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Trading profit – statutory results

Statutory results include merger items, integration and restructuring costs, and the disposal of subsidiaries.

	2003		2002		Growth	
	£m	%	£m	%	CER%	£%
Turnover	**21,441**	**100.0**	21,212	100.0	5	1
Cost of sales	**(4,544)**	**(21.2)**	(4,609)	(21.7)	–	(1)
Selling, general and administration	**(7,581)**	**(35.4)**	(8,041)	(37.9)	(2)	(6)
Research and development	**(2,791)**	**(13.0)**	(2,900)	(13.7)	(1)	(4)
Trading profit	**6,525**	**30.4**	5,662	26.7	21	15

Cost of sales
Cost of sales reduced as a percentage of turnover as a result of benefits arising from merger and manufacturing restructuring savings and a favourable product mix. A small pricing benefit was more than offset by an adverse exchange impact. Merger and manufacturing costs incurred of £356 million were £10 million lower than in 2002.

Selling, general and administration
Selling, general and administration (SG&A) costs declined two per cent reflecting reduced merger integration costs and operational excellence cost savings initiatives. These were partly offset by increased selling costs to support new product launches, charges relating to cost saving programmes and increased pension costs. Without the merger integration costs SG&A grew four per cent driven by selling cost increases, which accounted for a three percentage point increase. The charges relating to operational excellence and pension cost increases each individually added one percentage point, while cost savings reduced growth by one percentage point. Together these produced a reduction of 2.5 percentage points relative to 2002 for the expenses expressed as a percentage of turnover.

Research and development
R&D declined one per cent reflecting reduced merger integration costs, partly offset by increased clinical trial and in-licensing activity and the reinvestment of merger synergies. Pharmaceuticals R&D expenditure represented 14.9 per cent of pharmaceutical turnover in the year.

Trading profit
Statutory trading profit was £6,525 million with a growth of 21 per cent, stronger than turnover growth of five per cent, demonstrating an improved trading margin of 3.7 percentage points. This was principally due to lower merger integration costs, cost savings derived from merger integration, manufacturing and other initiatives partly offset by charges relating to operational excellence cost saving programmes and higher pension costs.

Profit before taxation – statutory results

The analysis and discussion below of profit before taxation relates to statutory performance.

Other operating income/(expense)	2003 £m	2002 £m
Royalties and other income	**75**	75
Other operating expense	**(436)**	(209)
	(361)	(134)
Income from equity investments and other disposals	**228**	23
	(133)	(111)

Other operating income/(expense) includes litigation costs and provisions relating to legal claims on withdrawn products, product withdrawals and anti-trust matters, equity investment carrying value adjustments arising from stock market price changes, royalty income, product disposals and equity investment sales.

Other operating expenses were £133 million in the year compared with £111 million in 2002. The year on year movement reflects higher provisions in 2003 for product liability, anti-trust and other claims, partially offset by higher 2003 proceeds from product disposals and equity investment sales.

Business disposals
The profit on disposal of businesses in 2003 of £5 million reflects the final settlements regarding the disposal of Healthcare Services businesses in 1999.

Share of profits/(losses) of joint ventures and associated undertakings
The share of profits of associates arises principally from the Group’s holding in Quest Diagnostics, Inc.

Net interest payable	2003 £m	2002 £m
Interest payable	**(214)**	(206)
Investment income	**61**	73
	(153)	(133)
Share of interest payable of associate	**(8)**	(8)
	(161)	(141)

Net interest payable increased compared with 2002 largely as a result of the unwinding of the discounts on provisions and long-term receivables.

Profit on ordinary activities before taxation – statutory results
Taking account of net other operating income/(expenses), the contribution from associates, business disposals and net interest payable, statutory profit before tax was £6,329 million compared with £5,506 million in 2002, an increase of 21 per cent.

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Trading profit – business performance

To illustrate GlaxoSmithKline business performance in 2003, the analysis below of trading profit and the subsequent discussion excludes merger items, integration and restructuring costs and the disposal of businesses. Management believes that exclusion of these items provides a better reflection of the way in which the business is managed. Accordingly this information is provided as a supplement to that contained in the consolidated statement of profit and loss on pages 88 and 89 prepared in accordance with UK GAAP.

	2003		2002		Growth	
	£m	%	£m	%	CER%	£%
Turnover	**21,441**	100.0	21,212	100.0	5	1
Cost of sales	**(4,188)**	(19.5)	(4,243)	(20.0)	–	(1)
Selling, general and administration	**(7,563)**	(35.3)	(7,543)	(35.5)	4	–
Research and development	**(2,770)**	(12.9)	(2,732)	(12.9)	4	1
Trading profit	**6,920**	32.3	6,694	31.6	9	3

Cost of sales
Cost of sales reduced as a percentage of turnover as a result of benefits arising from merger, manufacturing restructuring savings, and a favourable product mix. A small pricing benefit was more than offset by an adverse exchange impact.

Selling, general and administration
Selling, general and administration (SG&A) costs grew four per cent reflecting increased selling costs to support new product launches, charges relating to operational excellence cost saving programmes and increased pension costs, partly offset by cost saving initiatives. These cost saving initiatives were relatively small restructuring activities in 2002 and 2003. It is estimated that without the operational excellence charges SG&A would have grown three per cent, driven principally by selling cost increases. Pension cost increases added one percentage point, but these were offset by cost saving initiatives. Together these produced a reduction of 0.2 percentage points expressed as a percentage of turnover.

Research and development
Research and development (R&D) increased four per cent reflecting increased clinical trial and in-licensing activity and the reinvestment of merger synergies. Pharmaceuticals R&D expenditure represented 14.8 per cent of pharmaceutical turnover in the year.

Trading profit
Business performance trading profit was £6,920 million with a growth of nine per cent, stronger than turnover growth of five per cent, demonstrating an improved trading margin of 0.7 points to 32.3 per cent compared with 2002. This was principally due to cost savings derived from merger integration, manufacturing and other initiatives, partly offset by charges relating to operational excellence cost saving programmes and higher pension costs.

The focus of operational excellence is on value creation and the elimination of waste and bureaucracy. This programme has become an integral part of the way the business is managed and so any charges are booked to business performance.

Profit before taxation – business performance

The analysis and discussion below of profit before taxation relates to business performance.

Other operating income/(expense)	2003 £m	2002 £m
Royalties and other income	**75**	75
Other operating expense	**(436)**	(209)
	(361)	(134)
Income from equity investments and other disposals	**228**	23
	(133)	(111)

Other operating income/(expense) includes litigation costs and provisions relating to legal claims on withdrawn products, product withdrawals and anti-trust matters, equity investment carrying value adjustments arising from stock market price changes, royalty income, product disposals and equity investment sales.

Other operating expenses were £133 million in the year compared with £111 million in 2002. The year-on-year movement reflects higher provisions in 2003 for product liability, anti-trust and other claims, partially offset by higher 2003 proceeds from product disposals and equity investment sales.

Share of profits/(losses) of joint ventures and associated undertakings
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Interest payable	**(214)**	(206)
Investment income	**61**	73
	(153)	(133)
Share of interest payable of associate	**(8)**	(8)
	(161)	(141)

Net interest payable increased compared with 2002 largely as a result of the unwinding of the discounts on provisions and long-term receivables.

Profit on ordinary activities before taxation – business performance
Taking account of net other operating income/(expense), the contribution from associates and net interest payable, business performance profit before tax was £6,719 million, compared with £6,517 million in 2002, an increase of eight per cent.

Merger items, restructuring costs and disposal of businesses

Merger and manufacturing restructuring
GlaxoSmithKline has made good progress with its merger and manufacturing restructuring plans. The merger programmes are substantially complete at the end of 2003. Combined these programmes have now produced annual savings which exceeded the published target of £1.8 billion.

Costs of £369 million were incurred in the year in respect of merger and manufacturing restructuring. After tax relief of £91 million, the net charge was £278 million. The costs in 2003 include severance, asset write-downs, professional fees and site closure.