted by continuing restructuring spend of around £500 million in 2013, and the expected higher capital investment behind launch requirements as well as volume growth in vaccines.

As expected, capex was therefore about £200 million higher than in 2012. I am expecting 2014 capex and restructuring spend to be at similar levels to 2013.

Net debt reduced to £12.6bn

Despite these investment requirements, we still generated nearly £4.8 billion of free cash flow before legal settlements, and this funded £3.7 billion of dividends and contributed to the £1.5 billion of share buybacks we completed during the year, which were also partly covered by the anticipated proceeds from the disposals that we received in December.

The proceeds from these disposals made during the year totalled £2.5 billion, and they also helped fund the bolt-on investments we made during 2013, primarily the increase in the ownership of the Group’s Indian Consumer subsidiary from 43% to 72.5%. As a result, we reduced net debt by the end of the year by £1.4 billion. This allows us to go into 2014 with a balance sheet consistent with our targeted A1/P1 rating.

Returns to shareholders

During 2013, we have returned over £5 billion to shareholders through the dividend and the ongoing buyback, and we have delivered over £23 billion to shareholders over the last five years, which really relates to the last piece of our financial architecture, that is, converting more of our earnings per share to cash that we can either reinvest or return to shareholders.

Guidance 2014

To finish, let me summarise our guidance for this year. We expect 4% to 8% growth in core EPS on a constant currency basis. This is off a base for the ongoing business adjusted for the divestments completed in 2013, to give a revised EPS number for 2013 of 108.4p.

The earnings expectation is driven off a sales growth assumption of around 2%, again on a constant currency basis and off a base for the continuing business of £25.6 billion.

We are providing a wider range this year to account for some of the uncertainties I described earlier.

And as usual, you should expect some degree of quarterly volatility as a result of portfolio transition as well as the phasing of events such as tenders, stocking patterns and delivery of structural cost benefits. The reported numbers for Q1 2014 are likely to see some material negative drag from these factors.

For the year as a whole, our guidance reflects the momentum in the business from the multiple drivers of growth we have already invested in, and an expectation for contributions from our new product launches.

With that, I will conclude and I look forward to discussing these results in more detail with you in the coming days.

Thank you.

[*Ends*]