10-Q 1 tenq.txt UNITED STATES SECURITIES AND EXCHANGE COMMISSION Washington, D.C. 20549 FORM 10-Q (X) Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended September 26, 2004 or ( ) Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the for the transition period from to Commission file number 1-3215 JOHNSON & JOHNSON (Exact name of registrant as specified in its charter) NEW JERSEY 22-1024240 (State or other jurisdiction of (I.R.S.Employer Incorporation or organization) Identification No.) One Johnson & Johnson Plaza New Brunswick, New Jersey 08933 (Address of principal executive offices) Registrant's telephone number, including area code (732) 524-0400 Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes (X) No Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes (X) No Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. On October 24, 2004, 2,967,726,203 shares of Common Stock, $1.00 par value, were outstanding. 1 JOHNSON & JOHNSON AND SUBSIDIARIES TABLE OF CONTENTS Part I - Financial Information Page No. Item 1. Financial Statements (unaudited) Consolidated Balance Sheets - September 26, 2004 and December 28, 2003 3 Consolidated Statements of Earnings for the Fiscal Third Quarters Ended September 26, 2004 and September 28, 2003 6 Consolidated Statements of Earnings for the Fiscal Nine Months Ended September 26, 2004 and September 28, 2003 7 Consolidated Statements of Cash Flows for the Fiscal Nine Months Ended September 26, 2004 and September 28, 2003 8 Notes to Consolidated Financial Statements 10 Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations 31 Item 3. Quantitative and Qualitative Disclosures About Market Risk 42 Item 4. Controls and Procedures 42 Part II - Other Information Item 1. Legal Proceedings 42 Item 5. Exhibits and Reports on Form 8-K 42 Signatures 44 2 Part I - FINANCIAL INFORMATION Item 1 - Financial Statements JOHNSON & JOHNSON AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS (Unaudited; Dollars in Millions) ASSETS September 26, December 28, 2004 2003 Current Assets: Cash and cash equivalents $ 7,348 5,377 Marketable securities 5,746 4,146 Accounts receivable, trade, less allowances for doubtful accounts $204(2003, $192) 6,939 6,574 Inventories (Note 4) 3,669 3,588 Deferred taxes on income 1,662 1,526 Prepaid expenses and other receivables 1,452 1,784 Total current assets 26,816 22,995 Marketable securities, non-current 62 84 Property, plant and equipment, at cost 17,632 17,052 Less accumulated depreciation 8,037 7,206 Property, plant and equipment, net 9,595 9,846 Intangible assets (Note 5) 14,764 14,168 Less accumulated amortization 3,036 2,629 Intangible assets, net 11,728 11,539 Deferred taxes on income 955 692 Other assets 2,933 3,107 Total assets $52,089 48,263 See Notes to Consolidated Financial Statements 3 JOHNSON & JOHNSON AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS (Unaudited; Dollars in Millions) LIABILITIES AND SHAREHOLDERS' EQUITY September 26, December 28, 2004 2003 Current Liabilities: Loans and notes payable $ 454 1,139 Accounts payable 3,646 4,966 Accrued liabilities 2,951 2,639 Accrued rebates, returns and promotions 2,855 2,308 Accrued salaries, wages and commissions 995 1,452 Accrued Taxes on income 1,428 944 Total current liabilities 12,329 13,448 Long-term debt 2,961 2,955 Deferred tax liability 791 780 Employee related obligations 2,438 2,262 Other liabilities 2,057 1,949 Shareholders' equity: Preferred stock - without par value (authorized and unissued 2,000,000 shares) - - Common stock - par value $1.00 per share (authorized 4,320,000,000 shares; issued 3,119,842,000 shares) 3,120 3,120 Note receivable from employee stock ownership plan (11) (18) Accumulated other comprehensive income (Note 8) (491) (590) Retained earnings 35,022 30,503 4 Less common stock held in treasury, at cost (151,421,000 & 151,869,000 shares) 6,127 6,146 Total shareholders' equity 31,513 26,869 Total liabilities and shareholders' equity $52,089 48,263 See Notes to Consolidated Financial Statements 5 JOHNSON & JOHNSON AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF EARNINGS (Unaudited; dollars & shares in millions except per share figures) Fiscal Third Quarter Ended Sept. 26, Percent Sept. 28, Percent 2004 to Sales 2003 to Sales Sales to customers (Note 6) $11,553 100.0 10,455 100.0 Cost of products sold 3,187 27.6 2,980 28.5 Gross Profit 8,366 72.4 7,475 71.5 Selling, marketing and administrative expenses 3,854 33.3 3,428 32.8 Research expense 1,198 10.4 1,177 11.3 Purchased in-process research and development 18 .2 - - Interest income (49) (.4) (63) (.6) Interest expense, net of portion capitalized 30 .2 75 .7 Other (income)expense, net 41 .4 (91) (.9) Earnings before provision for taxes on income 3,274 28.3 2,949 28.2 Provision for taxes on income (Note 3) 933 8.0 877 8.4 NET EARNINGS $2,341 20.3 2,072 19.8 NET EARNINGS PER SHARE (Note 7) Basic $ .79 .70 Diluted $ .78 .69 CASH DIVIDENDS PER SHARE $ .285 .24 AVG. SHARES OUTSTANDING Basic 2,968.1 2,968.0 Diluted 3,009.0 3,008.3 See Notes to Consolidated Financial Statements 6 JOHNSON & JOHNSON AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF EARNINGS (Unaudited; dollars & shares in millions except per share figures) Fiscal Nine Months Ended Sept. 26, Percent Sept. 28, Percent 2004 to Sales 2003 to Sales Sales to customers (Note 6) $34,596 100.0 30,608 100.0 Cost of products sold 9,716 28.1 8,668 28.3 Gross Profit 24,880 71.9 21,940 71.7 Selling, marketing and administrative expenses 11,205 32.4 10,077 32.9 Research expense 3,476 10.0 3,195 10.4 Purchased in-process research and development 18 .1 918 3.0 Interest income (123) (.4) (145) (.5) Interest expense, net of portion capitalized 127 .4 164 .6 Other (income)expense, net (36) (.1) (203) (.6) Earnings before provision for taxes on income 10,213 29.5 7,934 25.9 Provision for taxes on income (Note 3) 2,921 8.4 2,582 8.4 NET EARNINGS $7,292 21.1 5,352 17.5 NET EARNINGS PER SHARE (Note 7) Basic $ 2.46 1.80 Diluted $ 2.43 1.78 CASH DIVIDENDS PER SHARE $ .81 .685 AVG. SHARES OUTSTANDING Basic 2,968.1 2,968.0 Diluted 3,004.4 3,012.0 See Notes to Consolidated Financial Statements 7 JOHNSON & JOHNSON AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited; Dollars in Millions) Fiscal Nine Months Ended Sept. 26, Sept. 28, 2004 2003 CASH FLOWS FROM OPERATIONS Net earnings $ 7,292 5,352 Adj. to reconcile net earnings to cash flows: Depreciation and amortization of property and intangibles 1,506 1,347 Purchased in-process research and development 18 918 Increase in deferred taxes (424) (508) Accounts receivable provisions 68 (31) Changes in assets and liabilities, net of effects from acquisition of businesses: Increase in accounts receivable (452) (679) Increase in inventories (91) (231) (Decrease) increase in accounts payable and accrued liabilities (787) 628 Decrease (increase) in other current and non-current assets 545 (505) Increase in other current and non-current liabilities 995 752 NET CASH FLOWS FROM OPERATING ACTIVITIES 8,670 7,043 CASH FLOWS FROM INVESTING ACTIVITIES Additions to property, plant and equipment (1,142) (1,472) Proceeds from the disposal of assets 235 334 Acquisition of businesses, net of cash acquired (330) (2,781) Purchases of investments (9,121) (5,064) Sales of investments 7,508 4,673 Other (91) (104) NET CASH USED BY INVESTING ACTIVITIES (2,941) (4,414) CASH FLOWS FROM FINANCING ACTIVITIES Dividends to shareholders (2,404) (2,033) Repurchase of common stock (985) (941) Proceeds from short-term debt 313 1,633 Retirement of short-term debt (1,114) (1,621) Proceeds from long-term debt 16 1,013 Retirement of long-term debt (1) (108) Proceeds from the exercise of stock options 434 240 NET CASH USED BY FINANCING ACTIVITIES (3,741) (1,817) 8

EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS (17) 144 INCREASE IN CASH AND CASH EQUIVALENTS 1,971 956 CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD 5,377 2,894 CASH AND CASH EQUIVALENTS, END OF PERIOD $ 7,348 3,850 ACQUISITION OF BUSINESSES Fair value of assets acquired 369 3,096 Fair value of liabilities assumed (39) (315) Net cash paid for acquisitions $ 330 2,781 See Notes to Consolidated Financial Statements 9 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS NOTE 1 - The accompanying unaudited interim financial statements and related notes should be read in conjunction with the Consolidated Financial Statements of Johnson & Johnson and Subsidiaries (the "Company") and related notes as contained in the Annual Report on Form 10-K for the fiscal year ended December 28, 2003. The unaudited interim financial statements include all adjustments (consisting only of normal recurring adjustments) and accruals necessary in the judgment of management for a fair presentation of such statements. NOTE 2 - FINANCIAL INSTRUMENTS The Company follows the provisions of SFAS 133 requiring that all derivative instruments be recorded on the balance sheet at fair value. As of September 26, 2004, the balance of deferred net losses on derivatives included in accumulated other comprehensive income was $76 million after-tax. For additional information, see Note 8. The Company expects that substantially all of this amount will be reclassified into earnings over the next 12 months as a result of transactions that are expected to occur over that period. The amount ultimately realized in earnings will differ as foreign exchange rates change. Realized gains and losses are ultimately determined by actual exchange rates at maturity of the derivative. Transactions with third parties will cause the amount in accumulated other comprehensive income to affect net earnings. The maximum length of time over which the Company is hedging is 18 months. For the first fiscal nine months ended September 26, 2004, the net impact of the hedges' ineffectiveness to the Company's financial statements was insignificant. For the first fiscal nine months ended September 26, 2004, the Company has recorded a net loss of $1 million after tax in the "other (income) expense, net" category of the consolidated statement of earnings, representing the impact of discontinuance of cash flow hedges because it is probable that the originally forecasted transactions will not occur by the end of the originally specified time period. NOTE 3 - INCOME TAXES The worldwide effective income tax rates for the first fiscal nine months of 2004 and 2003 were 28.6% and 32.5% respectively. The decrease in the effective tax rate for the first fiscal nine months of 2004 compared with the same period a year ago was due to acquisition-related In- process Research and Development (IPR&D) charges in 2003 that were non-deductible for tax purposes. The 2003 tax rate excluding the effect of IPR&D was 29.2%. The decrease was also due to the increase in taxable income in lower tax jurisdictions relative to taxable income in higher tax jurisdictions. 10 NOTE 4 - INVENTORIES (Dollars in Millions) Sept. 26, 2004 December 28, 2003 Raw materials and supplies $ 1,087 966 Goods in process 1,048 981 Finished goods 1,534 1,641 $ 3,669 3,588 NOTE 5 - INTANGIBLE ASSETS Intangible assets that have definite useful lives are amortized over their useful lives. Goodwill and non- amortizable intangible assets are assessed annually for impairment. The impairment assessment was completed in the fiscal fourth quarter of 2003 and no impairment was determined. In the absence of a triggering event during the year, future impairment tests will be performed in the fiscal fourth quarter, annually. (Dollars in Millions) Sept. 26, 2004 December 28, 2003 Goodwill $ 6,297 6,085 Less accumulated amortization 719 695 Goodwill - net 5,578 5,390 Trademarks (non-amortizable) 1,130 1,098 Less accumulated amortization 136 136 Trademarks (non-amortizable)- net 994 962 Patents and trademarks 3,997 3,798 Less accumulated amortization 1,027 818 Patents and trademarks - net 2,970 2,980 Other amortizable intangibles 3,340 3,187 Less accumulated amortization 1,154 980 Other intangibles - net 2,186 2,207 Total intangible assets 14,764 14,168 Less accumulated amortization 3,036 2,629 Total intangibles - net $11,728 11,539 11 Goodwill as of September 26, 2004 as allocated by segment of business is as follows: (Dollars in Millions) Med. Dev Consumer Pharm & Diag Total Goodwill, net of accumulated amortization at December 28, 2003 $882 781 3,727 5,390 Acquisitions 176 21 6 203 Translation & other 5 (3) (17) (15) Goodwill as of September 26, 2004 $1,063 799 3,716 5,578 The weighted average amortization periods for patents and trademarks and other intangible assets were 16 years and 18 years, respectively. The amortization expense of amortizable intangible assets for the first fiscal nine months ended September 26, 2004 was $382 million before tax and the estimated amortization expense for each of the five succeeding years approximates $500 million before tax. NOTE 6 - SEGMENTS OF BUSINESS AND GEOGRAPHIC AREAS (Dollars in Millions) SALES BY SEGMENT OF BUSINESS Fiscal Third Quarter Percent 2004 2003 Change Consumer U.S. $ 1,023 984 4.0 International 1,001 857 16.8 2,024 1,841 9.9% Pharmaceutical U.S. $ 3,694 3,285 12.5 International 1,791 1,550 15.5 5,485 4,835 13.4% Med Devices and Diagnostics U.S. $ 2,073 2,145 (3.4) International 1,971 1,634 20.6 4,044 3,779 7.0% U.S. $ 6,790 6,414 5.9 International 4,763 4,041 17.9 Worldwide $ 11,553 10,455 10.5% 12 Fiscal Nine Months Percent 2004 2003 Change Consumer U.S. $ 3,090 2,915 6.0 International 2,981 2,536 17.5 6,071 5,451 11.4% Pharmaceutical U.S. $ 10,980 9,825 11.8 International 5,308 4,559 16.4 16,288 14,384 13.2% Med Devices and Diagnostics U.S. $ 6,306 5,797 8.8 International 5,931 4,976 19.2 12,237 10,773 13.6% U.S. $ 20,376 18,537 9.9 International 14,220 12,071 17.8 Worldwide $ 34,596 30,608 13.0% OPERATING PROFIT BY SEGMENT OF BUSINESS Fiscal Third Quarter Percent 2004 2003 Change Consumer $ 358 364 (1.6) Pharmaceutical 1,922 1,751 9.8 Med. Dev. & Diag.(1) 1,052 931 13.0 Segments total 3,332 3,046 9.4 Expenses not allocated to segments (58) (97) Worldwide total $ 3,274 2,949 11.0% Fiscal Nine Months Percent 2004 2003 Change Consumer $ 1,187 1,148 3.4 Pharmaceutical(2) 6,117 4,702 30.1 Med. Dev. & Diag.(3) 3,179 2,332 36.3 Segments total 10,483 8,182 28.1 Expenses not allocated to segments (270) (248) Worldwide total $ 10,213 7,934 28.7% 13 (1)Includes $18 million of In-process Research and Development (IPR&D) charges related to an acquisition in the fiscal third quarter of 2004. (2)Includes $737 million of IPR&D charges related to acquisitions for the first fiscal nine months of 2003. (3)Includes $18 million and $181 million of IPR&D charges related to acquisitions for the first fiscal nine months of 2004 and 2003, respectively. SALES BY GEOGRAPHIC AREA Fiscal Third Quarter Percent 2004 2003 Change U.S. $ 6,790 6,414 5.9 Europe 2,638 2,241 17.7 Western Hemisphere, excluding U.S. 639 576 10.9 Asia-Pacific, Africa 1,486 1,224 21.4 Total $ 11,553 10,455 10.5% Fiscal Nine Months Percent 2004 2003 Change U.S. $ 20,376 18,537 9.9 Europe 8,124 6,909 17.6 Western Hemisphere, excluding U.S. 1,858 1,603 15.9 Asia-Pacific, Africa 4,238 3,559 19.1 Total $ 34,596 30,608 13.0% 14 NOTE 7 - EARNINGS PER SHARE The following is a reconciliation of basic net earnings per share to diluted net earnings per share for the fiscal third quarters ended September 26, 2004 and September 28, 2003. (Shares in Millions) Fiscal Third Quarter Ended Sept. 26, Sept. 28, 2004 2003 Basic net earnings per share $ .79 .70 Average shares outstanding - basic 2,968.1 2,968.0 Potential shares exercisable under stock option plans 194.9 95.8 Less: shares which could be repurchased under treasury stock method (168.6) (70.4) Convertible debt shares 14.6 14.9 Adjusted average shares outstanding - diluted 3,009.0 3,008.3 Diluted earnings per share $ .78 .69 The diluted earnings per share calculation included the dilutive effect of convertible debt that was offset by the related decrease in interest expense of $3 million each for the fiscal third quarters ended September 26, 2004 and September 28, 2003, respectively. The diluted earnings per share excluded 43 million and 125 million shares related to options for the fiscal third quarters ended September 26, 2004 and September 28, 2003, respectively, as the exercise

price per share of these options was greater than the average market value, which would have resulted in an anti-dilutive effect on diluted earnings per share. The following is a reconciliation of basic net earnings per share to diluted net earnings per share for the fiscal nine months ended September 26, 2004 and September 28, 2003. (Shares in Millions) Fiscal Nine Months Ended Sept. 26, Sept. 28, 2004 2003 Basic net earnings per share $ 2.46 1.80 Average shares outstanding - basic 2,968.1 2,968.0 Potential shares exercisable under stock option plans 193.4 172.9 Less: shares which could be repurchased under treasury stock method (171.7) (143.8) Convertible debt shares 14.6 14.9 Adjusted average shares outstanding - diluted 3,004.4 3,012.0 Diluted earnings per share $ 2.43 1.78 The diluted earnings per share calculation included the dilutive effect of convertible debt that was offset by the related 15 decrease in interest expense of $11 million each for the first fiscal nine months ended September 26, 2004 and September 28, 2003, respectively. The diluted earnings per share excluded 44 million and 48 million shares related to options for the first fiscal nine months ended September 26, 2004 and September 28, 2003, respectively, as the exercise price per share of these options was greater than the average market value, which would have resulted in an anti-dilutive effect on diluted earnings per share. NOTE 8 - ACCUMULATED OTHER COMPREHENSIVE INCOME The total comprehensive income for the first fiscal nine months ended September 26, 2004 was $7.4 billion, compared with $5.5 billion for the same period a year ago. Total comprehensive income included net earnings, net unrealized currency gains and losses on translation, net unrealized gains and losses on available for sale securities and net gains and losses on derivative instruments qualifying and designated as cash flow hedges. The following table sets forth the components of accumulated other comprehensive income. Total Unrld Gains/ Accum For. Gains/ Pens (Losses) Other Cur. (Losses) Liab on Deriv Comp Trans. on Sec Adj. & Hedg Inc/ (Loss) December 28, 2003 $ (373) 27 (64) (180) (590) 2004 nine months changes: Net change associated with current period hedging transactions - - - 211 Net amount reclassed to net earnings - - - (107)* Net nine months changes (46) 41 - 104 99 September 26, 2004 $ (419) 68 (64) (76) (491) Note: All amounts, other than foreign currency translation, are net of tax. Foreign currency translation adjustments are not currently adjusted for income taxes, as they relate to permanent investments in non-US subsidiaries. *Primarily offset in net earnings by changes in value of the underlying transactions. NOTE 9 - MERGERS, ACQUISITIONS AND DIVESTITURES There were no acquisitions in the fiscal first quarter of 2004. DePuy's Castings business was divested in the fiscal first quarter of 2004 and did not have a material effect on the Company's results of operations, cash flows or financial position. On March 30, 2004, Johnson & Johnson acquired Merck's 50% interest in the Johnson & Johnson-Merck Consumer Pharmaceuticals Co. European non-prescription pharmaceutical joint venture for a 16 net purchase price of $230 million. This resulted in Johnson & Johnson acquiring all the infrastructure and brand assets currently managed by the European JV including brands contributed by Merck (DOLORMIN (r), PEPCID (r), FRENADOL (r) and DACRYYO(r)) and those acquired by both companies (through the acquisition of Woelm Pharma and Laboratoires Martin). On May 18, 2004, Johnson & Johnson completed the acquisition of Egea Biosciences, Inc. through the exercise of the option to acquire the remaining outstanding stock not owned by Johnson & Johnson. Egea Biosciences has developed a proprietary technology platform called Gene Writer, that allows for the rapid and highly accurate synthesis of DNA sequences, gene assembly, and construction of large synthetic gene libraries. On June 18, 2004, Johnson & Johnson acquired the stock of Artemis Medical, Inc. Artemis was a privately held company founded in 1999. Its products include ultrasound and x-ray visible biopsy site breast markers as well as hybrid markers. On June 28, 2004, Johnson & Johnson acquired the U.S. commercial rights to certain patents and know-how in the field of sedation and analgesia from Scott Lab, Inc. The Company incurred a charge for IPR&D of approximately $18 million before tax and $12 million after tax. The total net cash paid for acquisitions in the first fiscal nine months of 2004 was $330 million. On January 29, 2003, Johnson & Johnson acquired certain assets of Orquest, Inc., a privately held biotechnology company focused on developing biologically based implants for orthopaedic and spine surgery. Orquest's principal product, HEALOS Bone Graft Substitute, is designed to reduce the time and pain associated with standard bone graft harvesting and represents a therapeutic advance for patients requiring bone graft material for spine fusion. The Company incurred a charge for IPR&D of approximately $11 million before tax and $8 million after tax. On February 10, 2003, Johnson & Johnson acquired OraPharma, Inc., a specialty pharmaceutical company focused on the development and commercialization of unique therapeutics. Orapharma's initial product, ARESTIN, is the first locally administered, time-released antibiotic encapsulated in microspheres that control the germs that can cause periodontal disease. The transaction was valued at approximately $85 million, net of cash. On March 28, 2003, Johnson & Johnson acquired 3-Dimensional Pharmaceuticals, Inc., a company with a technology platform focused on the discovery and development of potential new drugs in early stage development for the treatment of cardiovascular disorders, oncology and inflammation. The transaction was valued at approximately $88 million, net of cash. The Company incurred a before and after tax charge for IPR&D of approximately $7 million. On April 17, 2003, Johnson & Johnson acquired the CORTAID(r) brand business, the #3 brand in the anti-itch treatment segment of the first aid category. The transaction was valued at approximately $37 million. 17 On April 29, 2003, Johnson & Johnson acquired Scios Inc., a biopharmaceutical company with a marketed product for cardiovascular disease and research projects focused on auto- immune diseases. Scios was acquired to strengthen the Company's business in key therapeutic areas and technology platforms. Scios' product NATRECOR(r) is a novel agent approved for congestive heart failure and has several significant advantages over existing therapies. The transaction was valued at approximately $2.4 billion, net of cash, and the Company incurred a charge for IPR&D of $730 million before and after tax. The purchase price was allocated to the tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair values at the acquisition date. The excess of the purchase price over the fair values of assets and liabilities acquired was approximately $440 million and was allocated to goodwill. Goodwill associated with this deal will not be deductible for tax purposes. On May 9, 2003, Johnson & Johnson acquired Inscope, an intraluminal multiple clip applier technology. This transaction was valued at $26 million. On June 3, 2003, Johnson & Johnson acquired Link Spine Group, Inc., a privately owned corporation that has provided the Company with exclusive worldwide rights to the SB CHARITE (tm) Artificial Disc for the treatment of spine disorders. Under the terms of the agreement, the Company paid a $325 million upfront payment with further contingent payments due upon achievement of regulatory and other milestones, and the Company incurred a charge for IPR&D of $170 million before and after tax. The purchase price was allocated to the tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair values at the acquisition date. The excess of the purchase price over the fair values of assets and liabilities acquired was approximately $84 million and was allocated to goodwill. Goodwill associated with this deal will not be deductible for tax purposes. The supplemental pro forma information for the current interim period and the preceeding year per SFAS No. 141, "Business Combinations" and SFAS No. 142, "Goodwill and Other Intangible Assets" are not provided as the impact of these aforementioned acquisitions did not have a material effect on the Company's results of operations, cash flows or financial position. NOTE 10 - PRO FORMA STOCK BASED COMPENSATION At September 26, 2004, the Company had 21 stock-based employee compensation plans. The Company accounted for those plans under the recognition and measurement principles of

Accounting Principle Board Opinion No. 25 "Accounting for Stock Issued to Employees" and its related Interpretations. Compensation costs were not recorded in net income for stock options, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. As required by SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure-an amendment of FASB Statement No. 123," the following table shows the estimated effect on net income and earnings per share if the Company had applied the fair value recognition provision of SFAS No. 123, "Accounting for Stock-Based Compensation," to stock-based employee compensation. 18 (Dollars in Millions Except Per Share Data) Fiscal Third Quarter Ended Sept. 26, 2004 Sept. 28, 2003 Net income, as reported $ 2,341 2,072 Less: Compensation expense(1) 88 87 Pro forma $ 2,253 1,985 Earnings per share: Basic - as reported $.79 $.70 - pro forma .76 .67 Diluted - as reported $.78 $.69 - pro forma .75 .66 (1) Determined under fair value based method for all awards, net of tax. (Dollars in Millions Except Per Share Data) Fiscal Nine Months Ended Sept. 26, 2004 Sept. 28, 2003 Net income, as reported $ 7,292 5,352 Less: Compensation expense(1) 254 262 Pro forma $ 7,038 5,090 Earnings per share: Basic - as reported $2.46 $1.80 - pro forma 2.37 1.71 Diluted - as reported $2.43 $1.78 - pro forma 2.36 1.70 (1) Determined under fair value based method for all awards, net of tax. 19 NOTE 11 - PENSIONS AND OTHER POSTRETIREMENT BENEFITS Components of Net Periodic Benefit Costs Net periodic benefit costs for the Company's defined benefit retirement plans and other benefit plans for the fiscal third quarter of 2004 and 2003 include the following components: (Dollars in Millions) Retirement Plans Other Benefit Plans Fiscal Third Quarter ended Sept. 26, Sept. 28, Sept. 26, Sept. 28, 2004 2003 2004 2003 Service cost $ 107 81 13 7 Interest cost 114 97 26 18 Expected return on plan assets (129) (123) (1) - Amortization of prior service cost 4 5 (1) - Amortization of net transition asset (1) (1) - - Recognized actuarial losses (gains) 52 16 10 - Curtailments and settlements - - - - Net periodic benefit cost $ 147 75 47 25 Net periodic benefit costs for the Company's defined benefit retirement plans and other benefit plans for the first fiscal nine months of 2004 and 2003 include the following components: (Dollars in Millions) Retirement Plans Other Benefit Plans Fiscal Nine Months ended Sept. 26, Sept. 28, Sept. 26, Sept. 28, 2004 2003 2004 2003 Service cost $ 319 244 37 21 Interest cost 339 293 77 53 Expected return on plan assets (387) (371) (2) (2) Amortization of prior service cost 11 14 (2) (2) Amortization of net transition asset (2) (3) - - Recognized actuarial losses (gains) 155 49 32 2 Curtailments and settlements - 1 - - Net periodic benefit cost $ 435 227 142 72 Company Contributions As of September 26, 2004, the Company has contributed $155 million to its U.S. retirement plans during 2004. The Company has no statutory requirements to further fund U.S. retirement plans in 2004 but continually evaluates the need for future funding. 20 NOTE 12 - LEGAL PROCEEDINGS The Company is involved in numerous product liability cases in the United States, many of which concern adverse reactions to drugs and medical devices. The damages claimed are substantial, and while the Company is confident of the adequacy of the warnings and instructions for use which accompany such products, it is not feasible to predict the ultimate outcome of litigation. However, the Company believes that if any liability results from such cases, it will be substantially covered by existing amounts accrued in the Company's balance sheet under its self-insurance program and by third party product liability insurance. One group of cases against the Company concerns the Janssen Pharmaceutica Inc. product PROPULSID, which was withdrawn from general sale and restricted to limited use in 2000. In the wake of publicity about those events, numerous lawsuits have been filed against Janssen, which is a wholly owned subsidiary of the Company, and the Company regarding PROPULSID, in state and federal courts across the country. There are approximately 429 such cases currently pending, including the claims of approximately 5,900 plaintiffs. In the active cases, 415 individuals are alleged to have died from the use of PROPULSID. These actions seek substantial compensatory and punitive damages and accuse Janssen and the Company of inadequately testing for and warning about the drug's side effects, of promoting it for off-label use and of over promotion. In addition, Janssen and the Company have entered into agreements (tolling agreements) with various plaintiffs' counsel halting the running of the statutes of limitations with respect to the potential claims of a significant number of individuals while those attorneys evaluate whether or not to sue Janssen and the Company on their behalf. In September 2001, the first ten plaintiffs in the Rankin case, which comprises the claims of 155 PROPULSID plaintiffs, went to trial in state court in Claiborne County, Mississippi. The jury returned compensatory damage verdicts for each plaintiff in the amount of $10 million, for a total of $100 million. The trial judge thereafter dismissed the claims of punitive damages. On March 4, 2002, the trial judge reduced these verdicts to a total of $48 million, and denied the motions of Janssen and the Company for a new trial. On May 13, 2004, the Supreme Court of Mississippi reversed the verdicts against Janssen and the Company, and remanded the case to the trial court. The Supreme Court found the joint trial of multiple plaintiffs' cases against Janssen was prejudicial and directed the trial court to return the cases of the individual plaintiffs for separate trials to their home counties. A motion for rehearing was denied on August 5, 2004. In April 2002, a state court judge in New Jersey denied plaintiffs' motion to certify a national class of PROPULSID users for purposes of medical monitoring and refund of the costs of purchasing PROPULSID. An effort to appeal that ruling has been denied. In June 2002, the federal judge presiding over the 21 PROPULSID Multi-District Litigation in New Orleans, Louisiana similarly denied plaintiffs' motion there to certify a national class of PROPULSID users. Plaintiffs in the Multi- District Litigation have said they are preserving their right to appeal that ruling, and other complaints filed against Janssen and the Company include class action allegations, which could be the basis for future attempts to have classes certified. On February 5, 2004, Janssen announced that it had reached an agreement in principle with the Plaintiffs Steering Committee (PSC), of the PROPULSID Federal Multi- District Litigation (MDL), to resolve federal lawsuits related to PROPULSID. There are approximately 4,000 individuals included in the Federal MDL of whom approximately 300 are alleged to have died from use of the drug. The agreement becomes effective once 85 percent of the death claims, and 75 percent of the remainder, agree to the terms of the settlement. In addition, 12,000 individuals who have not filed lawsuits, but whose claims are the subject of tolling agreements suspending the running of the statutes of limitations against those claims, must also agree to participate in the settlement before it will become effective. Those agreeing to participate in the settlement will submit medical records to an independent panel of physicians who will determine whether the claimed injuries were caused by PROPULSID and otherwise meet the standards for compensation. If those standards are met, a court-appointed special master will determine compensatory damages. If the agreement becomes effective, Janssen will pay as compensation a minimum of $69.5 million and a maximum of $90 million, depending upon the number of plaintiffs who enroll in the program. Janssen will also establish an administrative fund not to exceed $15 million, and will pay legal fees to the PSC up to $22.5 million, subject to court approval. With respect to all the various PROPULSID actions against them, Janssen and the Company dispute the claims in those lawsuits and are vigorously defending against them except where, in their judgment, settlement is appropriate. Janssen and the Company believe they have adequate self- insurance accruals and third party product liability insurance with respect to these cases. In communications to the Company, the excess insurance carriers have raised certain defenses to their liability under the policies and to date have declined to reimburse Janssen and the Company for PROPULSID-related costs despite demand for payment. However, in the opinion of the Company, those defenses are pro forma and lack substance and the carriers will

honor their obligations under the policies either voluntarily or after litigation. In March 2004, the Company commenced arbitration against Allianz Underwriters Insurance Company, which issued the first layer of applicable excess insurance coverage, to obtain reimbursement of PROPULSID-related costs. The Company's Ethicon, Inc. subsidiary has over the last several years had a number of claims and lawsuits filed against it relating to VICRYL sutures. The actions allege that the sterility of VICRYL sutures was compromised by inadequacies in Ethicon's 22 systems and controls, causing patients who were exposed to these sutures to incur infections which would not otherwise have occurred. Ethicon on several occasions recalled batches of VICRYL sutures in light of questions raised about sterility but does not believe any contamination of suture products in fact occurred. In November 2003, a trial judge in West Virginia certified for class treatment all West Virginia residents who had VICRYL sutures implanted during Class I or II surgeries from May 1, 1994 to December 31, 1997. The certification is subject to later challenge following the conclusion of discovery. A previous trial date has been adjourned and not reset. Ethicon has been and intends to continue vigorously defending against the claims. In September 2004, plaintiffs in an employment discrimination litigation initiated against the Company in 2001 moved to certify a class of all African American and Hispanic salaried employees of the Company and its affiliates in the United States, who were employed at any time from November 1997 to the present. Plaintiffs seek monetary damages for the period 1997 through the present (including punitive damages) and equitable relief. The Company is expected to file its response to plaintiffs' class certification motion in the first quarter of 2005. A decision by the district court is not expected before late 2005. The Company disputes the allegations in the lawsuit and is vigorously defending against them. Affirmative Stent Patent Litigation In patent infringement actions tried in Delaware Federal Court in late 2000, Cordis Corporation, a subsidiary of Johnson & Johnson, obtained verdicts of infringement and patent validity, and damage awards, against Boston Scientific Corporation and Medtronic AVE, Inc., based on a number of Cordis vascular stent patents. On December 15, 2000, the jury in the damage action against Boston Scientific returned a verdict of $324 million and on December 21, 2000, the jury in the Medtronic AVE action returned a verdict of $271 million. These sums represent lost profit and reasonable royalty damages to compensate Cordis for infringement but do not include pre or post judgment interest. In February 2001 a hearing was held on the claims of Boston Scientific and Medtronic AVE that the patents at issue were unenforceable owing to alleged inequitable conduct before the patent office. In March and May 2002, the district judge issued post trial rulings that confirmed the validity and enforceability of the main Cordis stent patent claims but found certain other Cordis patents unenforceable. Further, the district judge granted Boston Scientific a new trial on liability and damages and vacated the verdict against Medtronic AVE on legal grounds. On August 12, 2003, the Court of Appeals for the Federal Circuit found the trial judge erred in vacating the verdict against Medtronic AVE and remanded the case to the trial judge for further proceedings. Cordis filed motions before the trial court on October 14, 2003 to reinstate the verdicts against both Medtronic AVE and Boston 23 Scientific and to award interest and enter injunctions against the stent products at issue in those two cases (the GFX and MicroStent stents of Medtronic AVE and the NIR stent of Boston Scientific) and colorable variations thereof. Medtronic AVE and Boston Scientific are resisting reinstatement of these verdicts and will likely attempt to appeal to the Court of Appeals for the Federal Circuit once judgments are entered. In January 2003, Cordis filed an additional patent infringement action against Boston Scientific in Delaware Federal Court accusing its Express2 and TAXUS stents of infringing one of the Cordis patents involved in the earlier actions against Boston Scientific and Medtronic AVE. In February 2003, Cordis moved in that action for a preliminary injunction seeking to bar the introduction of the TAXUS stent based on that patent. On November 21, 2003, the district judge denied that request for a preliminary injunction and that decision was affirmed by the Court of Appeals for the Federal Circuit in May 2004. Cordis also has pending in Delaware Federal Court another action against Medtronic AVE accusing Medtronic AVE of infringement by sale of stent products introduced by Medtronic AVE subsequent to its GFX and MicroStent products, the subject of the earlier action referenced above. In early June 2003, an arbitration panel in Chicago, in a preliminary ruling, found in favor of Cordis in its arbitration against ACS/Guidant involving infringement by ACS/Guidant of a Cordis stent patent. On August 19, 2003, the panel confirmed that ruling, rejecting the challenge of ACS/Guidant. Under the terms of an earlier agreement between Cordis and ACS/Guidant, the arbitration panel's ruling obligated ACS/Guidant to make a payment of $425 million to Cordis which was made in the fiscal fourth quarter of 2003. As a result of resolving this matter, in the fiscal fourth quarter, $230 million was recorded in other income and expense (approximately $142 million after tax) relating to past periods. The balance of the award, $195 million (approximately $120 million after tax), will be recognized in income in future periods over the estimated remaining life of the intellectual property. No additional royalties for ACS/Guidant's continued use of the technology and no injunction are involved. Patent Litigation Against Various Johnson & Johnson Operating Companies The products of various Johnson & Johnson operating companies are the subject of various patent lawsuits, which could potentially affect the ability of those operating companies to sell those products, or require the payment of past damages and future royalties. The following chart summarizes various patent lawsuits concerning important products of Johnson & Johnson operating companies: 24 Product Patents Plaintiff/ Court Trial Date J&J Patent Date Filed Oper Holder Company Stents Cordis Jang Boston D.Del. 6/13/05 3/03 Scientific Corporation Drug Cordis Ding Boston D.Del. 6/13/05 4/03 Eluting Scientific Corporation Stents Drug Cordis Kunz Boston D.Del. 10/17/05 12/03 Eluting Grainger Scientific Corporation Stents Stents Cordis Rockey Arlaine and S.D.Fla. TBD 7/02 Gena Rockey Inc. Stents Cordis Boneau Medtronic D.Del. TBD 4/02 Inc. Two- Cordis Kastenho- Boston N.D.Cal. TBD 2/02 layer fer Scientific Cathet- Forman Corporation ers Remi- Centocor Cerami Rockefeller E.D.Tex. TBD 4/04 cade University and Chiron Corporation Two- Cordis Kastenho- Boston Belgium TBD 12/03 layer fer Scientific Cathet- (Schneider) ers Stents Cordis Israel Medinol Multiple 1st 5/2003 trial - E.U. Netherl 5/2004 juris- ands dictions Jan 2005 With respect to all of these matters, the Johnson & Johnson operating company involved is vigorously defending against the claims of infringement and disputing where appropriate the validity and enforceability of the patent claims asserted against it. Litigation Against Filers of Abbreviated New Drug Applications (ANDAs) The following chart indicates lawsuits pending against generic firms that filed Abbreviated New Drug Applications seeking to market generic forms of products sold by various subsidiaries of the Company prior to expiration of the applicable patents covering those products. These ANDAs typically include allegations of non-infringement, invalidity and unenforceability 25 of these patents. In the event the subsidiary of the Company involved is not successful in these actions, the firms involved will then introduce generic versions of the product at issue resulting in very substantial market share and revenue losses for the product of the Company's subsidiary. Brand Name Patent/NDA Generic Court Trial Date Product Holder Challenger Date Filed Aciphex Eisai Teva SDNY TBD 11/20/03 20 mg delay (for Dr. SDNY TBD 11/17/03 release Janssen) Reddy's tablet Mylan SDNY TBD 01/28/04 Ditropan XL Ortho Mylan DWV 2/8/05 5/2/03 McNeil, 5, 10, 15 mg ALZA Impax NDCal TBD 9/4/03 controlled release tablet Duragesic Janssen, Mylan D Vt 8/25/03 1/25/02 ALZA 25, 50, 75, 100 micrograms/hr patch Levaquin Daiichi, Mylan DWV 5/24/04 2/22/02 Tablets JJPRD, 250, 500, 750 Ortho McNeil Teva DNJ TBD 6/11/06 mg tablets Levaquin Daiichi, Bedford/ DNJ TBD 3/24/03 Injectable Single use JJPRD, Ortho Ben vials and 5 Venue ml/mg premix McNeil

Sicor DNJ TBD 12/15/03 (Teva) Levaquin Daiichi, American DNJ TBD 12/19/03 Injectable Single use JJPRD, Ortho Pharmac- vials McNeil eutical Partners Quixin Daiichi, Hi-Tech DNJ TBD 12/18/03 Opthalmic Solution (Levo- floxacin) Ortho McNeil Pharmacal Opthalmic solution Ortho Tri- Ortho McNeil Barr DNJ TBD 10/01/03 cyclen LO 0.18 mg/0.025 mg, 0.215 mg/0.025 mg and 0.25 mg/0.025 mg Risperdal Janssen Mylan DNJ TBD 12/29/03 Tablets .25, 0.5, 1, Dr. DNJ TBD 12/29/03 2, 3, 4 mg Reddy's tablets Sporanox Janssen Eon Labs EDNY 5/17/04 4/15/01 100 mg capsule Topamax Ortho McNeil Mylan DNJ TBD 04/12/04 25, 100, 200 mg tablet Ultracet Ortho McNeil Kali DNJ TBD 11/25/02 (Par) 37.5 tram/325 Teva DNJ TBD 02/25/04 apap tablet Caraco ED TBD 09/22/04 Mich 26 In the Duragesic matter referenced above, the district court in March 2004 found ALZA's patent valid, enforceable and infringed by Mylan's generic. Mylan is appealing that ruling. In June 2004, FDA ruled that Mylan's ANDA would be subject to ALZA's period of pediatric exclusivity ending in January 2005. In late June, Mylan filed actions against FDA seeking to require the agency to grant it approval to market on July 24, 2004, the day after the Duragesic patent expired. On August 17, 2004, the district court ruled against Mylan and in favor of FDA's recognition of pediatric exclusivity for Duragesic. Mylan has appealed that ruling to the Court of Appeals for the District of Columbia Circuit. In the action against Mylan involving Levaquin, post- trial papers following the second phase of the trial were submitted to the district court in July 2004 and a decision is expected in the fourth quarter of 2004. In the action against Eon Labs involving Sporanox, the district court ruled on July 28, 2004 that Janssen's patent was valid but not infringed by Eon's generic. Janssen has appealed this ruling to the Court of Appeals for the Federal Circuit. In the action against Kali involving Ultracet, Kali has moved for summary judgment on the issues of infringement and invalidity. The briefing on that motion was completed in October 2004 and a decision is expected in the fourth quarter of 2004. With respect to claims other than that at issue in the litigation against Kali, Ortho-McNeil has filed a reissue application in the U.S. Patent and Trademark Office seeking to narrow the scope of the claims. In the action against Mylan involving Ditropan XL, Mylan moved for summary judgment on July 14, 2004 on the issues of non-infringement and invalidity. A decision is expected in the fourth quarter of 2004. In the action against Mylan relating to Topamax, Mylan on October 8, 2004 filed a motion for summary judgment of non-infringement of Ortho-McNeil's patent. A decision is expected after January 1, 2005. With respect to all of the above matters, the Johnson & Johnson operating company involved is vigorously defending the validity and enforceability and asserting the infringement of its own or its licensor's patents. Average Wholesale Price (AWP) Litigation Johnson & Johnson and its pharmaceutical operating companies, along with numerous other pharmaceutical companies, are defendants in a series of lawsuits in state and federal courts involving allegations that the pricing and marketing of certain pharmaceutical products amounted to fraudulent and otherwise actionable conduct because, among other things, the companies 27 allegedly reported an inflated Average Wholesale Price for the drugs at issue. Most of these cases, both federal actions and state actions removed to federal court, have been consolidated for pre- trial purposes in a Multi-District Litigation (MDL) in federal court in Boston, Massachusetts. The plaintiffs in these cases include classes of private persons or entities that paid for any portion of the purchase of the drugs at issue based on AWP, and state government entities that made Medicaid payments for the drugs at issue based on AWP. Ethicon Endo-Surgery, Inc., a Johnson & Johnson operating company which markets endoscopic surgical instruments, and the Company, are named defendants in a North Carolina state court class action lawsuit alleging AWP inflation and improper marketing activities against TAP Pharmaceuticals. Ethicon Endo-Surgery, Inc. is a defendant based on claims that several of its former sales representatives are alleged to have been involved in arbitrage of a TAP drug. The allegation is that these sales representatives persuaded certain physicians in states where the drug's price was low to purchase from TAP excess quantities of the drug and then resell it in states where its price was higher. Ethicon Endo- Surgery, Inc. and the Company deny any liability for the claims made against them in this case and are vigorously defending against it. On April 24, 2003, the trial judge certified a national class of purchasers of the TAP product at issue. On July 6, 2004, that class was decertified by the North Carolina Court of Appeals and the matter remanded to the trial court for additional consideration. Other The New York State Attorney General's office and the Federal Trade Commission issued subpoenas in January and February 2003 seeking documents relating to the marketing of sutures and endoscopic instruments by the Company's Ethicon, Inc. and Ethicon Endo-Surgery, Inc. subsidiaries. The Connecticut Attorney General's office also issued a subpoena for the same documents. These subpoenas focus on the bundling of sutures and endoscopic instruments in contracts offered to Group Purchasing Organizations and individual hospitals in which discounts are predicated on the hospital achieving specified market share targets for both categories of products. The operating companies involved have responded to the subpoenas. On June 26, 2003, the Company received a request for records and information from the U.S. House of Representatives' Committee on Energy and Commerce in connection with its investigation into pharmaceutical reimbursements and rebates under Medicaid. The Committee's request focuses on the drug REMICADE (infliximab), marketed by the Company's Centocor, Inc. subsidiary. On July 2, 2003, Centocor received a request that it voluntarily provide documents and information to the criminal division of the U.S. Attorney's Office, District of New Jersey, in connection with its investigation into various Centocor marketing practices. Both 28 the Company and Centocor have responded to these requests for documents and information. On August 1, 2003, the Securities and Exchange Commission (SEC) advised the Company of its informal investigation under the Foreign Corrupt Practices Act of allegations of payments to Polish governmental officials by U.S. pharmaceutical companies. On November 21, 2003, the SEC advised the Company that the investigation had become formal and issued a subpoena for the information previously requested in an informal fashion, plus other background documents. The Company and its operating units in Poland are responding to these requests. On December 8, 2003, the Company's Ortho-McNeil Pharmaceutical unit received a subpoena from the United States Attorney's office in Boston, Massachusetts seeking documents relating to the marketing, including alleged off- label marketing, of the drug TOPAMAX (topiramate). Ortho-McNeil is cooperating in responding to the subpoena. In October 2004, the U.S. Attorney's Office in Boston asked attorneys for Ortho-McNeil Pharmaceutical to cooperate in facilitating the subpoenaed testimony of several present and former Ortho-McNeil witnesses before a grand jury in Boston. That requested cooperation is being provided. On January 20, 2004, the Company's Janssen unit received a subpoena from the Office of the Inspector General of the United States Office of Personnel Management seeking documents concerning sales and marketing of, any and all payments to physicians in connection with sales and marketing of, and clinical trials for, RISPERDAL from 1997 to 2002. Janssen is cooperating in responding to the subpoena. In April 2004, the Company's pharmaceutical units were requested to submit information to the Senate Finance Committee on their use of the "nominal pricing exception" in calculating Best Price under the Medicaid Rebate Program. This request was sent to manufacturers for the top twenty drugs reimbursed under the Medicaid Program. The Company's pharmaceutical units have responded to the request. On July 27, 2004, the Company received a letter request from the New York State Attorney General's Office for documents pertaining to marketing, off-label sales and clinical trials for Topamax, Risperdal, Procrit, Reminyl, Remicade and Aciphex. The Company is responding to the request. On August 9, 2004, Johnson & Johnson Health Care Systems, Inc., a Johnson & Johnson operating company, received a subpoena from the Dallas, Texas

U. S. Attorney's Office seeking documents relating to the relationships between the group purchasing organization Novation and HCS and other J&J operating companies. The Company's operating entities involved are responding to the subpoena. On September 30, 2004, Ortho Biotech Inc. received a 29 subpoena from the U.S. Office of Inspector General's Denver, Colorado field office seeking documents directed to sales and marketing of Procrit from 1997 to the present. Ortho Biotech is responding to the subpoena. After a remand from the Federal Circuit Court of Appeals in January 2003, a partial retrial was commenced in October and concluded in November 2003 in Boston, Massachusetts in the action Amgen v. Transkaryotic Therapies, Inc. (TKT) and Aventis Pharmaceutical, Inc. The matter is a patent infringement action brought by Amgen against TKT, the developer of a gene-activated EPO product, and Aventis, which holds marketing rights to the TKT product, asserting that TKT's product infringes various Amgen patent claims. TKT and Aventis dispute infringement and are seeking to invalidate the Amgen patents asserted against them. On October 15, 2004, the district court issued rulings that upheld its initial findings in 2001, that Amgen's patent claims were valid and infringed. Further proceedings and an appeal will follow. The Amgen patents at issue in the case are exclusively licensed to Ortho Biotech Inc., a Johnson & Johnson operating company, in the U.S. for non-dialysis indications. Ortho Biotech Inc. is not a party to the action. On October 21, 2004, in a companion action brought by TKT and Aventis against Amgen and Ortho Biotech's U.K. affiliate in the United Kingdom, the House of Lords, the highest court in the U.K., invalidated the pertinent claims of Amgen's U.K. patent on EPO which expires in December 2004. The ruling clears the way for the commercial launch of TKT's gene-activated EPO product in the U.K., but has no effect outside the U.K. Elsewhere in Western Europe, Amgen's counterpart to the U.K. patent at issue in the proceeding also expires in December 2004, except in France, where it expires in November 2007. The Company is also involved in a number of other patent, trademark and other lawsuits incidental to its business. The ultimate legal and financial liability of the Company in respect to all claims, lawsuits and proceedings referred to above cannot be estimated with any certainty. However, in the opinion of management, based on its examination of these matters, its experience to date and discussions with counsel, the ultimate outcome of legal proceedings, net of liabilities already accrued in the Company's consolidated balance sheet, is not expected to have a material adverse effect on the Company's consolidated financial position, although the resolution in any reporting period of one or more of these matters could have a significant impact on the Company's results of operations and cash flows for that period. NOTE 13 - SUBSEQUENT EVENTS On October 7, 2004 Johnson & Johnson Consumer France S.A.S. acquired Biapharm SAS, a privately held French producer and marketer of skin care products centered around the leading brand BIAFINE(r) which is used as a radiotherapy burn-healing product. The American Jobs Creation Act of 2004 was signed into law on October 22, 2004. The Company is currently evaluating the impact 30 of this law. On October 26, 2004, the FDA approved the CHARITE(tm) Artificial Disc, a device that treats severe low back pain by replacing a damaged or worn out spinal disc with an artificial one. This is the first FDA approval of such a device for spinal discs. Item 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS Results of Operations Analysis of Consolidated Sales For the first fiscal nine months of 2004, worldwide sales were $34.6 billion, an increase of 13.0% over 2003 first fiscal nine month sales of $30.6 billion. The impact of foreign currencies accounted for 3.6% of the total reported fiscal nine month increase. Sales in the U.S. were $20.4 billion in the first fiscal nine months of 2004, which represented an increase of 9.9% over the same period last year. Sales in international markets were $14.2 billion, which represented an increase of 17.8%, of which 9.0% was due to currency fluctuations. All geographic areas throughout the world achieved sales increases during the first fiscal nine months of 2004 as sales increased 17.6% in Europe, 15.9% in the Western Hemisphere (excluding the U.S.) and 19.1% in the Asia- Pacific, Africa region. These sales gains include the positive impact of currency fluctuations between the U.S. dollar and foreign currencies in Europe of 11.0%, in the Western Hemisphere (excluding the U.S.) of 4.1% and in the Asia-Pacific, Africa region of 7.5%. For the fiscal third quarter of 2004, worldwide sales were $11.6 billion, an increase of 10.5% over 2003 fiscal third quarter sales of $10.5 billion. The impact of foreign currencies accounted for 2.8% of the total reported fiscal third quarter 2004 increase. Sales by U.S. companies were $6.8 billion in the fiscal third quarter of 2004, which represented an increase of 5.9%. Sales by international companies were $4.8 billion, which represented an increase of 17.9%, of which 7.1% was due to currency fluctuations. All geographic areas throughout the world posted sales increases during the fiscal third quarter of 2004 as sales increased 17.7% in Europe, 10.9% in the Western Hemisphere (excluding the U.S.) and 21.4% in the Asia- Pacific, Africa region. These sales gains include the positive impact of currency fluctuations between the U.S. dollar and foreign currencies in Europe of 9.5%, in the Western Hemisphere (excluding the U.S.) of 1.5% and in the Asia-Pacific, Africa region of 5.5%. Analysis of Sales by Business Segments Consumer Consumer segment sales in the first fiscal nine months of 2004 were $6.1 billion, an increase of 11.4% over the same period a year ago with 7.9% of operational growth and a positive currency 31 impact of 3.5%. U.S. Consumer segment sales increased by 6.0% while international sales gains of 17.5% included a positive currency impact of 7.5%. Major Consumer Franchise Sales - First Fiscal Nine Months Total Operations Currency 2004 2003 %Change %Change %Change OTC & Nutritionals $1,662 $1,433 16.0% 14.5% 1.5% Skin Care 1,580 1,334 18.5 13.5 5.0 Women's Health 1,087 1,015 7.1 2.8 4.3 Baby & Kids Care 1,064 971 9.6 4.9 4.7 Other 678 698 (2.9) (4.8) 1.9 Total $6,071 $5,451 11.4% 7.9% 3.5% Consumer segment sales in the fiscal third quarter of 2004 were $2.0 billion, an increase of 9.9% over the same period a year ago with 7.4% of operational growth and a positive currency impact of 2.5%. U.S. Consumer segment sales increased by 4.0% while international sales gains of 16.8% included a positive currency impact of 5.4%. Major Consumer Franchise Sales - Fiscal Third Quarter Total Operations Currency 2004 2003 %Change %Change %Change OTC & Nutritionals $ 566 $ 498 13.7% 12.7% 1.0% Skin Care 509 421 20.9 17.1 3.8 Women's Health 371 358 3.6 .5 3.1 Baby & Kids Care 361 337 7.4 3.8 3.6 Other 217 227 (4.4) (5.3) .9 Total $2,024 $1,841 9.9% 7.4% 2.5% Consumer segment sales growth in the fiscal third quarter was attributable to strong sales performance in the major franchises in this segment including McNeil Over-The-Counter and Nutritional products, Skin Care, and Baby & Kids Care in the U.S. The growth in McNeil Over-The-Counter and Nutritional products was driven by the acquisition of the remaining 50% stake in the Johnson & Johnson-Merck Consumer Pharmaceuticals Co. non-prescription pharmaceuticals joint venture, and the continued growth of SPLENDA(r) Tabletop brand no calorie sweetener, partially offset by the sale of the SPLENDA(r)ingredients business on April 2, 2004. The Skin Care franchise sales growth was broad based, with strong performance by the NEUTROGENA(r), AVEENO(r), RoC(r) and CLEAN & CLEAR(r) brands. NEUTROGENA(r) achieved strong growth in the U.S. with the new line of Advanced Solutions (tm)products, and RoC(r) had strong international growth with the Retinol Gold brand. The Baby & Kids Care franchise growth in the U.S. was led by JOHNSON'S(r)SOFTWASH(tm), Milk Lotion and Milk Bath products. Pharmaceutical Pharmaceutical segment sales in the first fiscal nine months of 2004 were $16.3 billion, an increase of 13.2% over the same period 32 a year ago with 10.4% of this change due to operational increases and the remaining 2.8% increase related to the positive impact of currency. The U.S. Pharmaceutical sales increase was 11.8% and the growth in international Pharmaceutical sales was 16.4% which included 9.0% related to the positive impact of

currency. Major Pharmaceutical Product Sales - First Fiscal Nine Months Total Operations Currency 2004 2003 %Change %Change %Change PROCRIT(r)/ EPREX(r) $2,739 $3,017 (9.2%) (11.8%) 2.6% RISPERDAL(r) 2,203 1,855 18.8 14.4 4.4 REMICADE(r) 1,548 1,273 21.6 21.6 0.0 DURAGESIC(r) 1,548 1,200 29.0 24.5 4.5 TOPAMAX(r) 1,029 747 37.7 35.4 2.3 Hormonal Contraceptives 975 847 15.1 14.0 1.1 LEVAQUIN(r)/ FLOXIN(r) 921 824 11.9 12.0 (0.1) Other 5,325 4,621 15.2 11.6 3.6 Total $16,288 $14,384 13.2% 10.4% 2.8% Pharmaceutical segment sales in the fiscal third quarter of 2004 were $5.5 billion, an increase of 13.4% over the same period a year ago with 11.1% of this change due to operational increases and the remaining 2.3% increase related to the positive impact of currency. The U.S. Pharmaceutical sales increase was 12.5% and the growth in international Pharmaceutical sales was 15.5% which included 7.2% related to the positive impact of currency. Major Pharmaceutical Product Sales - Fiscal Third Quarter Total Operations Currency 2004 2003 %Change %Change %Change PROCRIT(r)/ EPREX(r) $ 887 $1,005 (11.7%) (13.7%) 2.0% RISPERDAL(r) 746 599 24.6 20.8 3.8 REMICADE(r) 545 443 22.9 22.9 0.0 DURAGESIC(r) 536 424 26.7 22.8 3.9 TOPAMAX(r) 365 253 44.6 42.7 1.9 Hormonal Contraceptives 304 292 4.2 3.2 1.0 LEVAQUIN(r)/ FLOXIN(r) 270 253 7.0 7.2 (0.2) Other 1,832 1,566 17.0 14.0 3.0 Total $5,485 $4,835 13.4% 11.1% 2.3% Pharmaceutical segment sales growth was adversely affected by the sales decline of PROCRIT(r) (Epoetin alfa) and EPREX(r) (Epoetin alfa) due to increased competition. Combined, PROCRIT (r)(sold in the U.S.) and EPREX(r)(sold internationally) sales declined 11.7% in the fiscal third quarter of 2004 versus the same period a year ago. Sales of PROCRIT(r) in the fiscal third quarter were down 12.7% versus the same period last year. On a unit basis, PROCRIT(r) declined slightly when compared with the fiscal third quarter 2003. 33 RISPERDAL(r) (risperidone), a medication that treats the symptoms of schizophrenia, fueled by RISPERDAL(r) CONSTA(tm) grew by 24.6% in the fiscal third quarter 2004. REMICADE(r) (infliximab), a novel monoclonal antibody therapy indicated to treat Crohn's disease and used in the treatment of rheumatoid arthritis, continued to maintain its leadership position in the growing Anti-TNF-a (tumor necrosis factor alpha) market. In September the FDA approved REMICADE(r) for expanded use as a first line therapy in patients with moderate to severe rheumatoid arthritis. Sales of DURAGESIC(r) (fentanyl transdermal systems) grew by 26.7% in the fiscal third quarter 2004. In August, the U.S. District Court for the District of Columbia affirmed the pediatric exclusivity for DURAGESIC (r) granted to Janssen by the FDA. The pediatric exclusivity will expire on January 23, 2005. TOPAMAX(r) (topiramate), an antiepileptic and recently approved for use in the prevention of migraines, had strong growth over the same period a year ago. Growth was also achieved in DITROPAN XL(r) (oxybutynin chloride), a treatment for overactive bladder, REMINYL(r) (galantamine (HBr)), a treatment for patients with mild to moderate Alzheimer's disease, NATRECOR(r) (nesiritide), a treatment for acute congestive heart failure, and ULTRACET(r)(37.5 mg tramadol hydrochloride/325 mg acetaminophen tablets), used in the management of acute pain. CONCERTA(r)(methylphenidate HCl), a treatment for attention deficit hyperactivity disorder, sales continued to grow despite the current absence of patent exclusivity in the U.S. At present, the FDA has not approved any generic that is substitutable for CONCERTA(r). Medical Devices and Diagnostics Medical Devices and Diagnostics segment sales in the first fiscal nine months of 2004 were $12.2 billion, an increase of 13.6% over the same period a year ago with 9.1% of this change due to operational increases and the remaining 4.5% increase related to the positive impact of currency. The U.S. Medical Devices and Diagnostics sales increase was 8.8% and the growth in international Medical Devices and Diagnostics sales was 19.2% which included 9.8% related to the positive impact of currency. Major Medical Devices and Diagnostics Franchise Sales - First Fiscal Nine Months Total Operations Currency 2004 2003 %Change %Change %Change DePuy $2,468 $2,206 11.9% 7.9% 4.0% Cordis 2,298 1,811 26.9 23.1 3.8 Ethicon 2,085 1,942 7.3 1.7 5.6 Ethicon Endo- Surgery 2,047 1,894 8.1 3.7 4.4 LifeScan 1,240 1,040 19.2 15.0 4.2 Vision Care 1,123 959 17.2 11.6 5.6 Ortho-Clinical Diagnostics 928 868 7.0 2.5 4.5 Other 48 53 (9.4) (8.1) (1.3) Total $12,237 $10,773 13.6% 9.1% 4.5% 34 Medical Devices and Diagnostics segment sales in the fiscal third quarter of 2004 were $4.0 billion, an increase of 7.0% over the same period a year ago with 3.6% of this change due to operational increases and the remaining 3.4% increase related to the positive impact of currency. The U.S. Medical Devices and Diagnostics sales decrease was 3.4% and the growth in international Medical Devices and Diagnostics sales was 20.6% which included 7.8% related to the positive impact of currency. Major Medical Devices and Diagnostics Franchise Sales - Fiscal Third Quarter Total Operations Currency 2004 2003 %Change %Change %Change DePuy $ 790 $ 718 10.0% 6.9% 3.1% Cordis 756 791 (4.4) (7.0) 2.6 Ethicon 687 640 7.3 3.0 4.3 Ethicon Endo- Surgery 672 622 8.0 4.7 3.3 LifeScan 420 362 16.1 12.6 3.5 Vision Care 392 343 14.6 10.2 4.4 Ortho-Clinical Diagnostics 309 287 7.9 4.4 3.5 Other 18 16 12.5 3.8 8.7 Total $4,044 $3,779 7.0% 3.6% 3.4% DePuy franchise growth in the fiscal third quarter was primarily due to DePuy's orthopaedic joint reconstruction products including the knee and hip product lines. Solid growth was also reported in the area of spine. The positive growth was partially offset by the sale of the Castings business in the first quarter of 2004 and weakness in the neuro and trauma lines. Cordis sales declined by 4.4% in the fiscal third quarter 2004. This was the result of a 37% decrease in U.S. sales of the CYPHER(r) Sirolimus-eluting Stent when compared to the fiscal third quarter 2003. The third quarter of this year is the second full quarter with a competitive product in the U.S. marketplace. Internationally, Cordis sales grew by 51.3% in the fiscal third quarter. This included 41.8% of operational growth and a favorable currency impact of 9.5%. The launch of CYPHER(r)in Japan during the fiscal third quarter 2004 contributed to the strong international sales growth. On April 2, 2004 and July 22, 2004, Cordis Cardiology Division of Cordis Corporation, a Johnson & Johnson Company, received warning letters from the FDA regarding observations concerning Good Manufacturing Practice regulations. These observations followed post-approval site inspections completed in 2003, including sites involved in the production of the CYPHER(r) stent. In response to the warning letters, Cordis as met periodically with the FDA representatives at the Center and the Districts advising them of the progress in addressing the Quality System issues. Ethicon franchise growth was related to strong sales of VICRYL 35 (r)(polyglactin 910) PLUS antibacterial coated sutures, as well as new products such as the Multipass needle introduced in April 2004. Ethicon Endo-Surgery franchise experienced growth in Endocutter sales that include products used in performing bariatric procedures, an important focus for the franchise. Strong sales in the Advanced Sterilization product line were also a key contributor to results in the quarter. LifeScan franchise growth was due to increased sales of the OneTouch(r) Ultra(r) brand primarily in international markets. Vision Care franchise growth was led by continued success in the Japanese market as well as strong growth in the U.S. market led by the introduction of Acuvue(r) Advance(tm) with HydraClear(tm), a silicone hydrogel material launched nationwide in the U.S. in January 2004. Cost of Goods Sold and Selling, General and Administrative Expenses Consolidated costs of goods sold for the first fiscal nine months of 2004 decreased to 28.1% from 28.3% of sales over the same period a year ago. The cost of goods sold for the fiscal third quarter of 2004 was 27.6% of sales. The cost of goods sold as a percentage of sales in the fiscal third quarter of 2003 was 28.5%. The favorable change in the third fiscal quarter of 2004 was primarily in the Medical Devices and Diagnostics segment, related to positive mix, divestiture of low gross margin businesses, and the absence of certain CYPHER(r)stent related costs incurred in 2003. There were also cost containment activities across all segments. Consolidated selling, general and

administrative expenses as a percent to sales for the first fiscal nine months of 2004 were 32.4% versus 32.9% for the same period a year ago, which represented an improvement of .5% as a percent of sales. This improvement was primarily due to the Company's focus on managing expenses. Consolidated selling, general and administrative expenses as a percent to sales increased from 32.8% in the fiscal third quarter of 2003 to 33.3% in the fiscal third quarter of 2004. This increase was primarily attributable to decisions to increase investment spending behind certain OTC and Consumer brands and certain products and regions in the Pharmaceutical segment. Research & Development Research activities represent a significant part of the Company's business. These expenditures relate to the development of new products, improvement of existing products, technical support of products and compliance with governmental regulations for the protection of the consumer. Worldwide costs of research activities, for the first fiscal nine months of 2004 were $3.5 billion, an increase of 8.8% over the same period a year ago. Research and development spending in the fiscal third quarter of 2004 was $1.2 billion, an increase of 1.8% over the fiscal third quarter of 2003. 36 In-Process Research & Development In the fiscal third quarter of 2004, the Company recorded In- process Research & Development (IPR&D) charges of $18 million before tax and $12 million after tax as a result of the acquisition of U.S. commercial rights to certain patents and know-how in the field of sedation and analgesia from Scott Lab, Inc. In the fiscal second quarter of 2003, the Company recorded In-process Research & Development charges of $900 million before and after tax related to acquisitions. These acquisitions included Scios Inc. and the Link Spine Group, Inc. Scios Inc. is a biopharmaceutical company with a marketed product for cardiovascular disease and research projects focused on auto- immune diseases. Link Spine Group, Inc. was acquired to provide the Company with exclusive worldwide rights to the SB Charite Artificial Disc for the treatment of spine disorders. In the fiscal first quarter of 2003, the Company recorded IPR&D charges of $15 million after tax ($18 million before tax) related to acquisitions. These acquisitions included certain assets of Orquest, Inc., a privately-held biotechnology company focused on developing biologically-based implants for orthopaedics spine surgery, and 3-Dimensional Pharmaceuticals, Inc., a company with a technology platform focused on the discovery and development of potential new drugs in early stage development for the treatment of cardiovascular diseases, oncology and inflammation. Other (Income) Expense, Net Other (income) expense included gains and losses related to the sale and write-down of certain equity securities of the Johnson & Johnson Development Corporation, losses on the disposal of assets, currency gains & losses, minority interests, litigation settlement expense as well as royalty income. The unfavorable change in other (income) expense in the first fiscal nine months of 2004 as compared to the same period a year ago was due primarily to the gain associated with the Vascular Access divestiture in the fiscal second quarter of 2003. The unfavorable change in other (income) expense in the fiscal third quarter of 2004 as compared to the same period a year ago was due primarily to the positive impact in 2003 of the recovery of a loan that had been written off in a prior year, as well as the establishment of an insurance receivable reserve and an increase in asset write-offs in the fiscal third quarter of 2004. OPERATING PROFIT BY SEGMENT Consumer Segment Operating profit for the Consumer segment as a percent to sales in the first fiscal nine months of 2004 was 19.6% versus 21.1% over the same period a year ago. This decrease was primarily due to ongoing costs associated with a plant closure and the decision to increase investment spending behind certain OTC and Consumer brands. Operating profit as a percent to sales in the fiscal third quarter of 2004 was 17.7% versus 19.8% over the same period a year ago. This decrease was due to the decision to increase investment spending behind certain OTC and Consumer brands. 37 Pharmaceutical Segment Operating profit for the Pharmaceutical segment as a percent to sales in the first fiscal nine months of 2004 was 37.6% versus 32.7% over the same period a year ago. Excluding IPR&D charges, operating profit as a percent to sales in the first fiscal nine months of 2003 was 37.8%. Operating profit as a percent to sales in the fiscal third quarter of 2004 was 35.0% versus 36.2% over the same period a year ago. The decrease in 2004 was due to the decision to increase investment spending for certain products and in certain regions. Medical Devices and Diagnostics Segment Operating profit for the Medical Devices and Diagnostics segment as a percent to sales in the first fiscal nine months of 2004 was 26.0% versus 21.6% over the same period a year ago. Excluding IPR&D charges, operating profit as a percent to sales was 26.1% in the first fiscal nine months of 2004, and 23.3% in the first fiscal nine months of 2003. Operating profit as a percent to sales in the fiscal third quarter of 2004 was 26.0% versus 24.6% in the fiscal third quarter of 2003. Excluding IPR&D charges, operating profit as a percent to sales in the fiscal third quarter of 2004 was 26.5%. The increase in 2004 was due to favorable sales mix, the impact of divestitures of low gross margin businesses, the absence of certain CYPHER(r) stent related costs incurred in 2003, and cost containment activities. Interest (Income) Expense Interest income decreased in both the first fiscal nine months and fiscal third quarter of 2004 as compared to the same periods a year ago. The decrease was due to a decline in the average rate on investments partially offset by a higher average cash balance. The cash balance including marketable securities at the end of the fiscal third quarter of 2004 was $13.2 billion, which was $4.2 billion higher than the same period a year ago. Interest expense decreased in both the first fiscal nine months and fiscal third quarter of 2004 as compared to the same periods a year ago. The decrease is due to the redemption of commercial paper during 2004. Provision For Taxes on Income The worldwide effective income tax rates for the first fiscal nine months of 2004 and 2003 were 28.6% and 32.5%. The decrease in the effective tax rate for the first fiscal nine months of 2004 compared with the same period a year ago was principally due to 2003 acquisition related IPR&D charges that are non-deductible for tax purposes. The 2003 tax rate excluding the effect of IPR&D was 29.2%. LIQUIDITY AND CAPITAL RESOURCES Cash Flows Cash generated from operations provided the major sources of funds for the growth of the business, including working capital, capital expenditures, acquisitions, share repurchases, dividends and debt repayments. In the first fiscal nine months of 2004, cash flow 38 from operations was $8.7 billion, an increase of $1.6 billion over the same period a year ago. The major factor contributing to the increase in cash generated from operations was from a net income increase of $1.0 billion, net of the non-cash impact of IPR&D charges. Net cash used by investing activities decreased by $1.5 billion versus the same period a year ago due to a decrease in acquisition activity offset by an increase in the purchase of investments. Net cash used by financing activities increased by $1.9 billion primarily due to a decrease in proceeds from short and long term debt. On October 1, 2004 the Company announced that it had exercised its option to redeem all of its $300,000,000 aggregate principal amount of 8.72% debentures due 2024 that remained outstanding on the redemption date, November 1, 2004. Dividends On July 20, 2004, the Board of Directors declared a regular cash dividend of $0.285 per share, payable on September 7, 2004 to shareholders of record as of August 17, 2004. On October 22, 2004, the Board of Directors declared a regular cash dividend of $0.285 per share, payable on December 7, 2004 to shareholders of record as of November 16, 2004. The Company expects to continue the practice of paying regular cash dividends. OTHER INFORMATION New Accounting Standards In January 2003, the FASB issued FIN 46, "Consolidation of Variable Interest Entities - an interpretation of ARB No. 51", and in December 2003, issued a revised FIN 46(R), "Consolidation of Variable Interest Entities - an interpretation of ARB No. 51", both of which address consolidation of variable interest entities. FIN 46 expanded the criteria for consideration in determining whether a variable interest entity should be consolidated by a business entity, and requires existing unconsolidated variable interest entities

(which include, but are not limited to, Special Purpose Entities, or SPEs) to be consolidated by their primary beneficiaries if the entities do not effectively disperse risks among parties involved. This interpretation was immediately applicable to variable interest entities created after January 31, 2003. The adoption of this portion of FIN 46 did not have a material effect on the Company's results of operations, cash flows or financial position. FIN 46 is applicable in 2004 to variable interest entities in which an enterprise holds a variable interest that was acquired before February 1, 2003. The adoption of this portion of FIN 46 did not have a material effect on the results of operations, cash flows and financial position of the Company. In December 2003, the FASB issued FASB Staff Position (FSP) FAS No. 106-1, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003", which is effective for interim or annual financial statements of fiscal years ending after December 7, 2003. The Company elected to defer adoption of FSP FAS No. 106-1 until 39 authoritative guidance was issued, as allowed by the Standard. This guidance was issued by the FASB in May 2004 via FSP FAS No. 106-2. The Company adopted FSP FAS No. 106-1 and 106-2 in the fiscal third quarter of 2004, as allowed by the Standards. This adoption did not have a material effect on the Company's results of operations, cash flows or financial position. In July 2004 the FASB ratified the EITF consensus on Issue 02- 14, "Whether an Investor should Apply the Equity Method of Accounting to Investments Other Than Common Stock". The Company will adopt EITF Issue 02-14 in the fourth quarter of 2004, as prescribed by the Standard. This adoption is not expected to have a material effect on the Company's results of operations, cash flows and financial position. The Company adopted EITF Issue 03-6 "Participating Securities and the Two-Class Method under FASB Statement No. 128" in the fiscal third quarter of 2004. This adoption did not have an effect on the Company's results of operations, cash flows and financial position. Economic and Market Factors Johnson & Johnson is aware that its products are used in an environment where, for more than a decade, policymakers, consumers and businesses have expressed concern about the rising cost of health care. Johnson & Johnson has a long-standing policy of pricing products responsibly. For the period 1993 - 2003, in the United States, the weighted average compound annual growth rate of Johnson & Johnson price increases for health care products (prescription and over-the-counter drugs, hospital and professional products) was below the U.S. Consumer Price Index (CPI). Inflation rates, even though moderate in many parts of the world during 2004, continue to have an effect on worldwide economies and, consequently, on the way companies operate. In the face of increasing costs, the Company strives to maintain its profit margins through cost reduction programs, productivity improvements and periodic price increases. The Company faces various worldwide health care changes that may result in pricing pressures that include health care cost containment and government legislation relating to sales, promotions and reimbursement. On December 8, 2003, the Medicare Prescription Drug Improvement and Modernization Act of 2003 was enacted that introduces a prescription drug benefit under Medicare as well as a subsidy to sponsors of retiree health care benefit plans. The Company elected to defer the recognition of the Act until such time when the authoritative guidance was issued. This guidance was issued by the FASB in May 2004. The Company adopted the recognition of the Act in the fiscal third quarter of 2004. 40 The Company also operates in an environment which is becoming increasingly hostile to intellectual property rights. Generic drug firms have filed Abbreviated New Drug Applications seeking to market generic forms of most of the Company's key pharmaceutical products, prior to expiration of the applicable patents covering those products. In the event the Company is not successful in defending a lawsuit resulting from an Abbreviated New Drug Application filing, the generic competition typically results in creating a loss of market exclusivity and may result in a significant reduction in sales. For further information see the discussion on "Litigation Against Filers of Abbreviated New Drug Applications" in Note 12. CAUTIONARY FACTORS THAT MAY AFFECT FUTURE RESULTS This Form 10-Q contains forward-looking statements. Forward- looking statements do not relate strictly to historical or current facts and anticipate results based on management's plans that are subject to uncertainty. Forward-looking statements may be identified by the use of words like "plans," "expects," "will," "anticipates," "estimates" and other words of similar meaning in conjunction with, among other things, discussions of future operations, financial performance, the Company's strategy for growth, product development, regulatory approval, market position and expenditures. Forward-looking statements are based on current expectations of future events. The Company cannot guarantee that any forward- looking statement will be accurate, although the Company believes that it has been reasonable in its expectations and assumptions. Investors should realize that if underlying assumptions prove inaccurate or that unknown risks or uncertainties materialize, actual results could vary materially from the Company's expectations and projections. Investors are therefore cautioned not to place undue reliance on any forward-looking statements. The Company assumes no obligation to update any forward-looking statements as a result of new information or future events or developments. Risks and uncertainties include general industry conditions and competition; economic conditions, such as interest rate and currency exchange rate fluctuations; technological advances, new products and patents attained by competitors; challenges inherent in new product development, including obtaining regulatory approvals; challenges to patents; U.S. and foreign health care reforms and governmental laws and regulations; trends toward health care cost containment; increased scrutiny of the health care industry by government agencies; product efficacy or safety concerns resulting in product recalls or regulatory action. The Company's report on Form 10-K for the year ended December 28, 2003 contains, as an Exhibit, a discussion of additional factors that could cause actual results to differ from expectations. The Company notes these factors as permitted by the Private Securities Litigation Reform Act of 1995. 41 Item 3 - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK There has been no material change in the Company's assessment of its sensitivity to market risk since its presentation set forth in Item 7A, "Quantitative and Qualitative Disclosures About Market Risk," in its Annual Report on Form 10-K for the fiscal year ended December 28, 2003. Item 4 - CONTROLS AND PROCEDURES-EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES Disclosure controls and procedures. As of the end of the period covered by this report, the Company evaluated the effectiveness of the design and operation of its disclosure controls and procedures. The Company's disclosure controls and procedures are designed to ensure that the Company records, processes, summarizes and reports in a timely manner the information the Company must disclose in its reports filed under the Securities Exchange Act. William C. Weldon, Chairman and Chief Executive Officer, and Robert J. Darretta, Vice Chairman and Chief Financial Officer, reviewed and participated in this evaluation. Based on this evaluation, Messrs. Weldon and Darretta concluded that, as of the date of their evaluation, the Company's disclosure controls and procedures were effective. Internal control. Since the date of the evaluation described above, there have not been any significant changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control. Part II - OTHER INFORMATION Item 1. Legal Proceedings The information called for by this item is incorporated herein by reference to Note 12 included in Part I, Notes to Consolidated Financial Statements. Item 5. Exhibits and Reports on Form 8-K (a) Exhibit Exhibit 99.3 Certifications Under Rule 13a-14(a) of the Securities Exchange Act Pursuant to Section 302 of the Sarbanes-Oxley Act. Exhibit 99.15 Certifications Pursuant to Section 906 of the Sarbanes-Oxley Act. 42 (b) Reports on Form 8-K A Report on Form 8-K was furnished on July 15, 2004, which

included the press release for the period ended June 27, 2004. Also included in this filing are the unaudited comparative supplementary sales data and condensed consolidated statement of earnings for this fiscal second quarter and six month period ended June 27, 2004. A Report on Form 8-K was filed on October 4, 2004, which included a press release dated October 1, 2004 announcing the redemption of 8.72% debentures due November 2024. A Report on Form 8-K was filed on October 6, 2004, which included a press release dated October 1, 2004 announcing that Ortho Biotech Products, L.P., a Johnson & Johnson company, received a subpoena from the Inspector General, Department of Health and Human Services, requesting documents related to the sales and marketing of PROCRIT(r) (Epoetin Alfa) A report on Form 8-K was furnished on October 13, 2004, which included the press release for the period ended September 26, 2004. Also included in this filing are the unaudited comparative supplementary sales data and condensed consolidated statement of earnings for the fiscal third quarter and nine month period ended September 26, 2004. 43 SIGNATURES Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized. JOHNSON & JOHNSON (Registrant) Date: November 3, 2004 By /s/ R. J. DARRETTA R. J. DARRETTA Vice Chairman (Chief Financial Officer) Date: November 3, 2004 By /s/ S. J. COSGROVE S. J. COSGROVE Controller (Chief Accounting Officer) 44