FOREST LABORATORIES INC
Form 10-K
June 14, 2004

# SECURITIES AND EXCHANGE COMMISSION

**WASHINGTON, D.C. 20549**

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FORM 10-K

(Mark one)

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the Fiscal Year Ended March 31, 2004

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period From _____ to _____

Commission File No. 1-5438

FOREST LABORATORIES, INC.

*(Exact name of registrant as specified in its charter)*

| Delaware | 11-1798614 |
|---|---|
| *(State or other jurisdiction of incorporation or organization)* | *(I.R.S. Employer Identification Number)* |
| 909 Third Avenue<br>New York, New York | 10022 |
| *(Address of principal executive offices)* | *(Zip code)* |

(212) 421-7850

*(Registrant's telephone number, including area code)*

Securities registered pursuant to Section 12(b) of the act:

| **Title of each class** | Name of each exchange on which registered |
|---|---|
| Common Stock, $.10 par value | New York Stock Exchange |
| Rights, as adjusted, to purchase one eighth of one-hundredth share of Series A Junior Participating Preferred Stock, par value $1.00 per share | New York Stock Exchange |

Securities registered pursuant to Section 12(g) of the act:

None

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein and will not be contained, to the best of the registrant's knowledge, in the Proxy Statement incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. __ .

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes _X_ No ___.

The aggregate market value of the voting stock held by non-affiliates of the registrant as of September 30, 2003 was $18,393,051,894.

Number of shares outstanding of the registrant's Common Stock as of June 10, 2004: 369,850,601.

The following documents are incorporated by reference herein:

Portions of the definitive proxy statement to be filed pursuant to Regulation 14A promulgated under the Securities Exchange Act of 1934 in connection with the 2004 Annual Meeting of Stockholders of registrant.

Portions of the registrant's Annual Report to Stockholders for the fiscal year ended March 31, 2004.

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PART I

PART I

ITEM 1. BUSINESS

General

Forest Laboratories, Inc. and its subsidiaries (collectively, "Forest" or the "Company") develop, manufacture and sell ethical drug products which require a physician's prescription, as well as non-prescription pharmaceutical products sold over-the-counter. Forest's most important United States products consist of branded ethical drug specialties marketed directly, or "detailed," to physicians by the Company's Forest Pharmaceuticals, Forest Therapeutics, Forest Healthcare, Forest Ethicare and Forest Specialty Sales salesforces. The Company emphasizes detailing to physicians of those branded ethical drugs it believes have the most potential for growth, and the development and introduction of new products, including products developed in collaboration with licensing partners.

Forest's products include those developed by Forest and those acquired from other pharmaceutical companies and integrated into Forest's marketing and distribution systems. See "Recent Developments."

Forest is a Delaware corporation organized in 1956. Forest's principal executive offices are located at 909 Third Avenue, New York, New York 10022 (telephone number 212-421-7850) and its corporate website address is http://www.frx.com. Forest makes its electronic filings with the Securities and Exchange Commission ("SEC"), including annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to these reports available on the corporate website free of charge as soon as practicable after filing with or furnishing to the SEC.

Recent Developments

**Namenda™**: In October 2003, Namenda (memantine HCl) was approved for marketing and distribution by the United States Food and Drug Administration ("FDA") for the treatment of moderate to severe Alzheimer's disease. Initial stocking of Namenda began in December 2003 and the Company's salesforce began promotion of the product in March 2004. Sales of Namenda to March 31, 2004 were $45,472,000. Namenda is a moderate-affinity, uncompetitive NMDA receptor antagonist that modulates the effects of glutamate - a neurotransmitter found in the brain. Excessive levels of glutamate are hypothesized to contribute to the dysfunction and eventual death of brain cells observed in Alzheimer's disease. Forest believes that Namenda's mechanism of action is distinct from drugs currently available to treat Alzheimer's disease. Forest obtained the exclusive rights to develop and market memantine in the United States by license agreement with Merz Pharma GmbH of Germany ("Merz"), the originator of the product.

During fiscal 2004, Forest announced the results of a six month placebo-controlled Phase III study of memantine in patients with mild to moderate Alzheimer's disease. In the study, patients who received memantine performed significantly better on both primary measures of cognition and global functioning than those given a placebo. Based on the results of this study, Forest expects to submit a supplemental NDA ("sNDA") to the FDA seeking approval for the mild to moderate Alzheimer's disease indication during the second half of calendar 2004.

In addition, Forest is conducting a Phase II program for the use of Namenda in neuropathic pain. While a 16 week Phase III clinical study for this indication completed during fiscal year 2004 failed to demonstrate statistical significance for the study's primary endpoints, an analysis of the study results demonstrated statistically significant weekly improvements in the assessments of nocturnal pain for the first 14 weeks. Based on the outcome of this Phase II program, Forest may choose to initiate additional Phase III trials required to submit an NDA for approval of Namenda for this indication.

**Lexapro®**: In September 2002, Forest launched Lexapro (escitalopram oxalate), a single isomer version of Forest's Celexa® (citalopram HBr) for the treatment of major depression, following approval of the product by the FDA in August 2002. Citalopram is a racemic mixture with two mirror image molecules, the S- and R-isomers. The S-isomer of citalopram is the active isomer in terms of its contribution to citalopram's antidepressant effects, while the R-isomer does not contribute to the antidepressant activity. With Lexapro, the R-isomer has been removed, leaving only the active S-isomer. Clinical trials demonstrate that Lexapro is a more potent selective serotonin reuptake inhibitor ("SSRI") than its parent compound, and confirm the antidepressant activity of Lexapro in all major clinical measures of depression. During fiscal 2004, sales of Lexapro were $1,088,957,000. According to data published by IMS, an independent prescription audit firm, as of May 21, 2004, Lexapro achieved a 16.7% share of total prescriptions for antidepressants in the SSRI/SNRI category.

In December 2003, Lexapro received FDA approval of its sNDA for the treatment of generalized anxiety disorder ("GAD"), a disorder characterized by excessive anxiety and worry about every day events or activities for a period of 6 months or more. The approval was based upon three GAD studies involving Lexapro which demonstrated significantly greater improvement in anxiety symptoms relative to placebo. Forest began marketing Lexapro for the treatment of GAD in January 2004. An additional sNDA to further expand the labeling for Lexapro to include an indication for the treatment of social phobia, was filed on May 25, 2004 .

Lexapro was developed by Forest and H. Lundbeck A/S, a Danish pharmaceutical firm which licenses the exclusive United States marketing rights to this compound, as well as Celexa, to Forest.

**Celexa**: Sales of Celexa, an SSRI for the treatment of depression, were $1,087,281,000 for the fiscal year ended March 31, 2004. Forest continues to sell Celexa, but discontinued the active promotion of the product at the time Lexapro was launched. According to data published by IMS, an independent prescription audit firm, as of May 21, 2004 Celexa declined from a peak share of 17.5% achieved in August 2002, to an 8.7% share of total prescriptions for antidepressants in the SSRI/SNRI category.

Forest believes that one or more applications by generic distributors to introduce generic forms of Celexa are pending at the FDA, with possible approval during Forest's 2005 fiscal year. Forest expects to launch its own generic version of Celexa to compete with third party generic products when those products become available.

**Neramexane:** In July 2001, Forest entered into a license agreement with Merz for the development and marketing in the United States of neramexane. Neramexane, a patented novel NMDA receptor antagonist, is currently in Phase II clinical trials and is being tested for various CNS disorders.

**Milnacipran:** In January 2004, Forest entered into a license and collaboration agreement with Cypress Bioscience, Inc. for the development and marketing in the United States of milnacipran. Milnacipran is currently in Phase III development as a treatment of Fibromyalgia Syndrome ("FMS"). FMS is a frequent cause of chronic, widespread pain and is estimated to affect six to twelve million people in the United States. There are currently no products approved by the FDA for the treatment of this disorder. Pursuant to the collaboration agreement, Forest paid Cypress an upfront license fee and will pay Cypress milestone payments on the achievement of specific product development milestones, as well as running royalties based on net sales of the product following approval. Forest will be responsible for funding further development activities, which will be jointly managed by the two companies, and will have responsibility for sales and marketing activities, with Cypress having the option to perform up to 25% of physician details. The license agreement includes two patents covering the use of milnacipran for the treatment of FMS. In addition, Forest believes that, as a new chemical entity, milnacipran will qualify for five years of exclusivity under the Hatch-Waxman Act.

The current Phase III program is based on the results of a controlled randomized Phase II Study in 125 FMS patients. The Phase II Study demonstrated statistically significant improvements in multiple measures of clinical pain and secondary symptoms, including fatigue, mood and patient global status reports.

Subject to the successful completion of the Phase III program, Forest anticipates filing an NDA for milnacipran in fiscal 2008.

**CCR1 Antagonists**: In March, 2004, Forest entered into a license and collaboration agreement with ChemoCentryx, Inc., a privately held pharmaceutical development company, to develop and commercialize novel small-molecular therapeutics for autoimmune and inflammatory diseases, such as rheumatoid arthritis and multiple sclerosis. The collaboration focuses on CCR1, a specific chemokine receptor involved in the inflammation process. Under the terms of the arrangement, Forest paid ChemoCentryx an upfront payment and purchased shares of a class of ChemoCentryx preferred stock. Forest will provide funding for joint research for up to three years and will have exclusive worldwide marketing rights to CCR1 antagonists developed during such research, subject to the payment of product development milestones and running royalties. Forest will be responsible for clinical development of compounds selected during the research phase. The most advanced compound in the research program may be ready to enter Phase I clinical studies within the next 12 months.

**Benicar® Co-Promotion with Sankyo Pharma**: In December 2001, Forest entered into a co-promotion agreement with Sankyo Pharma ("Sankyo") for the co-promotion in the United States of Benicar (olmesartan medoxomil) an angiotensin receptor blocker discovered and developed by Sankyo for the treatment of hypertension. The NDA for Benicar was approved by the FDA in April 2002 and the product was commercially launched by the Sankyo and Forest salesforces in the United States in May 2002.

Pursuant to the co-promotion agreement with Sankyo, Forest and Sankyo will share in the detailing of the product to physicians, hospitals, managed care organizations and other institutional users of pharmaceutical products over a six-year period. Forest will receive co-promotion income once the product becomes profitable on a cumulative basis beginning with the product launch based upon the Company's agreed contribution to the overall co-promotion effort for the six-year period. Thereafter, the Company will receive a reduced share of the profits. The Company expects that the product will become cumulatively profitable during the first half of fiscal 2005.

In August 2003 Forest and Sankyo jointly launched Benicar HCT™, a combination of Benicar and hydrochlorothiazide, a diuretic, which received FDA approval in June 2003. Hypertension is increasingly treated with drugs with different and complementary modes of action and accordingly Forest believes that the inclusion of this combination product in the co-promotion arrangement will enhance overall sales of the Benicar products. According to data published by IMS, an independent prescription audit firm, as of May 21, 2004, Benicar achieved a 9.44% share of total prescriptions in the angiotensin receptor blocker ("ARB") market.

**Lercanidipine**: In November 2000, Forest entered into a license agreement with Recordati, S.p.A., a pharmaceutical company based in Milan, Italy, for the exclusive rights to develop and market lercanidipine in the United States for the treatment of hypertension. Lercanidipine, currently marketed in forty-two countries, belongs to the dihydropyridine calcium channel blocker class of antihypertensives, one of the most widely used classes of antihypertensives. Lercanidipine has been widely studied in clinical trials and was found to have an excellent safety profile and comparable blood pressure lowering effects to other drugs in this class.

Although Forest received an approvable letter from the FDA in August 2002, the FDA did not approve the once-daily dosing regimen as submitted and requested additional data. Subsequently, Forest has reformulated lercanidipine and has begun a clinical program to support the requested dosing regimen. Forest expects to be able to submit the additional data requested by the FDA during fiscal 2008.

**Acamprosate**: In October 2001, Forest entered into a distribution, marketing, trademark license and supply agreement with a subsidiary of Merck KGaA ("Merck") of Darmstadt, Germany, pursuant to which Forest licensed exclusive rights to market acamprosate in the United States for the treatment of alcohol dependence. Acamprosate, developed by Merck, has been marketed in most European countries for several years under the brand name "Campral®." Merck submitted the NDA for acamprosate to the FDA in December 2001.

During fiscal 2003 the FDA determined that the acamprosate NDA was not approvable at this time. Merck has submitted an amendment to the NDA and expects FDA action during the second half of calendar 2004.

**Tiazac®**: Tiazac, licensed from Biovail Corporation and launched in 1996, is Forest's once-daily formulation of diltiazem, used in the treatment of hypertension and angina. In April 2003, the FDA approved a generic formulation of this product distributed by a third party. Forest has also launched a generic version of this product under Forest's license arrangement with Biovail and has discontinued promotional activities with respect to the brand.

**Combunox™**: In October 2002, Forest received an approvable letter from the FDA with respect to Combunox, Forest's combination oxycodone/ibuprofen product being developed for the management of moderate to severe acute pain. The Company submitted its response to the approvable letter in May 2004, and expects an FDA action in response to the information submitted in the second half of fiscal 2005. Forest licenses the United States rights to this product from the British Technology Group.

**Dexloxiglumide**: During fiscal 2004, Forest discontinued the development of dexloxiglumide for the treatment of constipation-predominant irritable bowel syndrome in the United States. The decision was based on the outcome of two placebo-controlled Phase III studies which failed to demonstrate statistically significant results on the studies' primary endpoint. Forest is continuing to evaluate dexloxiglumide, licensed from Rotta Research Laboratorium S.p.A. of Italy, the originator of the compound, for potential development in other gastrointestinal indications.

**Forward Looking Statements**: Except for the historical information contained herein, this report contains forward looking statements that involve a number of risks and uncertainties, including the difficulty of predicting FDA approvals, acceptance and demand for new pharmaceutical products, the impact of competitive products and pricing, the impact of legislative and regulatory developments on the manufacture and marketing of pharmaceutical products and the uncertainty and timing of the development and launch of new pharmaceutical products.

Principal Products

The Company actively promotes in the United States those of its branded products which the Company's management believes have the most potential for growth and which enable its salesforces to concentrate on groups of physicians who are high prescribers of its products. Such products include: Namenda, Forest's NMDA antagonist for the treatment of moderate to severe Alzheimer's disease; Lexapro, Forest's SSRI for the treatment of major depression; and Benicar, an angiotensin receptor blocker for the treatment of hypertension, which the Company co-promotes with Sankyo.

Sales of Lexapro, launched in September 2002, accounted for 41.1% of Forest's sales for the fiscal year ended March 31, 2004 and 11.1% of Forest's sales for the fiscal year ended March 31, 2003.

Sales of Celexa, launched in September 1998, accounted for 41.0% of Forest's sales for the fiscal year ended March 31, 2004 and 65.8% and 69.4%, respectively, of Forest's sales for the fiscal years ended March 31, 2003 and 2002.

Sales of Namenda, launched in March 2004, accounted for 1.7% of Forest's sales for the fiscal year ended March 31, 2004.

Sales of Tiazac, launched in 1996, accounted for 4.8%, 9.1% and 12.1% of sales for the fiscal years ended March 31, 2004, 2003 and 2002, respectively. See "Recent Developments - Tiazac."

Forest's generic line, marketed by the Company's Inwood Laboratories, Inc. subsidiary, includes generic equivalents to certain of the Company's branded products, as well as products using the Company's controlled release

technology.

The Company's United Kingdom and Ireland subsidiaries sell both ethical products requiring a doctor's prescription and over-the-counter preparations. Their most important products include Sudocrem®, a topical preparation for the treatment of diaper rash; Colomycin®, an antibiotic used in the treatment of Cystic Fibrosis; Suscard® and Sustac®, sustained action nitroglycerin tablets in both buccal and oral form used in the treatment of angina pectoris; and Exorex™, used in the treatment of eczema and psoriasis.

Marketing

In the United States, Forest directly markets its products through its domestic salesforces, Forest Pharmaceuticals, Forest Therapeutics, Forest Healthcare, Forest Ethicare and Forest Specialty Sales, which detail products directly to physicians, pharmacies, hospitals, managed care and other healthcare organizations. During the 2004 fiscal year, the Company expanded its salesforce for the launch of the GAD indication of Lexapro and Namenda by 525 persons to approximately 2,825 persons. In the United Kingdom, the Company's Forest Laboratories U.K. subsidiary's salesforce, currently 40 persons, markets its products directly. Forest's products are sold elsewhere through independent distributors.

Competition

The pharmaceutical industry is highly competitive as to the sale of products, research for new or improved products and the development and application of competitive drug formulation and delivery technologies. There are numerous companies in the United States and abroad engaged in the manufacture and sale of both proprietary and generic drugs of the kind sold by Forest. Many of these companies have substantially greater financial resources than Forest. The Company also faces competition for the acquisition or licensing of new product opportunities from other companies. In addition, the marketing of pharmaceutical products is increasingly affected by the growing role of managed care organizations, including pharmaceutical benefit management companies, in the provision of health services. Such organizations negotiate with pharmaceutical manufacturers for highly competitive prices for pharmaceutical products in equivalent therapeutic categories, including certain of the Company's principal promoted products. Failure to be included or to have a preferred position in a managed care organization's drug formulary could result in decreased prescriptions of a manufacturer's products.

Government Regulation

The pharmaceutical industry is subject to comprehensive government regulation which substantially increases the difficulty and cost incurred in obtaining the approval to market newly proposed drug products and maintaining the approval to market existing drugs. In the United States, products developed, manufactured or sold by Forest are subject to regulation by the FDA, principally under the Federal Food, Drug and Cosmetic Act, as well as by other federal and state agencies. The FDA regulates all aspects of the testing, manufacture, safety, labeling, storage, record keeping, advertising and promotion of new and old drugs, including the monitoring of compliance with good manufacturing practice regulations. Non-compliance with applicable requirements can result in fines and other sanctions, including the initiation of product seizures, injunction actions and criminal prosecutions based on practices that violate statutory requirements. In addition, administrative remedies can involve voluntary recall of products as well as the withdrawal of approval of products in accordance with due process procedures. Similar regulations exist in most foreign countries in which Forest's products are manufactured or sold. In many foreign countries, such as the United Kingdom, reimbursement under national health insurance programs frequently require that manufacturers and sellers of pharmaceutical products obtain government approval of initial prices and increases if the ultimate consumer is to be eligible for reimbursement for the cost of such products.

During the past several years, the FDA, in accordance with its standard practice, has conducted a number of inspections of the Company's manufacturing facilities. Following these inspections, the FDA called the Company's

attention to certain "Good Manufacturing Practices" compliance and record keeping deficiencies. Forest has responded to the FDA's comments and has modified procedures to comply with the requests made by the FDA.

The cost of human healthcare products continues to be a subject of investigation and action by governmental agencies, legislative bodies and private organizations in the United States and other countries. In the United States, most states have enacted generic substitution legislation requiring or permitting a dispensing pharmacist to substitute a different manufacturer's version of a drug for the one prescribed. Federal and state governments continue to press efforts to reduce costs of Medicare and Medicaid programs, including restrictions on amounts agencies will reimburse for the use of products. In addition, several states have adopted prescription drug benefit programs which supplement Medicaid programs and are seeking discounts or rebates from pharmaceutical manufacturers to subsidize such programs. Failure to provide such discounts or rebates may lead to restrictions upon the availability of a manufacturer's products in health programs, including Medicaid, run by such states. Under the Omnibus Budget Reconciliation Act of 1990 ("OBRA"), manufacturers must pay certain statutorily-prescribed rebates on Medicaid purchases for reimbursement of prescription drugs under state Medicaid plans. Federal Medicaid reimbursement for drug products of original NDA-holders is denied if less expensive generic versions are available from other manufacturers. In addition, the federal government follows a diagnosis related group ("DRG") payment system for certain institutional services provided under Medicare or Medicaid. The DRG system entitles a healthcare facility to a fixed reimbursement based on discharge diagnoses rather than actual costs incurred in patient treatment, thereby increasing the incentive for the facility to limit or control expenditures for many healthcare products. Under the Prescription Drug User Fee Act of 1992, the FDA has imposed fees on various aspects of the approval, manufacture and sale of prescription drugs.

In April 2003, the Federal Office of the Inspector General published guidance for pharmaceutical manufacturers with respect to compliance programs to assure manufacturer compliance with federal laws and programs relating to healthcare. The Company maintains a compliance program to assure compliance with applicable laws and regulations, as well as the standards of professional bodies governing interactions between pharmaceutical manufacturers and physicians, and believes it is in compliance with all material legal requirements and standards.

During fiscal 2004, the Medicare-Approved Prescription Drug Discount Card and Transitional Assistance Program was established pursuant to the Medicare Prescription Drug, Improvement and Modernization Act of 2003. Under the program, pharmaceutical benefit managers and health programs will offer discounted prices on prescription drugs to qualified Medicare recipients reflecting discounts negotiated with manufacturers. The failure of a manufacturer to offer discounts to these programs could result in reduced use of the manufacturer's products.

In March 2004, the FDA issued a public health advisory that requires companies that manufacture antidepressants, including the Company, to revise their products' labels to include detailed warnings about the potential for suicidal tendencies in patients who take the medications. FDA officials noted that studies have not established a link between suicidal tendencies and such antidepressants and the Company believes that its analysis of clinical data involving Lexapro and Celexa indicates no such link. There can be no assurance that labeling changes required by the latest or subsequent rule making will not have an adverse effect upon the marketing of the Company's antidepressant products.

The Company expects that competing healthcare reform proposals will continue to be introduced and debated. The adoption of any such proposal may entail new regulatory requirements and may affect the marketing of prescription drugs. The Company cannot predict the outcome or effect on the marketing of prescription drug products of the legislative and political process.

Principal Customers

For the years ended March 31, 2004, 2003 and 2002, McKesson Drug Corporation, Cardinal Health, Inc. and AmerisourceBergen Corporation accounted for 28%, 23% and 21%, 25%, 21% and 22%, and 23%, 19% and

23%, respectively, of the Company's net sales. No other customer accounted for 10% or more of Forest's net sales for those fiscal years.

Environmental Standards

Forest anticipates that the effects of compliance with federal, state and local laws and regulations relating to the discharge of materials into the environment will not have any material effect on capital expenditures, earnings or the competitive position of Forest.

Raw Materials

The principal raw materials used by Forest for its various products are purchased in the open market. Most of these materials are obtainable and available from several sources in the United States and elsewhere in the world, although the Company's most important products, including Namenda, Lexapro and Celexa, contain patented or other exclusively manufactured materials available to the Company only through its arrangements with its licensing partners. Forest has not experienced any significant shortages in supplies of such raw materials.

Product Liability Insurance

Forest currently maintains $150 million of product liability coverage per "occurrence" and in the aggregate. Although in the past there have been product liability claims asserted against Forest, none for which Forest has been found liable, there can be no assurance that all potential claims which may be asserted against Forest in the future would be covered by Forest's present insurance.

Research and Development

During the year ended March 31, 2004, Forest spent $246,461,000 for research and development, as compared to $204,883,000 and $157,794,000 in the fiscal years ended March 31, 2003 and 2002, respectively. Included in research and development expense are payments made pursuant to licensing agreements for new product opportunities where safety and efficacy have not yet been demonstrated and accordingly payments made in connection with acquiring the product rights are charged to research and development. Forest's research and development expenditures consist primarily of the conduct of preclinical and clinical studies required to obtain approval of new products, as well as clinical studies designed to further differentiate Forest's products from those of its competitors or to obtain additional labeling indications for its products.

Employees

At March 31, 2004, Forest had a total of 4,967 employees.

Patents and Trademarks

Forest owns or licenses certain U.S. and foreign patents on many of its branded products and products in development, including, but not limited to, Aerobid®, Aerospan®, Lexapro, Tiazac, Cervidil®, Monurol®, Combunox, Namenda, lercanidipine, dexloxiglumide, neramexane and other compounds under development pursuant to license arrangements (see "Recent Developments"), which patents expire through 2014. Celexa is no longer subject to patent protection and its exclusivity under the Hatch-Waxman Act expired in January 2004, at which time third parties became eligible to file for approval of generic equivalents. Lexapro is covered by a United States patent which expires in 2009 and should be subject to a patent term extension until 2012. See "Item 3. Legal Proceedings" for a description of certain challenges to the validity of Forest's Lexapro patent. Forest believes these patents and other rights are or may become of significant benefit to its business. Additionally, Forest owns and licenses certain U.S. patents, and has pending U.S. and foreign patent applications, relating to various aspects of its Synchron® technology

and to other controlled release technology, which patents expire through 2008. Forest believes that these patents are useful in its business; however, there are numerous patents and unpatented technologies owned by others covering other controlled release processes.

Forest owns various trademarks and trade names which it believes are of significant benefit to its business.

Backlog -- Seasonality

Backlog of orders is not considered material to Forest's business prospects. Forest's business is not seasonal in nature.

ITEM 2. PROPERTIES

Forest owns a 150,000 square foot building on 28 acres in Commack, New York. This facility is used for packaging, warehousing, administration and sales training. Forest is currently expanding this facility by 185,000 square feet to accommodate additional packaging and distribution requirements for current and future products and to further expand sales training. The Company anticipates completing this expansion in the second half of calendar 2004. Forest recently purchased a 105,000 square foot warehouse and administrative office facility in Hauppauge, New York, which it was previously leasing.

Forest owns additional buildings of 180,000, 100,000 and 20,000 square feet in Commack, New York and is developing these locations as a research and development complex. Both the 100,000 and 20,000 square foot facilities are operational, and the 180,000 square foot facility (on 11 acres) to be used for research and development and warehousing is expected to become operational in fiscal 2007. Forest also leases an additional 28,000 square foot facility in Hauppauge, New York, for offices and warehousing for its research and development group. Forest recently leased a portion of a hotel facility in Hauppauge, New York for the purpose of housing sales representatives during sales training.

Forest also owns five buildings and leases three buildings in and around Inwood, New York, containing a total of approximately 145,000 square feet. The buildings are used for manufacturing, research and development, warehousing and administration. In addition, Forest leases approximately 59,000 square feet in Farmingdale, New York for use as a clinical laboratory testing facility. Forest leases an additional 57,000 square foot facility in Commack, which is used for Forest's information technology departments.

Forest also leases approximately 166,000 square feet of office space in Jersey City, New Jersey, which is used by certain of its medical, scientific and regulatory personnel.

Forest Pharmaceuticals, Inc. ("FPI"), a wholly-owned subsidiary of the Company, owns two facilities in Cincinnati, Ohio aggregating approximately 140,000 square feet used for manufacturing. In St. Louis, Missouri, FPI owns a 330,000 square foot facility on 26 acres of land. This facility is being used for warehousing, distribution and administration. FPI recently purchased a 40,000 square foot facility near its current distribution center, which will be used as offices. In addition, FPI owns a 22,000 square foot manufacturing facility in St. Louis, Missouri.

Forest Laboratories UK owns an approximately 95,000 square foot complex in the London suburb of Bexley, England, which houses its plant and administrative and central marketing offices.

Forest's Tosara subsidiary owns a 33,000 square foot manufacturing and distribution facility located in an industrial park in Dublin, Ireland. Forest Ireland, a subsidiary of Forest, owns an approximately 130,000 square foot manufacturing and distribution facility located in Dublin, Ireland. The facility is currently used principally for the manufacture of and distribution to the United States of Celexa, Lexapro and Namenda tablets. Forest Ireland recently purchased a 90,000 square foot facility in Dublin which, once it is refurbished, will provide complete redundancy for

the manufacture of Lexapro and Namenda and additional capacity for future products.

Forest presently leases approximately 120,000 square feet of executive office space at 909 Third Avenue, New York, New York. The lease expires in 2010, subject to a five-year renewal option.

Management believes that further purchases or leases of property are likely in order to meet the present and anticipated increases in Forest's overall operations.

Net rentals for leased space for the fiscal year ended March 31, 2004 aggregated approximately $14,790,000 and for the fiscal year ended March 31, 2003 aggregated approximately $11,752,000.

ITEM 3. LEGAL PROCEEDINGS

The Company remains a defendant in actions filed in various federal district courts alleging certain violations of the federal anti-trust laws in the marketing of pharmaceutical products. In each case, the actions were filed against many pharmaceutical manufacturers and suppliers and allege price discrimination and conspiracy to fix prices in the sale of pharmaceutical products. The actions were brought by various pharmacies (both individually and, with respect to certain claims, as a class action) and seek injunctive relief and monetary damages. The Judicial Panel on Multi-District Litigation has ordered these actions coordinated (and, with respect to those actions brought as class actions, consolidated) in the Federal District Court for the Northern District of Illinois (Chicago) under the caption "In re Brand Name Prescription Drugs Antitrust Litigation."

On November 30, 1998, the defendants remaining in the consolidated federal class action (which proceeded to trial beginning in September 1998), including the Company, were granted a directed verdict by the trial court after the plaintiffs had concluded their case. In ruling in favor of the defendants, the trial Judge held that no reasonable jury could reach a verdict in favor of the plaintiffs and stated "the evidence of conspiracy is meager, and the evidence as to individual defendants paltry or non-existent." The Court of Appeals for the Seventh Circuit subsequently affirmed the granting of the directed verdict in the federal class case in favor of the Company.

Following the Seventh Circuit's affirmance of the directed verdict in favor of the Company, the Company has secured the voluntary dismissal of the conspiracy allegations contained in all of the federal cases brought by individual plaintiffs who elected to "opt-out" of the federal class action, which cases were included in the coordinated proceedings, as well as the dismissal of similar conspiracy and price discrimination claims pending in various state courts. The Company, together with other manufacturers, remains a defendant in many of the federal opt-out cases included in the coordinated proceedings to the extent of claims alleging price discrimination in violation of the Robinson-Patman Act. While no discovery or other significant proceedings have been taken to date in respect of such claims, there can be no assurance that the Company will not be required to actively defend such claims or to pay substantial amounts to dispose of such claims.

On January 14, 2003, Forest Pharmaceuticals, Inc., a wholly-owned subsidiary of the Company, was named as a defendant, together with 29 other manufacturers of pharmaceutical products, in an action brought in the United States District Court for the Eastern District of New York by the County of Suffolk, New York, as plaintiff. The action alleges that plaintiff County was overcharged for its share of Medicare and Medicaid drug reimbursement costs as a result of reporting by manufacturers of "Average Wholesale Prices" which did not correspond to actual provider costs of prescription drugs. The action includes counts under the Federal RICO and False Claims Acts, as well as claims arising under state statutes and common law. The action asserts substantially similar claims to other actions (none of which include the Company as a defendant) which have been brought in various Federal District and State Courts by various plaintiffs against pharmaceutical manufacturers and which have been assigned to the United States District Court of the District of Massachusetts under the caption "In re Pharmaceutical Industry AWP Litigation" for coordinated treatment. The action brought by plaintiff has been transferred to the District of Massachusetts for coordination with these multi-district proceedings. Forest has filed a motion to dismiss which is

currently under consideration by the Court. Identical actions naming the Company as a defendant have been filed by the Counties of Westchester and Rockland in New York State, which actions have been transferred to the United States District Court for the District of Massachusetts. These actions are being held in abeyance pending the outcome of Forest's motion to dismiss. The Company believes there is no merit to these actions.

The Company has received a subpoena from the Office of the Inspector General of the Federal Office of Personnel Management requesting documents related to Celexa, a prescription medication approved for the treatment of depression. The subpoena primarily requests documents related to the marketing of Celexa and educational and promotional programs with physicians. The Company believes that other makers of pharmaceutical products for the treatment of various CNS indications have received subpoenas from this office. The Office of Personnel Management is the Federal Government's human resources agency. The Company is cooperating in responding to the subpoena. No claim, litigation or assessment has been asserted in connection with the subpoena.

In September 2003, the Company, together with H. Lundbeck A/S, filed an action for patent infringement against Ivax Pharmaceuticals, Inc. in the United States District Court of the District of Delaware under the caption "Forest Pharmaceuticals, Inc., Forest Laboratories Ireland, Ltd. and H. Lundbeck A/S v. Ivax Pharmaceuticals, Inc." The action is based upon the filing by Ivax with the Food and Drug Administration of an Abbreviated New Drug Application (an "ANDA") for a generic equivalent to the Company's Lexapro brand escitalopram oxalate. The Ivax ANDA seeks approval to market the generic product prior to the expiration of the Company's Lexapro patent which the Company expects to extend until 2012. Ivax has denied that the manufacture or marketing of its generic product, if approved by the FDA, would infringe the Company's patent and has asserted a counterclaim to the effect that the Company's Lexapro patent is invalid.

On May 21, 2004, the Company, together with H. Lundbeck A/S, filed an action for patent infringement against Alphapharma Pty Ltd. in the United States District Court for the Southern District Court of New York under the caption "Forest Laboratories, Inc., Forest Laboratories Ireland, Ltd. and H. Lundbeck A/S v. Alphapharma Pty Ltd." The action is based upon the filing by Alphapharma with the Food and Drug Administration of an Abbreviated New Drug Application (an "ANDA") for a generic equivalent to the Company's Lexapro brand escitalopram oxalate. The Alphapharma ANDA seeks approval to market the generic product prior to the expiration of the Company's Lexapro patent which the Company expects to extend until 2012. Alphapharma has not yet filed its Answer to the Company's Complaint.

The Company believes its patent is valid and intends to vigorously prosecute these actions.

The Company is not subject to any other pending legal proceedings, other than ordinary routine claims incidental to its business.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE

**OF SECURITY HOLDERS**

Not Applicable.

PART II

**ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER**

**MATTERS**

The information required by this item is incorporated by reference to page 44 of the Annual Report.

Forest has never paid cash dividends on its Common Stock and does not expect to pay such dividends in the foreseeable future. Management presently intends to retain all available funds for the development of its business and for use as working capital. Future dividend policy will depend upon Forest's earnings, capital requirements, financial condition and other relevant factors.

ITEM 6. SELECTED FINANCIAL DATA

The information required by this item is incorporated by reference to page 22 of the Annual Report.

ITEM 7. MANAGEMENT'S DISCUSSION AND

**ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The information required by this item is incorporated by reference to pages 15 through 21 of the Annual Report.

ITEM 7A. QUANTITATIVE AND QUALITATIVE

**DISCLOSURES ABOUT MARKET RISK**

The information required by this item is incorporated by reference to page 21 of the Annual Report.

ITEM 8. FINANCIAL STATEMENTS AND

**SUPPLEMENTARY DATA**

The information required by this item is incorporated by reference to pages 23 through 43 of the Annual Report.

ITEM 9. CHANGES IN AND DISAGREEMENTS

**WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

Not Applicable.

ITEM 9A. CONTROLS AND PROCEDURES

As of the end of the period covered by this report, the Company conducted an evaluation, under the supervision and with the participation of the principal executive officer and principal financial officer, of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")). Based on this evaluation, the principal executive officer and principal financial officer concluded that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms. There was no change in the Company's internal control over financial reporting during

the Company's most recently completed fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART III

In accordance with General Instruction G(3), and except for certain of the information called for by Items 10 and 12 which is set forth below, the information called for by Items 10 through 13 of Part III is incorporated by reference from Forest's definitive proxy statement to be filed pursuant to Regulation 14A promulgated under the Securities Exchange Act of 1934 in connection with Forest's 2004 Annual Meeting of Stockholders.

### ITEM 10. DIRECTORS AND OFFICERS OF THE REGISTRANT

The Company has adopted a written code of conduct and ethics that applies to Forest's Chief Executive Officer, Chief Financial Officer and all of Forest's officers and employees and can be found on the Company's website, which is located at www.frx.com. Forest intends to make all required disclosures concerning any amendments to, or waivers from, the code of conduct and ethics on the Company's website.

### ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The following sets forth certain information as of March 31, 2004 with respect to compensation plans of the Company under which securities of the Company may be issued:

Equity Compensation Plan Information

| Plan Category | Number of securities to be issued upon exercise of outstanding options, warrants and rights | Weighted-average exercise price of outstanding options, warrants and rights | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in first column) |
|---|---|---|---|
| Equity compensation plans approved by security holders | 27,305,423 | $28.54 | 5,723,034 |
| Equity | -0- | N/A | -0- |

| | | | |
|---|---|---|---|
| compensation plans not approved by security holders | | | |
| Total | 27,305,423 | $28.54 | 5,723,034 |

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The response to this item is incorporated by reference to the issuer's definitive proxy statement for the 2004 Annual Meeting of Stockholders.

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

(a) 1. Financial statements. The following consolidated financial statements of Forest Laboratories, Inc. and Subsidiaries included in the Annual Report are incorporated by reference herein in Item 8:

Report of Independent Certified Public Accountants

Consolidated balance sheets -
March 31, 2004 and 2003

Consolidated statements of income -
years ended March 31, 2004, 2003 and 2002

Consolidated statements of comprehensive income -
years ended March 31, 2004, 2003 and 2002

Consolidated statements of stockholders' equity -
years ended March 31, 2004, 2003 and 2002

Consolidated statements of cash flows -
years ended March 31, 2004, 2003 and 2002

Notes to consolidated financial statements

2. Financial statement schedules. The following consolidated financial statement schedules of Forest Laboratories, Inc. and Subsidiaries are included herein:



All other schedules for which provision is made in the applicable accounting regulations of the Securities and Exchange Commission are not required under the related instructions or are inapplicable, and therefore have been omitted.

3. Exhibits:

(3)(a) Articles of Incorporation of Forest, as amended. Incorporated by reference from the Current Report on Form 8-K dated March 9, 1981 filed by Forest, from Registration Statement on Form S-1 (Registration No. 2-97792) filed by Forest on May 16, 1985, from Forest's definitive proxy statement filed pursuant to Regulation 14A with respect to Forest's 1987, 1988 and 1993 Annual Meetings of Stockholders and from the Current Report on Form 8-K dated March 15, 1988.

(3)(b) By-laws of Forest. Incorporated by reference to Forest's Current Report on Form 8-K dated October 11, 1994.

(10) Material Contracts

10.1 Benefit Continuation Agreement dated as of December 1, 1989 between Forest and Howard Solomon. Incorporated by reference to Forest's Annual Report on Form 10-K for the fiscal year ended March 31, 1990 (the "1990 l0-K").

10.2 Benefit Continuation Agreement dated as of May 27, 1990 between Forest and Kenneth E. Goodman. Incorporated by reference to the 1990 10-K.

10.3 Benefit Continuation Agreement dated as of April 1, 1995 between Forest and Phillip M. Satow. Incorporated by reference to Forest's Annual Report on Form 10-K for the fiscal year ended March 31, 1995 (the "1995 10-K").

10.4 Employment Agreement dated as of September 30, 1994 by and between Forest and Howard Solomon. Incorporated by reference to 1995 10-K.

10.5

| | |
|---|---|
| | Employment Agreement dated as of September 30, 1994 by and between Forest and Kenneth E. Goodman. Incorporated by reference to the 1995 10-K. |
| 10.6 | Employment Agreement dated as of October 24, 1995 by and between Forest and Dr. Lawrence S. Olanoff. Incorporated by reference to Forest's Annual Report on Form 10-K for the fiscal year ended March 31, 1996 (the "1996 10-K"). |
| 10.7 | Employment Agreement dated June 24, 1998 between Forest and Elaine Hochberg. Incorporated by reference to Forest's Annual Report on Form 10-K for the fiscal year ended March 31, 1998 (the "1998 10-K"). |
| 10.8 | Employment Agreement dated June 21, 1999 between Forest and John E. Eggers. Incorporated by reference to Forest's Annual Report on Form 10-K for the fiscal year ended March 31, 1999 (the "1999 10-K"). |
| 10.9 | Employment Agreement dated January 16, 1995 between Forest and Mary Prehn. Incorporated by reference to the 1998 10-K. |
| 10.10 | Employment Agreement dated November 22, 2000 between Forest and Charles E. Triano. Incorporated by reference to Forest's Annual Report on Form 10-K for the fiscal year ended March 31, 2001. |
| 10.11 | License Agreement dated September 11, 1995 between Biovail Corporation International and Forest. Incorporated by reference to Exhibit No. (C)(2) to Schedule 14D-1 of Forest dated September 18, 1995. |
| 10.12 | License and Supply Agreement dated October 3, 1995 between Forest Laboratories (Ireland) Limited and H. Lundbeck A/S. Incorporated by reference to the 1999 10-K. |
| 10.13 | Co-Promotion Agreement dated December 10, 2001 by and between Sankyo Pharma Inc. and Forest Laboratories, Inc. Incorporated by reference to Forest's Annual Report on form 10-K for the fiscal year ended March 31, 2002 (the "2002 10-K). |
| 10.14 | S-Enantiomer License Agreement dated May 29, 2002 by and between Forest Laboratories (Ireland) Limited and H. Lundbeck A/S. Incorporated by reference to the 2002 10-K. |
| 10.15 | S-Enantiomer Supply Agreement dated May 29, 2002 by and between Forest Laboratories (Ireland) Limited and H. Lundbeck A/S. Incorporated by reference to the 2002 10-K. |
| 10.16 | License and Cooperation Agreement dated June 28, 2000 by and between Merz Pharma GmbH and Forest Laboratories Ireland Limited. |

| | |
|---|---|
| 13 | Portions of the Registrant's 2004 Annual Report to Stockholders. |
| 21 | List of Subsidiaries. |
| 23 | Consent of BDO Seidman, LLP. |
| 31.1 | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2 | Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |

(b) Reports on Form 8-K.

On January 12, 2004, the registrant filed a Report on Form 8-K to report a press release announcing that earnings for the quarter ended December 31, 2003 were expected to exceed consensus estimates.

On January 20, 2004, the registrant filed a Report on Form 8-K to report a press release announcing results of operations for the quarter ended December 31, 2003.

SIGNATURES

Pursuant to the requirements of Section 13 and 15(d) of the Securities Exchange Act of 1934, Forest has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: June 14, 2004

FOREST LABORATORIES, INC.

By: /s/Howard Solomon
Howard Solomon,
Chairman of the Board,
Chief Executive Officer
and Director

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of Forest and in the capacities and on the dates indicated.

PRINCIPAL EXECUTIVE
OFFICERS:

| | | |
|---|---|---|
| /s/ Howard Solomon<br>Howard Solomon | Chairman of the Board, Chief Executive Officer and Director | June 14, 2004 |
| /s/ Kenneth E. Goodman<br>Kenneth E. Goodman | President, Chief Operating Officer and Director | June 14, 2004 |
| PRINCIPAL FINANCIAL AND ACCOUNTING OFFICER: | | |
| /s/ John E. Eggers<br>John E. Eggers | Vice President - Finance and Chief Financial Officer | June 14, 2004 |
| DIRECTORS: | | |
| /s/ William J. Candee, III<br>William J. Candee, III | Director | June 14, 2004 |
| /s/ George S. Cohan<br>George S. Cohan | Director | June 14, 2004 |
| /s/ Dan L. Goldwasser<br>Dan L. Goldwasser | Director | June 14, 2004 |
| /s/ Lester B. Salans<br>Lester B. Salans | Director | June 14, 2004 |
| /s/ Phillip M. Satow<br>Phillip M. Satow | Director | June 14, 2004 |

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS
Board of Directors and Stockholders
Forest Laboratories, Inc.

The audits referred to in our report dated April 16, 2004 relating to the consolidated financial statements of Forest Laboratories Inc. and Subsidiaries, which is referred to in Item 8 of this Form 10-K, include the audit of the accompanying financial statement schedule. This financial statement schedule is the responsibility of the Company's management. Our responsibility is to express an opinion on the financial statement schedule based on our audits.

In our opinion, such financial statement schedule presents fairly, in all material respects, the information set forth

therein.

/s/ BDO Seidman, LLP
BDO Seidman, LLP

New York, New York
April 16, 2004



SCHEDULE II

FOREST LABORATORIES, INC. AND SUBSIDIARIES

VALUATION AND QUALIFYING ACCOUNTS

| Column A | Column B | Column C | Column D | Column E |
|---|---|---|---|---|
| Description | Balance at beginning of period | Additions | Deductions | Balance at end of period |
| Year ended March 31, 2004: | | | | |
| Allowance for doubtful accounts | $16,925,000 | $ 4,246,000 | $ 409,000 (i) | $20,762,000 |
| Allowance for cash discounts | 16,040,000 | 84,826,000 | 85,812,000 (ii) | 15,054,000 |
| Inventory reserve | 23,213,000 | 6,065,000 | 11,901,000 (i) | 17,377,000 |
| Year ended March 31, 2003: | | | | |
| Allowance for doubtful accounts | $13,641,000 | $ 4,415,000 | $ 1,131,000 (i) | $16,925,000 |
| Allowance for cash discounts | 13,466,000 | 66,734,000 | 64,160,000 (ii) | 16,040,000 |
| Inventory reserve | 15,846,000 | 9,606,000 | 2,239,000 (i) | 23,213,000 |
| Year ended March 31, 2002: | | | | |
| Allowance for doubtful accounts | $11,123,000 | $ 2,920,000 | $ 402,000 (i) | $13,641,000 |
| Allowance for cash discounts | 8,665,000 | 47,870,000 | 43,069,000 (ii) | 13,466,000 |

| | | | | | |
|---|---|---|---|---|---|
| Inventory reserve | 12,949,000 | 7,110,000 | 4,213,000 | (i) | 15,846,000 |

(i) Represents actual amounts written off.

(ii) Represents cash discounts given.



FOREST LABORATORIES, INC. AND SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED MARCH 31, 2004, 2003 AND 2002

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors and Stockholders
Forest Laboratories, Inc.
New York, New York

We have audited the accompanying consolidated balance sheets of Forest Laboratories, Inc. and Subsidiaries as of March 31, 2004 and 2003, and the related consolidated statements of income, comprehensive income, stockholders' equity and cash flows for each of the three years in the period ended March 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Forest Laboratories, Inc. and Subsidiaries as of March 31, 2004 and 2003, and the results of their operations and their cash flows for each of the three years in the period ended March 31, 2004 in conformity with accounting principles generally accepted in the United States of America.

/s/ BDO Seidman, LLP

BDO Seidman, LLP

New York, New York
April 16, 2004

FOREST LABORATORIES, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(*In thousands*)

| | MARCH 31, | |
|---|---|---|
| | 2004 | 2003 |
| Assets | | |
| Current assets: | | |
| Cash (including cash equivalent investments of $1,724,942 in 2004 and $1,263,156 in 2003) | $1,726,558 | $1,265,508 |
| Marketable securities | 66,064 | 176,338 |
| Accounts receivable, less allowance for doubtful accounts of $20,762 in 2004 and $16,925 in 2003 | 287,618 | 192,067 |
| Inventories, net | 610,182 | 452,886 |
| Deferred income taxes | 205,071 | 156,957 |
| | 20,741 | 11,577 |
| Other current assets | | |
| | 2,916,234 | 2,255,333 |
| Total current assets | | |
| | 337,890 | 114,639 |
| Marketable securities | | |

| | | |
|---|---|---|
| Property, plant and equipment: | | |
| Land and buildings | 253,922 | 174,725 |
| | 150,160 | 130,093 |
| Machinery, equipment and other | | |
| | 404,082 | 304,818 |
| | 106,125 | 86,820 |
| Less accumulated depreciation | | |
| | 297,957 | 217,998 |
| Other assets: | | |
| Goodwill | 14,965 | 14,965 |
| License agreements, product rights and other intangibles, net | 274,835 | 279,171 |
| Deferred income taxes | 16,387 | 17,627 |
| | 4,468 | 18,374 |
| Other | | |
| | 310,655 | 330,137 |
| | $3,862,736 | $2,918,107 |

See accompanying notes to consolidated financial statements.

FOREST LABORATORIES, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
*(In thousands, except for par values)*

| | MARCH 31, | |
|---|---|---|
| | 2004 | 2003 |
| Liabilities and Stockholders' Equity | | |

| | | |
|---|---|---|
| Current liabilities: | | |
| Accounts payable | $ 159,798 | $ 151,719 |
| Accrued expenses | 321,564 | 245,240 |
| | 123,392 | 167,438 |
| Income taxes payable | | |
| | 604,754 | 564,397 |
| Total current liabilities | | |
| | 2,118 | 1,892 |
| Deferred income taxes | | |
| Commitments and contingencies | | |
| Stockholders' equity: | | |
| Series A junior participating preferred stock, $1.00 par; shares authorized 1,000; no shares issued or outstanding | | |
| Common stock $.10 par; shares authorized 500,000; issued 405,144 shares in 2004 and 399,011 shares in 2003 | 40,514 | 39,901 |
| Additional paid-in capital | 846,297 | 687,905 |
| Retained earnings | 2,655,934 | 1,920,060 |
| | | ( 3,429) |
| Accumulated other comprehensive income (loss) | 10,324 | |
| Treasury stock, at cost (35,617 shares in 2004 and 35,539 shares in 2003) | ( 297,205) | ( 292,619) |
| | 3,255,864 | 2,351,818 |
| | $3,862,736 | $2,918,107 |
| | ======== | ======== |

See accompanying notes to consolidated financial statements.

FOREST LABORATORIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
*(In thousands, except per share data)*

| | YEARS ENDED MARCH 31, | | |
|---|---|---|---|
| | 2004 | 2003 | 2002 |
| Net sales | $2,650,432 | $2,206,706 | $1,566,626 |
| | 29,842 | 39,100 | 35,198 |
| Other income | | | |
| | 2,680,274 | 2,245,806 | 1,601,824 |
| Costs and expenses: | | | |
| Cost of sales | 608,474 | 504,922 | 371,061 |
| Selling, general and administrative | 888,517 | 715,432 | 602,791 |
| | 246,461 | 204,883 | 157,794 |
| Research and development | | | |
| | 1,743,452 | 1,425,237 | 1,131,646 |
| Income before income tax expense | 936,822 | 820,569 | 470,178 |
| | 200,948 | 198,581 | 132,224 |
| Income tax expense | | | |
| Net income | $ 735,874 | $ 621,988 | $ 337,954 |
| Net income per common and common equivalent share: | | | |
| Basic | $2.01 | $1.72 | $0.95 |
| Diluted | $1.95 | $1.66 | $0.91 |

| | | | |
|---|---|---|---|
| Weighted average number of common and common equivalent shares outstanding: | | | |
| Basic | 365,447 | 360,874 | 355,390 |
| Diluted | 376,779 | 373,702 | 370,484 |

See accompanying notes to consolidated financial statements.

FOREST LABORATORIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
*(In thousands)*

| | YEARS ENDED MARCH 31, | | |
|---|---|---|---|
| | 2004 | 2003 | 2002 |
| Net income | $735,874 | $621,988 | $337,954 |
| Other comprehensive income (loss), net of tax: | | | |
| Foreign currency translation gains (losses) | 14,339 | 17,169 | ( 424) |
| Unrealized gains (losses) on securities: | | | |
| Unrealized holding gain (loss) arising during the period | ( 586) | 2,692 | ( 3,293) |
| Other comprehensive income (loss) | 13,753 | 19,861 | ( 3,717) |
| Comprehensive income | $749,627 | $641,849 | $334,237 |

See accompanying notes to consolidated financial statements.

FOREST LABORATORIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
YEARS ENDED MARCH 31, 2004, 2003 AND 2002

(In thousands)

| | Common stock | | Additional paid-in | Retained | Accumulated other comprehensive | Treasury stock | |
|---|---|---|---|---|---|---|---|
| | Shares | Amount | capital | earnings | income (loss) | Shares | Amount |
| Balance, March 31, 2001 | 388,653 | $38,865 | $528,989 | $ 960,118 | ($19,573) | 35,451 | $286,285 |
| Shares issued upon exercise of stock options | 5,356 | 536 | 34,216 | | | | |
| Treasury stock acquired from employees upon exercise of stock options | | | | | | 46 | 3,557 |
| Tax benefit related to stock options exercised by employees | | | 37,543 | | | | |
| Other comprehensive loss | | | | | ( 3,717) | | |
| Net income | | | | 337,954 | | | |
| Balance, March 31, 2002 | 394,009 | 39,401 | 600,748 | 1,298,072 | ( 23,290) | 35,497 | 289,842 |
| Shares issued upon exercise of stock options | 5,002 | 500 | 42,172 | | | | |
| Treasury stock acquired from employees upon exercise of stock options | | | | | | 42 | 2,777 |
| Tax benefit related to stock options exercised by employees | | | 44,985 | | | | |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Other comprehensive income | | | | | 19,861 | | |
| Net income | | | | 621,988 | | | |
| Balance, March 31, 2003 | 399,011 | 39,901 | 687,905 | 1,920,060 | ( 3,429) | 35,539 | 292,619 |
| Shares issued upon exercise of stock options | 6,133 | 613 | 72,333 | | | | |
| Treasury stock acquired from employees upon exercise of stock options | | | | | | 78 | 4,586 |
| Tax benefit related to stock options exercised by employees | | | 86,059 | | | | |
| Other comprehensive income | | | | | 13,753 | | |
| Net income | | | | 735,874 | | | |
| Balance, March 31, 2004 | 405,144 | $40,514 | $846,297 | $2,655,934 | $10,324 | 35,617 | $297,205 |

See accompanying notes to consolidated financial statements.

FOREST LABORATORIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(*In thousands*)

| | YEARS ENDED MARCH 31, | | |
|---|---|---|---|
| | 2004 | 2003 | 2002 |
| Cash flows from operating activities: | | | |
| Net income | $ 735,874 | $ 621,988 | $337,954 |

| | | | |
|---|---|---|---|
| Adjustments to reconcile net income to | | | |
| net cash provided by operating activities: | | | |
| Depreciation | 22,191 | 21,119 | 14,320 |
| Amortization, impairments and write-offs | 37,367 | 30,442 | 40,308 |
| Deferred income tax benefit | ( 10,880) | ( 75,338) | ( 21,534) |
| Foreign currency translation loss (gain) | 1,023 | 147 | ( 667) |
| Tax benefit realized from the exercise | | | |
| of stock options by employees | 50,291 | 52,889 | 28,188 |
| Net change in operating assets and liabilities: | | | |
| Decrease (increase) in: | | | |
| Accounts receivable, net | ( 95,551) | ( 75,777) | ( 699) |
| Inventories, net | ( 157,296) | ( 104,671) | ( 84,258) |
| Refundable income taxes | | 12,733 | 12,291 |
| Other current assets | ( 9,164) | 4,066 | ( 5,696) |
| Increase (decrease) in: | | | |
| Accounts payable | 8,079 | 72,323 | 37,475 |
| Accrued expenses | 76,324 | 80,990 | 25,112 |
| Income taxes payable | ( 44,046) | 86,116 | 38,763 |
| | 13,906 | 1,358 | 4,927 |
| Decrease in other assets | | | |
| | 628,118 | 728,385 | 426,484 |
| Net cash provided by operating activities | | | |
| Cash flows from investing activities: | | | |
| Purchase of property, plant and equipment, net | ( 101,511) | ( 79,574) | ( 36,446) |
| Purchase of marketable securities | ( 862,268) | ( 741,015) | ( 680,467) |
| Redemption of marketable securities | 749,291 | 883,045 | 373,635 |
| Purchase of license agreements, product | | | |
| rights and other intangibles | ( 32,759) | ( 43,960) | ( 31,045) |
| Net cash provided by (used in) | | | |
| | ( 247,247) | 18,496 | ( 374,323) |
| investing activities | | | |
| Cash flows from financing activities: | | | |
| Net proceeds from common stock options | | | |
| | 68,360 | 39,895 | 31,195 |
| exercised by employees under stock option plans | | | |

| | | | |
|---|---|---|---|
| | 11,819 | 18,871 | ( 3,044) |
| Effect of exchange rate changes on cash | | | |
| Increase in cash and cash equivalents | 461,050 | 805,647 | 80,312 |
| | 1,265,508 | 459,861 | 379,549 |
| Cash and cash equivalents, beginning of year | | | |
| Cash and cash equivalents, end of year | $1,726,558 | $1,265,508 | $459,861 |
| | ======== | ======== | ======= |

See accompanying notes to consolidated financial statements.

FOREST LABORATORIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(*In thousands*)

| | YEARS ENDED MARCH 31, | | |
|---|---|---|---|
| | 2004 | 2003 | 2002 |
| Supplemental disclosures of cash flow information: | | | |
| Cash paid during the year for: | | | |
| Income taxes | $205,506 | $122,531 | $74,977 |
| | ======= | ======= | ====== |

See accompanying notes to consolidated financial statements.

FOREST LABORATORIES, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of significant accounting policies:

Basis of consolidation:

The consolidated financial statements include the accounts of Forest Laboratories, Inc. (the "Company") and its subsidiaries, all of which are wholly-owned. All significant intercompany accounts and transactions have been eliminated.

Foreign currency translation:

An Irish subsidiary of the Company reports its financial position and results of operations in the reporting currency of the Company. The financial position and results of operations of the Company's other foreign subsidiaries, which in the aggregate are immaterial, are determined using the respective local currency.

Cash equivalents:

Cash equivalents consist of short-term, highly liquid investments (primarily municipal bonds with interest rates that are re-set monthly) which are readily convertible into cash at par value (cost).

Inventories:

Inventories are stated at the lower of cost or market, with cost determined on the first-in, first-out basis.

Marketable securities:

Marketable securities, which are all accounted for as available-for-sale, are stated at fair value in accordance with Statement of Financial Accounting Standards No. 115, "Accounting for Certain Investments in Debt and Equity Securities," and consist of investments in municipal bonds maturing through 2006.

Accounts receivable and credit policies

**:** The carrying amount of accounts receivable is reduced by a valuation allowance that reflects management's best estimate of the amounts that will not be collected. In addition to reviewing delinquent accounts receivable, management considers many factors in estimating its general allowance, including historical data, experience, customer types, credit worthiness and economic trends. From time to time, management may adjust its assumptions for anticipated changes in any of those or other factors expected to affect collectability.

Property, plant and equipment and depreciation:

Property, plant and equipment are stated at cost. Depreciation is provided primarily by the straight-line method over the following estimated useful lives:

| | Years |
|---|---|
| Buildings and improvements | 10-40 |
| Machinery, equipment and other | 3-10 |

Leasehold improvements are amortized over the lesser of the useful life of the assets or the lease term.

Goodwill and other intangible assets:

In accordance with Statements of Financial Accounting Standards No. 141 ("SFAS 141"), "Business Combinations," and No. 142 ("SFAS 142"), "Goodwill and Other Intangible Assets", goodwill and intangible assets deemed to have indefinite lives are no longer amortized but are subject to annual impairment tests. Goodwill impairment tests require the comparison of the fair value and carrying value of reporting units. Measuring fair value of a reporting unit is generally based on valuation techniques using multiples of sales or earnings, unless supportable information is

available for using a present value technique, such as estimates of future cash flows. The Company assesses the potential impairment of goodwill annually and on an interim basis whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

Revenue recognition:

Revenues are recorded in the period the merchandise is shipped. Provisions for estimated sales allowances, returns, rebates and other pricing adjustments are accrued at the time revenues are recognized as a direct reduction of such revenue. The accruals are estimated based on available information regarding the portion of sales on which rebates and discounts can be earned, adjusted as appropriate for specific known events, and the prevailing contractual discount rates. Provisions are reflected either as a direct reduction to accounts receivable or, to the extent that they are due to entities other than customers, as accrued expense. Adjustments to estimates, which have not been material, are recorded when customer credits are issued or payments made to third parties.

Shipping and handling costs:

Presently, the Company does not charge its customers for any freight costs. The amounts of such costs are included in selling, general and administrative expenses and are not material.

Research and development:

Expenditures for research and development, including licensing fees of early-stage development products, are charged to expense as incurred.

Savings and profit sharing plan:

Substantially all non-bargaining unit employees of the Company's domestic subsidiaries may participate in the savings and profit sharing plan after becoming eligible (as defined). Profit sharing contributions are primarily at the discretion of the Company. The savings plan contributions include a matching contribution made by the Company. Savings and profit sharing contributions amounted to approximately $19,500,000, $14,600,000 and $11,000,000 for fiscal years 2004, 2003 and 2002, respectively.

Earnings per share:

Basic earnings per share includes no dilution and is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflect, in periods in which they have a dilutive effect, the effect of common shares issuable upon exercise of stock options and warrants. The two-for-one stock split effected as a 100% stock dividend in December 2002 has been reflected retroactively for all outstanding common stock, stock options and warrants.

Accumulated other comprehensive income (loss):

Other comprehensive income (loss) refers to revenues, expenses, gains and losses that under generally accepted accounting principles are excluded from net income as these amounts are recorded directly as an adjustment to stockholders' equity. Accumulated other comprehensive income (loss) is comprised of the cumulative effects of foreign currency translation and unrealized gains (losses) on securities which amounted to approximately $10,782,000 and ($458,000) at March 31, 2004 and ($3,557,000) and $128,000 at March 31, 2003.

Income taxes:

The Company accounts for income taxes using the liability method. Under the liability method, deferred income taxes are provided on the differences in bases of assets and liabilities between financial reporting and tax returns using enacted tax rates.

Use of estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The Company reviews all significant estimates affecting the financial statements on a recurring basis and records the effect of any adjustments when necessary.

Long-lived assets:

Long-lived assets, such as intangible assets, property and equipment and certain sundry assets, are evaluated for impairment periodically or when events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable through the estimated undiscounted future cash flows from the use of these assets. When any such impairment exists, the related assets will be written down to fair value.

Stock-based compensation:

The Company accounts for its stock option awards to employees under the intrinsic value based method of accounting prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." Under the intrinsic value based method, compensation cost is the excess, if any, of the quoted market price of the stock at grant date or other measurement date over the amount an employee must pay to acquire the stock. The Company makes pro forma disclosures of net income and earnings per share as if the fair value based method of accounting had been applied as required by Statement of Financial Accounting Standards No. 123 ("SFAS 123"), "Accounting for Stock-Based Compensation." The Company has never granted options below market price on the date of grant.

SFAS 123 requires the Company to provide pro forma information regarding net income and earnings per share as if compensation cost for the Company's stock option plans had been determined in accordance with the fair value of each stock option at the grant date by using the Black-Scholes option-pricing model with the following weighted average assumptions used for grants: dividend yield of zero for all three fiscal years; expected volatility of 29.23% in fiscal 2004, 31.29% in fiscal 2003 and 27.62% in fiscal 2002; risk-free interest rates of 4.5% in fiscal 2004, 4.3% in fiscal 2003 and 5.4% in fiscal 2002; and expected lives of 5 to 10 years for all three fiscal years.

Under the accounting provisions of SFAS 123, the Company's net income and earnings per share would have been reduced to the pro forma amounts indicated below:

| Years ended March 31, (In thousands, except per share data) | 2004 | 2003 | 2002 |
|---|---|---|---|
| Net income: | | | |
| As reported | $735,874 | $621,988 | $337,954 |
| Deduct: Total stock-based employee compensation expense determined under fair value method | ( 39,021) | ( 32,594) | ( 65,659) |
| Pro forma | $696,853 | $589,394 | $272,295 |
| | ======= | ======= | ======= |
| Net income per common share: | | | |

| | | | |
|---|---|---|---|
| Basic: | | | |
| As reported | $2.01 | $1.72 | $0.95 |
| Pro forma | $1.91 | $1.63 | $0.77 |
| Diluted: | | | |
| As reported | $1.95 | $1.66 | $0.91 |
| Pro forma | $1.85 | $1.58 | $0.73 |

Fair value of financial instruments:

The carrying amounts of cash, accounts receivable, accounts payable, accrued expenses and income taxes payable are reasonable estimates of their fair value because of the short maturity of these items.

Recent accounting standards:

In April 2003, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 149 ("SFAS 149"), "Amendment of Statement 133 ("SFAS 133") on Derivative Instruments and Hedging Activities." SFAS 149 amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities under SFAS 133. This statement is generally effective for contracts entered into or modified after June 30, 2003 and for hedging relationships designated after June 30, 2003. Presently, the company does not utilize any derivative instruments and only has minimal hedging activities.

2. Earnings per share

:

A reconciliation of shares used in calculating basic and diluted earnings per share follows:

| Years ended March 31, (In thousands) | 2004 | 2003 | 2002 |
|---|---|---|---|
| Basic | 365,447 | 360,874 | 355,390 |
| Effect of assumed conversion of employee stock options and warrants | 11,332 | 12,828 | 15,094 |
| Diluted | 376,779 | 373,702 | 370,484 |

Options to purchase approximately 1,604,800, 3,110,600 and 4,591,600 shares of common stock at exercise prices ranging from $38.15 to $76.66 per share were outstanding during a portion of fiscal 2004, 2003 and 2002, respectively, but were not included in the computation of diluted earnings per share because they were anti-dilutive. These options expire through 2014.

3. Business operations:

The Company and its subsidiaries, which are located in the United States, Ireland and the United Kingdom, manufacture and market ethical and other pharmaceutical products. The Company operates in only one segment. Sales are made primarily in the United States and European markets. The net sales and long-lived assets for the years ended March 31, 2004, 2003 and 2002, are from the Company's or one of its subsidiaries' country of origin, as follows:

| (In thousands) | 2004 | | 2003 | | 2002 | |
|---|---|---|---|---|---|---|
| | Net sales | Long-lived assets | Net sales | Long-lived assets | Net sales | Long-lived assets |
| United States | $2,604,479 | $446,499 | $2,167,021 | $420,760 | $1,531,100 | $347,026 |
| Ireland | 7,331 | 134,658 | 7,152 | 106,159 | 6,019 | 108,517 |
| United Kingdom | 38,622 | 11,068 | 32,533 | 3,589 | 29,507 | 3,507 |
| | $2,650,432 | $592,225 | $2,206,706 | $530,508 | $1,566,626 | $459,050 |

Net sales exclude sales between the Company and its subsidiaries.

For the years ended March 31, 2004, 2003 and 2002, McKesson Corporation, Cardinal Health, Inc. and AmerisourceBergen Corporation accounted for 28%, 23% and 21%, 25%, 21% and 22%, and 23%, 19% and 23%, respectively, of the Company's net sales.

The Company's antidepressant franchise consisting of Lexapro®, a selective serotonin reuptake inhibitor ("SSRI") for the treatment of depression, launched in September 2002 and Celexa®, an SSRI launched in September 1998, accounted for 82%, 77% and 69% of the Company's net sales for the years ended March 31, 2004, 2003 and 2002, respectively.

4. Inventories:

Inventories, net of reserves for obsolescence, consist of the following:

| March 31, | 2004 | 2003 |
|---|---|---|
| *(In thousands)* | | |
| Raw materials | $359,075 | $101,607 |
| Work in process | 40,982 | 38,190 |
| Finished goods | 210,125 | 313,089 |
| | $610,182 | $452,886 |

5. Marketable securities

:

The debt security composition of the investment portfolio at March 31 was:

| (In thousands) | Cost | Gross unrealized gains | Gross unrealized losses | Market value |
|---|---|---|---|---|
| 2004 | | | | |
| Federal, state and local obligations | $404,412 | | ($458) | $403,954 |
| 2003 | | | | |
| Federal, state and local obligations | $290,849 | $128 | | $290,977 |

The contractual maturities of debt securities at March 31, 2004 consist of the following:

| *(In thousands)* | Cost | Fair value |
|---|---|---|
| Less than one year | $ 66,607 | $ 66,064 |
| One to two years | 337,805 | 337,890 |
| | $404,412 | $403,954 |

The net unrealized holding loss of approximately $458,000 at March 31, 2004, as well as the net unrealized holding gain of approximately $128,000 at March 31, 2003 are included in Stockholders' equity: Accumulated other comprehensive income (loss).

6. Intangible assets:

License agreements, product rights and other intangibles consist of the following:

| (In thousands, except for amortization periods which are stated in years) | | March 31, 2004 | | March 31, 2003 | |
|---|---|---|---|---|---|
| | Weighted average amortization period | Gross carrying amount | Accumulated amortization | Gross carrying amount | Accumulated amortization |
| Amortized intangible assets: | | | | | |
| License agreements | 14 | $213,709 | $ 75,842 | $193,709 | $ 64,200 |
| Product rights | 14 | 81,959 | 13,498 | 81,473 | 12,463 |
| Buy-out of royalty agreements | 9 | 95,061 | 48,744 | 95,061 | 39,612 |
| Trade names | 20 | 34,190 | 15,997 | 34,190 | 13,842 |
| Non-compete agreements | 9 | 22,987 | 22,875 | 22,987 | 22,064 |
| Other | 2 | 8,848 | 4,963 | 8,847 | 4,915 |
| Total | 11 | $456,754 | $181,919 | $436,267 | $157,096 |

Amortization of license agreements, product rights and other intangibles for fiscal years ended March 2004, 2003 and 2002 amounted to approximately $37,367,000, $30,442,000 and $40,308,000, respectively. The annual amortization expense expected for fiscal years 2005 through 2009 is $29,866,000, $31,981,000, $32,090,034, $32,287,000 and $29,864,000, respectively.

During fiscal years 2004 and 2003, the Company determined that certain product rights were impaired due to a significant reduction in sales of those products because of heightened competition. These impairments amounted to $2,054,000 in fiscal 2004 and $5,000,000 in fiscal 2003, and are included in amortization expense. During fiscal 2004 the Company also announced that it had discontinued development of dexloxiglumide for irritable bowel syndrome ("IBS"), causing a write-off of the product right of $12,545,000 to research and development expense.

License agreements:

During fiscal year 2004, the Company made a $20,000,000 milestone payment to Merz Pharma GmbH upon FDA approval of Namenda™ (memantine) for the treatment of moderate to severe Alzheimer's disease. The cost of this agreement is being amortized using the straight-line method over the estimated life of the product.

Product rights:

In fiscal 2004 the Company made a milestone payment of $5,000,000 to Sankyo Pharma upon the launch of Benicar HCT™. In December 2001, the Company signed a marketing agreement with Sankyo Pharma to co-promote Benicar® for the treatment of hypertension. The Company will co-promote the product for a period of six years and receive a share of the product profits during that period, as defined. The Company will receive a reduced share of the product profits thereafter. Benicar was commercially launched in the first quarter of fiscal 2003, at which time the Company paid Sankyo $43,960,000. The costs incurred for Benicar are included in product rights and will be amortized in the future based on estimated revenues.

Marketing agreements:

In January 2004, the Company entered into a marketing agreement with Cypress Bioscience, Inc. for the development and marketing of milnacipran in the United States. Milnacipran is currently being evaluated in a Phase III program for the treatment of Fibromyalgia Syndrome ("FMS"). The Company made an initial payment of $25,000,000 during the year which was recorded to research and development expense.

In March 2004, the Company entered into a collaboration agreement with ChemoCentryx, Inc. to develop and commercialize novel small molecule therapeutics for autoimmune and inflammatory diseases such as rheumatoid arthritis and multiple sclerosis. Under the terms of the agreement, Forest will license on a worldwide basis small molecule development candidates discovered by ChemoCentryx, and will take the lead in the clinical development and commercialization of the drugs. The Company made an initial payment of $10,000,000 during the year which was recorded to research and development expense.

7. Accrued expenses:

Accrued expenses consist of the following:

| March 31, (In thousands) | 2004 | 2003 |
|---|---|---|
| Employee compensation and other benefits | $ 83,558 | $ 69,972 |
| Managed care and Medicaid rebates | 185,854 | 123,984 |
| Clinical research and development costs | 31,103 | 31,814 |
| Other | 21,049 | 19,470 |
| | $321,564 | $245,240 |

8. Commitments

:

Leases:

The Company leases manufacturing, office and warehouse facilities, equipment and automobiles under operating leases expiring through 2018. Rent expense approximated $32,212,000, $25,843,000 and $18,802,000 for fiscal years

ended March 31, 2004, 2003 and 2002, respectively.

Future minimum rental payments under noncancellable leases are as follows:

| Year ending March 31, (In thousands) | |
|---|---|
| 2005 | $ 29,886 |
| 2006 | 23,880 |
| 2007 | 18,940 |
| 2008 | 13,482 |
| 2009 | 13,580 |
| Thereafter | 68,450 |
| | $168,218 |

Royalty agreements:

The Company has royalty agreements on certain of its licensed products. Royalties are paid based on a percentage of sales, as defined. For fiscal years ended March 31, 2004, 2003 and 2002, royalties amounted to $10,406,000, $22,247,000 and $19,938,000, respectively.

License agreements

: The Company has entered into several license agreements for products currently under development. The Company may be obligated in future periods to pay additional amounts subject to the achievement of certain product milestones, as defined.

9. Stockholders' equity:

Preferred stock purchase rights:

On September 30, 1994, the Company's Board of Directors declared a dividend of one preferred share purchase right ("Right") for each outstanding share of the Company's common stock, par value $.10 per share. Each Right will entitle the holder to buy one eighth of one-hundredth of a share of authorized Series A Junior Participating Preferred Stock, par value $1.00 per share ("Series A Preferred Stock") at an exercise price of $250 per Right, subject to adjustment. Prior to becoming exercisable, the Rights are evidenced by the certificates representing the common stock and may not be traded apart from the common stock. The Rights become exercisable on the tenth day after public announcements that a person or group has acquired, or obtained the right to acquire, 20% or more of the Company's outstanding common stock, or an announcement of a tender offer that would result in a beneficial ownership by a person or group of 20% or more of the Company's common stock.

If, after the Rights become exercisable, the Company is a party to certain merger or business combination transactions, or transfers 50% or more of its assets or earning power, or if an acquirer engages in certain self-dealing transactions, each Right (except for those held by the acquirer) will entitle its holder to buy a number of shares of the Company's Series A Preferred Stock or, in certain circumstances, a number of shares of the acquiring company's common stock, in either case having a value equal to two-and-one-half times the exercise price of the Right. The Rights may be redeemed by the Company at any time up to ten days after a person or group acquires 20% or more of the Company's common stock at a redemption price of $.001 per Right. The Rights will expire on September 30, 2004.

The Company has reserved 900,000 shares of Series A Preferred Stock for the exercise of the Rights.

Stock options:

The Company has various Employee Stock Option Plans whereby options to purchase an aggregate of 52,000,000 shares of common stock have been or remain to be issued to employees of the Company and its subsidiaries at prices not less than the fair market value of the common stock at the date of grant. Both incentive and non-qualified options may be issued under the plans. The options are exercisable for five to ten years from the date of issuance.

The following table summarizes information about stock options outstanding at March 31, 2004:

| | Options outstanding | | | Options exercisable | |
|---|---|---|---|---|---|
| Range of exercise prices | Number outstanding | Weighted average remaining contractual life | Weighted average exercise price | Number exercisable | Weighted average exercise price |
| $ 4.55 to $30.00 | 12,240,895 | 3.2 | $12.89 | 9,158,985 | $11.23 |
| 30.01 to 50.00 | 13,011,852 | 5.4 | 38.98 | 6,430,506 | 37.03 |
| 50.01 to 76.66 | 1,921,220 | 6.8 | 59.13 | 19,155 | 53.23 |
| | 27,173,967 | 4.5 | $28.65 | 15,608,646 | $21.91 |

Transactions under the stock option plans are summarized as follows:

| | Shares | Weighted average exercise price |
|---|---|---|
| Shares under option at March 31, 2001 (at $3.71 to $33.46 per share) | 33,973,276 | $13.44 |
| Granted (at $31.43 to $41.49 per share) | 4,884,100 | 38.48 |
| Exercised (at $3.71 to $33.46 per share) | ( 5,402,722) | 6.44 |
| Forfeited | ( 782,920) | 21.09 |
| Shares under option at March 31, 2002 (at $3.71 to $41.49 per share) | 32,671,734 | 18.18 |
| Granted (at $35.86 to $53.23 per share) | 4,516,200 | 44.78 |
| Exercised (at $3.71 to $41.49 per share) | ( 5,002,043) | 8.44 |
| Forfeited | ( 662,539) | 29.43 |
| Shares under option at March 31, 2003 (at $3.75 to $53.23 per share) | 31,523,352 | 23.33 |
| Granted (at $43.30 to $76.66 per share) | 2,503,550 | 54.65 |
| Exercised (at $3.75 to $53.23 per share) | ( 6,133,451) | 11.61 |
| Forfeited | ( 719,484) | 36.23 |

| | | |
|---|---|---|
| Shares under option at March 31, 2004 | | |
| (at $4.55 to $76.66 per share) | 27,173,967 | $28.65 |
| | ======== | |
| Options exercisable at March 31: | | |
| 2002 | 18,355,342 | $14.27 |
| 2003 | 17,674,627 | 16.51 |
| 2004 | 15,608,646 | 21.91 |
| | | |
| Weighted average fair value of options granted during: | | |
| 2002 | | $15.32 |
| 2003 | | 18.81 |
| 2004 | | 20.89 |

At March 31, 2004, 5,723,034 shares were available for grant.

In connection with the acquisition of product rights in fiscal 1995, the Company issued 2,240,000 warrants, which expire on July 7, 2004, at an exercise price of $5.72 per share, which was equal to the then fair market value of the Company's common stock. As of March 31, 2004, 131,456 warrants remain outstanding.

10. Contingencies:

The Company remains a defendant in actions filed in various federal district courts alleging certain violations of the federal anti-trust laws in the marketing of pharmaceutical products. In each case, the actions were filed against many pharmaceutical manufacturers and suppliers and allege price discrimination and conspiracy to fix prices in the sale of pharmaceutical products. The actions were brought by various pharmacies (both individually and, with respect to certain claims, as a class action) and seek injunctive relief and monetary damages. The Judicial Panel on Multi-District Litigation has ordered these actions coordinated (and, with respect to those actions brought as class actions, consolidated) in the Federal District Court for the Northern District of Illinois (Chicago) under the caption "In re Brand Name Prescription Drugs Antitrust Litigation."

On November 30, 1998, the defendants remaining in the consolidated federal class action (which proceeded to trial beginning in September 1998), including the Company, were granted a directed verdict by the trial court after the plaintiffs had concluded their case. In ruling in favor of the defendants, the trial Judge held that no reasonable jury could reach a verdict in favor of the plaintiffs and stated "the evidence of conspiracy is meager, and the evidence as to individual defendants paltry or non-existent." The Court of Appeals for the Seventh Circuit subsequently affirmed the granting of the directed verdict in the federal class case in favor of the Company.

Following the Seventh Circuit's affirmance of the directed verdict in favor of the Company, the Company has secured the voluntary dismissal of the conspiracy allegations contained in all of the federal cases brought by individual plaintiffs who elected to "opt-out" of the federal class action, which cases were included in the coordinated proceedings, as well as the dismissal of similar conspiracy and price discrimination claims pending in various state courts. The Company, together with other manufacturers, remains a defendant in many of the federal opt-out cases included in the coordinated proceedings to the extent of claims alleging price discrimination in violation of the Robinson-Patman Act. While no discovery or other significant proceedings have been taken to date in respect of such claims, there can be no assurance that the Company will not be required to actively defend such claims or to pay substantial amounts to dispose of such claims.

On January 14, 2003, Forest Pharmaceuticals, Inc., a wholly-owned subsidiary of the Company, was named as a defendant, together with 29 other manufacturers of pharmaceutical products, in an action brought in the United States District Court for the Eastern District of New York by the County of Suffolk, New York, as plaintiff. The action alleges that plaintiff County was overcharged for its share of Medicare and Medicaid drug reimbursement costs as a result of reporting by manufacturers of "Average Wholesale Prices" which did not correspond to actual provider costs of prescription drugs. The action includes counts under the Federal RICO and False Claims Acts, as well as claims arising under state statutes and common law. The action asserts substantially similar claims to other actions (none of which include the Company as a defendant) which have been brought in various Federal District and State Courts by various plaintiffs against pharmaceutical manufacturers and which have been assigned to the United States District Court of the District of Massachusetts under the caption "In re Pharmaceutical Industry AWP Litigation" for coordinated treatment. The action brought by plaintiff has been transferred to the District of Massachusetts for coordination with these multi-district proceedings. Forest has filed a motion to dismiss which is currently under consideration by the Court. Identical actions naming the Company as a defendant have been filed by the Counties of Westchester and Rockland in New York State, which actions have been transferred to the United States District Court for the District of Massachusetts. These actions are being held in abeyance pending the outcome of Forest's motion to dismiss. The Company believes there is no merit to these actions.

The Company has received a subpoena from the Office of the Inspector General of the Federal Office of Personnel Management requesting documents related to Celexa, a prescription medication approved for the treatment of depression. The subpoena primarily requests documents related to the marketing of Celexa and educational and promotional programs with physicians. The Company believes that other makers of pharmaceutical products for the treatment of CNS indications have received subpoenas from this office. The Office of Personnel Management is the Federal Government's human resources agency. The Company is cooperating in responding to the subpoena. No claim, litigation or assessment has been asserted in connection with the subpoena.

In September 2003, the Company, together with H. Lundbeck A/S, filed an action for patent infringement against Ivax Pharmaceuticals, Inc. in the United States District Court of the District of Delaware under the caption "Forest Pharmaceuticals, Inc., Forest Laboratories Ireland, Ltd. and H. Lundbeck A/S v. Ivax Pharmaceuticals, Inc." The action is based upon the filing by Ivax with the Food and Drug Administration of an Abbreviated New Drug Application (an "ANDA") for a generic equivalent to the Company's Lexapro brand escitalopram oxalate. The Ivax ANDA seeks approval to market the generic product prior to the expiration of the Company's Lexapro patent which the Company expects to extend until 2012. Ivax has denied that the manufacture or marketing of its generic product, if approved by the FDA, would infringe the Company's patent and has asserted a counterclaim to the effect that the Company's Lexapro patent is invalid.

On May 21, 2004, the Company, together with H. Lundbeck A/S, filed an action for patent infringement against Alphapharma Pty Ltd. in the United States District Court for the Southern District Court of New York under the caption "Forest Laboratories, Inc., Forest Laboratories Ireland, Ltd. and H. Lundbeck A/S v. Alphapharma Pty Ltd." The action is based upon the filing by Alphapharma with the Food and Drug Administration of an Abbreviated New Drug Application (an "ANDA") for a generic equivalent to the Company's Lexapro brand escitalopram oxalate. The Alphapharma ANDA seeks approval to market the generic product prior to the expiration of the Company's Lexapro patent which the Company expects to extend until 2012. Alphapharma has not yet filed its Answer to the Company's Complaint.

The Company believes its patent is valid and intends to vigorously prosecute these actions.

The Company is not subject to any other pending legal proceedings, other than ordinary routine claims incidental to its business.

11. Other income:

Other income consists of the following:

| Years ended March 31, (In thousands) | 2004 | 2003 | 2002 |
|---|---|---|---|
| Interest and dividends | $23,824 | $30,343 | $27,464 |
| Contract revenue | 5,810 | 6,552 | 5,899 |
| Other income | 208 | 2,205 | 1,835 |
| | $29,842 | $39,100 | $35,198 |

12. Income taxes:

The Company and its U.S. subsidiaries file a consolidated federal income tax return.

The components of income before income tax expense were:

| Years ended March 31, (In thousands) | 2004 | 2003 | 2002 |
|---|---|---|---|
| U.S. | $460,897 | $373,832 | $347,518 |
| Non-U.S. | 475,925 | 446,737 | 122,660 |
| Income before income tax expense | $936,822 | $820,569 | $470,178 |

The provision for income taxes consists of the following:

| Years ended March 31, (In thousands) | 2004 | 2003 | 2002 |
|---|---|---|---|
| Current: | | | |
| U.S. federal | $107,155 | $118,293 | $101,393 |
| State and local | 11,267 | 10,683 | 10,000 |
| Foreign | 43,115 | 92,054 | 14,177 |
| | 161,537 | 221,030 | 125,570 |

| | | | |
|---|---|---|---|
| Deferred: | | | |
| Domestic | ( 15,543) | ( 40,102) | ( 22,152) |
| Foreign | 4,663 | ( 35,236) | 618 |
| | ( 10,880) | ( 75,338) | ( 21,534) |
| Charge in lieu of income taxes, relating to the tax effect of stock option tax deduction | 50,291 | 52,889 | 28,188 |
| | $200,948 | $198,581 | $132,224 |

No provision has been made for income taxes on substantially all of the undistributed earnings of the Company's foreign subsidiaries of approximately $1,562,000,000 at March 31, 2004 as the Company intends to indefinitely reinvest such earnings.

The reasons for the difference between the provision for income taxes and expected federal income taxes at statutory rates are as follows:

| Years ended March 31, (percentage of income before income tax expense) | 2004 | 2003 | 2002 |
|---|---|---|---|
| U.S. statutory rate | 35.0% | 35.0% | 35.0% |
| Effect of foreign operations (principally Ireland) | (12.1) | (10.4) | ( 5.8) |
| State and local taxes, less federal tax benefit | 0.8 | 0.9 | 1.3 |
| Research credit | ( 0.9) | ( 0.4) | ( 0.3) |
| Permanent differences and other | ( 1.4) | ( 0.9) | ( 2.1) |
| | 21.4% | 24.2% | 28.1% |

The Company's effective tax rate is lower than the statutory rate principally as a result of the earnings generated in lower taxed foreign jurisdictions as compared with the United States. These earnings include income from manufacturing operations in Ireland, which operate under tax incentives that currently expire in 2010.

The IRS has completed and closed its audits of the Company's tax returns through fiscal 1995.

Net deferred income taxes consist of the following:

| March 31, | 2004 | 2003 |
|---|---|---|
| *(In thousands)* | | |
| Inventory reserves | $ 38,794 | $ 52,454 |
| Receivable allowances and other reserves | 110,858 | 85,392 |
| Depreciation | ( 4,729) | ( 3,120) |
| Amortization | 10,216 | 9,606 |

| | | |
|---|---|---|
| Tax credits and other carryforwards | 282 | 264 |
| Accrued liabilities | 15,839 | 14,955 |
| Expenses deferred for tax purposes | 6,276 | 6,517 |
| Employee stock option tax benefits | 43,488 | 7,720 |
| Other | ( 1,684) | ( 1,096) |
| | $219,340 | $172,692 |
| | ======= | ======= |

**13. Quarterly financial data (unaudited):**

(In thousands, except per share data)

| | Net sales | Gross profit | Net income | Diluted earnings per share |
|---|---|---|---|---|
| 2004 | | | | |
| First quarter | $605,748 | $465,080 | $179,817 | $0.48 |
| Second quarter | 619,157 | 481,322 | 184,457 | 0.49 |
| Third quarter | 700,447 | 539,581 | 226,118 | 0.60 |
| Fourth quarter | 725,080 | 555,975 | 145,482 | 0.38 |
| | | | | |
| 2003 | | | | |
| First quarter | $467,189 | $356,516 | $123,828 | $0.33 |
| Second quarter | 531,599 | 411,766 | 142,842 | 0.38 |
| Third quarter | 586,804 | 452,441 | 174,581 | 0.47 |
| Fourth quarter | 621,114 | 481,061 | 180,737 | 0.48 |

FOREST LABORATORIES, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The Company posted record revenues and earnings for the year which will be discussed further in Results of Operations. Among the key events during the year was the October approval by the Food and Drug Administration ("FDA") of Namenda™ for the treatment of moderate to severe Alzheimer's disease. In December, the FDA also approved a new indication for Lexapro® for the treatment of Generalized Anxiety Disorder ("GAD"). Both Namenda and the new indication for Lexapro were launched during the fourth quarter and have performed well thus far. These products will be an important component for our continued growth over the next several years. Also encouraging was a positive study outcome for the mild to moderate monotherapy study for Namenda which will support a supplemental New Drug Application ("sNDA") for that indication during the next fiscal year. The Company has continued to add new product opportunities during the year by completing license agreements for the treatments of Fibromyalgia Syndrome and therapeutics in the inflammation area.

Critical Accounting Policies

The following accounting policies are important in understanding the Company's financial condition and results of operations and should be considered an integral part of the financial review. Refer to Note 1 to the consolidated financial statements, "Summary of significant accounting policies" for additional policies.

Estimates and Assumptions

The preparation of financial statements in conformity with generally accepted accounting principles requires the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities and of revenues and expenses during the reporting period. Estimates are made when accounting for sales allowances, returns, rebates and other pricing adjustments, depreciation, amortization and certain contingencies. The Company is subject to risks and uncertainties, which may include but are not be limited to competition, federal or local legislation and regulations, litigation and overall changes in the healthcare environment that may cause actual results to vary from estimates. The Company reviews all significant estimates affecting the financial statements on a recurring basis and records the effect of any adjustments when necessary. Certain of these risks, uncertainties and assumptions are discussed further under the section entitled "Forward Looking Statements".

Goodwill and Other Intangible Assets

The Company has made acquisitions in the past that include goodwill, license agreements, product rights and other intangibles. Through fiscal 2001, these assets were amortized over their estimated useful lives, and were tested periodically to determine if they were recoverable from operating earnings on an undiscounted basis over their useful lives.

Effective with fiscal 2002, goodwill was no longer amortized but is subject to an annual impairment test based on its estimated fair value. License agreements, product rights and other intangibles will continue to be amortized over their useful lives and tested periodically to determine if they are recoverable from operating earnings on an undiscounted basis over their useful lives.

Revenue Recognition

Revenues are recorded in the period the merchandise is shipped. Provisions for estimated sales allowances, returns, rebates and other pricing adjustments are accrued at the time revenues are recognized as a direct reduction of such revenue. The accruals are estimated based on available information regarding the portion of sales on which rebates and discounts can be earned, adjusted as appropriate for specific known events, and the prevailing contractual discount rates. Provisions are reflected either as a direct reduction to accounts receivable or, to the extent that they are due to entities other than customers, as accrued expense. Adjustments to estimates, which have not been material, are recorded when customer credits are issued or payments are made to third parties.

Financial Condition and Liquidity

During fiscal year 2004 net current assets increased by $620,544,000. Continued growth of the Company's ongoing operations, particularly the antidepressant franchise and the launch in the fourth fiscal quarter of Namenda, contributed to increases in cash, marketable securities, accounts receivable and deferred income taxes. During the year, the Company shifted the composition of marketable securities in favor of longer term securities to receive more favorable rates of return. Accounts receivable increased in total due to the increase in sales but also increased in the number of days sales in accounts receivable, from 32 days in the prior year to 40 days. This increase was principally due to wholesaler buying patterns as proportionally more sales occurred the last month of the period than in the prior year. In the prior year's fourth quarter, approximately 29% of sales occurred in March in contrast to the current year's fourth quarter where approximately 35% of sales occurred in March and were not due at March 31 under the

Company's standard payment terms of 30 days. Contributing to the relative increase in accounts receivable was the launch of Namenda. As is common in the industry, to ensure broad availability of Namenda in pharmacies, extended dating terms were offered to customers for their initial purchases of Namenda. Under these special terms, these receivables were not yet due at the end of March, and accounted for approximately three days of the increase. During fiscal year 2004, the Company shifted certain managed care contracts to performance-based rebate programs. Provisions for rebates are reflected in accrued expenses rather than as a reduction of accounts receivable. Consequently, this shift also contributed to an increase in accounts receivable and a caused a corresponding increase to accrued expenses.

The increase in inventories during the period was due primarily to an increase in raw materials which was partially offset by a decrease in finished goods. Raw materials increased in volume to support increasing sales and average cost increased due to a change in the mix of materials held in inventory for sale and for sampling. Under our licensing arrangements raw materials acquired for sampling of Celexa® (citalopram) and Lexapro (escitalopram oxalate) are purchased at a discount and raw materials held for samples made up a smaller proportion of inventories as compared to March 2003, at which time Lexapro was in its launch phase. The change in the mix of inventory has no impact on gross margin as sample expense is a component of selling, general and administrative expenses. In addition, finished goods inventories at March 31, 2003 were relatively high due to the early stage of the Lexapro launch where we were maintaining safety stock levels for both Lexapro and Celexa at a high level until the rate of conversion was established. During the course of this year inventories of both have been adjusted to appropriate levels.

Property, plant and equipment increased as the result of the continuing expansion of the Company's facilities in order to meet current and future product and research and development demands. On Long Island, the Company completed a 100,000 square foot research and development laboratory and is expanding its packaging and distribution facility, which will add approximately 185,000 square feet to that location. During the year an additional 180,000 square foot facility was purchased on Long Island and will be converted for future research and development activities. The Company also purchased an additional 90,000 square foot facility in Ireland which will provide additional manufacturing capacity for the production of Lexapro, Namenda and future products. Further property expansions and acquisitions are planned in the future to meet the needs from increased sales and related production, warehousing and distribution and for products under development.

During the third quarter a $20,000,000 milestone payment was made to Merz Pharma GmbH upon FDA approval of Namenda, which was recorded in license agreements, product rights and other intangibles. In the second quarter the Company announced that it had discontinued development of dexloxiglumide for irritable bowel syndrome ("IBS"), causing a write-off of the license agreement of $12,545,000 to research and development expense. During the fourth quarter, the Company entered into a development and marketing agreement with Cypress Bioscience, Inc. for milnacipran for the treatment of fibromyalgia and ChemoCentryx, Inc. for therapeutics in the inflammation area. The initial payments of $35,000,000 for these early stage licenses were recorded to research and development expense.

Management believes that current cash levels, coupled with funds to be generated by ongoing operations, will continue to provide adequate liquidity to facilitate potential acquisitions of products and capital investments.

Contractual Obligations

The following table shows the Company's contractual obligations (refer to Note 8 to the consolidated financial statements, "Commitments").

| | Payments due by period *(in thousands)* | | | | |
|---|---|---|---|---|---|
| | <1 year | 1-3 years | 4-5 years | >5 years | Total |
| Operating lease obligations | $29,886 | $42,820 | $27,062 | $68,450 | $168,218 |

Off-Balance Sheet Arrangements

The Company is a party to several license agreements for products currently under development that may obligate Forest, in future periods, to pay additional amounts subject to the achievement of certain product development milestones, as defined.

Results of Operations

Net sales increased $443,726,000 to $2,650,432,000, a 20% increase from fiscal year 2003, primarily due to the continued success of the antidepressant franchise, particularly Lexapro. During the year Lexapro, which was launched in September 2002, surpassed Celexa as the Company's largest product with sales of $1,088,957,000 as compared to Celexa sales of $1,087,281,000 and contributed $844,227,000 to the net sales change. As anticipated, a portion of Lexapro's market share has come from Celexa which resulted in a Celexa sales decline of $364,698,000 for the year primarily due to volume. The Company anticipates further declines in Celexa sales as Lexapro continues to gain market share. At the end of the year, Lexapro had achieved a 15.9% share of total prescriptions in the SSRI market, while Celexa's share declined to 9.1% from a peak share of 17.5% in August 2002. Lexapro has patent protection until 2009 and the Company has applied for an extension to 2012. Earlier in the year, the Company received notification from generic manufacturers that had filed an Abbreviated New Drug Application ("ANDA") with a Paragraph IV Certification with the FDA for a generic equivalent to Lexapro. The Company believes that its patents on Lexapro are valid and expects to defend its rights under those patents which would preclude the introduction of a generic product at least until after the expiration of the substance patent, including patent extension, which will be in 2012. The Company has commenced an action for patent infringement against the third party ANDA filers. Celexa had Hatch-Waxman marketing exclusivity through July 2003 and was granted a six-month extension based upon the submission of results of clinical studies in depressed pediatric patients. The earliest date at which a generic competitor was able to file an ANDA for review by the FDA was January 17, 2004. The Company believes that several have. Also contributing to the overall net sales change was the Company's introduction to the market of Namenda, for the treatment of moderate to severe Alzheimer's disease, which was launched by the salesforce in March 2004. Net sales, which include wholesaler stocking from December 2003 and January 2004, amounted to $45,472,000 for the year. Although the salesforce launched the product on March 1, 2004, the demand for the product was such that the Company began initial stocking sales in December 2003 to ensure Namenda's availability in pharmacies nationwide by January 2004 and samples were available via a "by request" sample program. While it is still early in the launch phase, Namenda's success thus far in terms of prescription trends and product reorders have been quite encouraging. In April 2003, a generic equivalent to the Company's Tiazac was introduced into the market, resulting in a decrease in sales of $109,884,000 for the year. The Company ceased all promotional efforts for Tiazac as of September 2003 and expects further declines in sales of its Tiazac brand as generic substitution rates continue to increase. During the June 2003 quarter, the Company introduced its own generic version of Tiazac. Sales of that product for the year were $35,519,000, including initial stocking. The remainder of the net sales change for the year was due principally to volume declines on the Company's older unpromoted product lines.

Net sales in fiscal 2003 increased $640,080,000 to $2,206,706,000, a 41% increase from fiscal 2002. In September 2002, the Company launched Lexapro, the single isomer of Celexa. For the year, Lexapro sales amounted to $244,730,000 and Celexa sales amounted to $1,451,979,000. Combined, the antidepressant franchise contributed $608,915,000 to the net sales change. At March 31, 2003 Celexa's share of total prescriptions in the SSRI market was approximately 13.5% and Lexapro's share was approximately 8.1%. The Company believes, based on the results of clinical trials, that Lexapro is a superior product to Celexa. Therefore, upon the introduction of Lexapro, the Company ceased nearly all promotion and sampling of Celexa. A portion of Lexapro's market share was taken from Celexa and the Company anticipates prescription share and sales of Celexa will decline as Lexapro continues to gain market share. Net sales of Tiazac® increased $10,919,000 during fiscal year 2003 due primarily to volume. The remainder of the net sales change of $20,246,000 was due primarily to price increases for our generic and other non-promoted

product lines.

Other income for fiscal year 2004 decreased over the same period last year as the prior year included capital gains on the liquidation of certain long-term investments, a gain on the sale of assets and interest on tax refunds. Interest income also decreased as the Company received lower rates of return on invested funds during the current period. The increase in other income in fiscal year 2003 was the result of higher interest income resulting from increases in funds available for investment and capital gains on the liquidation of certain long-term investments, a gain on the sale of assets and interest on tax refunds. Included in other income for all periods were royalties on sales of Climara®, a transdermal estrogen product, which amounted to $5,810,000, $6,552,000 and $5,899,000 in fiscal years 2004, 2003 and 2002, respectively.

Cost of sales as a percentage of net sales for fiscal year 2004 was 23%, unchanged from fiscal year 2003. Cost of sales as a percentage of sales was 24% in fiscal year 2002. The improvement was due to an increase in overall plant utilization as well as a change in product mix, as the Company's antidepressant franchise, which has a relatively lower cost of goods, increased to 77% of total consolidated net sales for fiscal year 2003 as compared to 69% in fiscal year 2002. In fiscal year 2004, the antidepressant franchise comprised 82% of total consolidated net sales.

Selling, general and administrative expenses increased $173,085,000 in fiscal year 2004 and $112,641,000 in fiscal year 2003. In December 2003, the Company received marketing approval from the FDA for both its GAD indication for Lexapro and for Namenda to treat moderate to severe Alzheimer's disease. To effectively market these products, the Company added approximately 525 additional representatives to its salesforce during the third quarter. The GAD indication for Lexapro was launched in January 2004 and Namenda was launched in March 2004. This latest salesforce expansion brings the total number of representatives and managers to approximately 2,825. The cost of the expanded salesforce, including initial hiring and training costs, together with pre-launch and launch costs, resulted in an increase in selling, general and administrative expenses for the year.

The increases in research and development expense during each of the years presented were due primarily to costs associated with ongoing clinical trials and from staff increases and associated costs required to support currently marketed products and products in various stages of development. Fiscal year 2004 included a one-time write-off of the dexloxiglumide license after its phase III clinical program for the treatment of IBS failed to achieve statistically significant results. The Company continues to conduct clinical trials for additional indications for Lexapro. In May 2004, a supplemental New Drug Application ("sNDA") was filed to expand Lexapro's labeling to include the treatment of social phobia. In October 2003, the Company received FDA approval to market Namenda for the treatment of moderate to severe Alzheimer's disease. Namenda is also being studied for the treatment of mild to moderate Alzheimer's disease as well as an additional indication for neuropathic pain. Based on positive results from a Phase III study released in January 2004, Forest plans to file an sNDA for the treatment of mild to moderate Alzheimer's disease during the second half of calendar 2004. Neramexane, a follow-on NMDA receptor antagonist to Namenda, is currently in Phase II clinical trials and is being tested for various CNS disorders. Forest received an approvable letter from the FDA in August 2002 regarding lercanidipine for the treatment of hypertension. In December 2002, the FDA indicated that it would require the Company to conduct additional clinical trials in order to approve the dosing regimen requested by Forest. The Company has reformulated the lercanidipine formulation and has begun a clinical program to support the requested dosing regimen. During fiscal 2003, the FDA determined that the NDA for acamprosate, licensed from Merck KGaA for the treatment of alcohol dependence, was non-approvable. Subsequently, Merck KGaA submitted an amendment to the NDA and expects FDA action during the second half of calendar 2004. During the fourth quarter of fiscal 2004, the Company entered into two licensing agreements; the first with Cypress Bioscience, Inc. for the development and marketing of milnacipran, which is currently being evaluated for the treatment of Fibromyalgia Syndrome ("FMS"), a frequent cause of chronic, widespread pain, estimated to affect six to twelve million people in the United States. There are currently no products approved for the treatment of FMS. The second was a development agreement with ChemoCentryx, Inc. for a novel oral rheumatoid arthritis and multiple sclerosis therapeutic. The Company anticipates further increases in research and development for next fiscal year and beyond.

The effective income tax rate declined to 21% in fiscal year 2004 as compared to 24% and 28% in fiscal years 2003 and 2002, respectively. The lower effective tax rate was a direct result of the increase in the proportion of earnings generated in lower-taxed foreign jurisdictions versus the United States. These earnings include manufacturing and development income from our operations in Ireland, which are taxed at 10% through 2010 and at 12.5% thereafter.

The Company expects to continue its profitability into fiscal 2005 with continued growth in its principal promoted products.

Inflation has not had a material effect on the Company's operations for the periods presented.

Forward Looking Statements

Except for the historical information contained herein, the Management Discussion and other portions of this Form 10-K contain forward looking statements that involve a number of risks and uncertainties, including the difficulty of predicting FDA approvals, acceptance and demand for new pharmaceutical products, the impact of competitive products and pricing, the timely development and launch of new products and the risk factors listed from time to time in the Company's filings with the SEC, including the Company's Annual Report on Form 10-K for the fiscal year ended March 31, 2004.

Quantitative and Qualitative Disclosures About Market Risk

In the normal course of business, operations of the Company may be exposed to fluctuations in currency values and interest rates. These fluctuations can vary the costs of financing, investing and operating transactions. Because the Company had no debt and only minimal foreign currency transactions, there was no material impact on earnings due to fluctuations in interest and currency exchange rates.