

# **MCKESSON**

*Empowering Healthcare*

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## **Credit Suisse First Boston Global Healthcare Conference**

**November 17, 2004**

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# **John H. Hammergren, Chairman and Chief Executive Officer**

# Safe Harbor Clause

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**Some of the information in this presentation may constitute forward-looking statements that are subject to various uncertainties. These uncertainties could cause actual results to differ materially from those projected or implied. The risk factors associated with those uncertainties are described in the Company's reports and exhibits filed with the Securities and Exchange Commission. Financial information is presented here in summary form. Full details are provided in the Company's most recent 10-Q report. All of this information is available at [www.mckesson.com](http://www.mckesson.com).**

# Overview

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- **Who We Are**
- **Our View of Healthcare**
- **How Our Businesses Are Currently Performing**

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# Who We Are

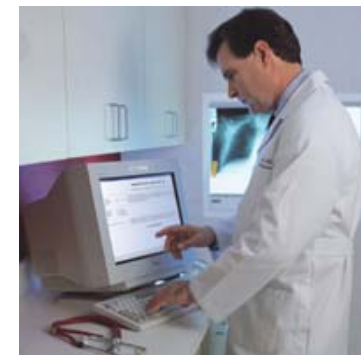
# McKesson's Solutions ... Building on Distribution Strength



**Pharmaceutical & medical-surgical distribution to all sites**



**Solutions for medication safety**



**Clinical, financial & resource management for hospitals & IDNs**



**Retail pharmacy automation**



**Inpatient automation**



**Specialty pharmaceuticals**



**Disease management**



**Drug cards for seniors**



**Pharmaceutical repackaging**

# Our Business Today

# MCKESSON

## McKesson Pharmaceutical

**#1 in U.S., Canada, and Mexico**

**Large Rx repackaging**

**Leading generics provider**

**#1 in retail pharmacy automation**

**Specialty distribution & patient services for manufacturers**

**#1 in medical management software and services for payors**

**#1 in disease management for Medicaid agencies**

## McKesson Medical-Surgical

**#1 in primary care**

**#1 in extended care**

**Total supply solution in acute care**

**Private label product offerings**

**Rapid growth in physician office pharmaceuticals and equipment**

## McKesson Provider Technologies

**63% of health systems**

**51% of hospitals with 200+ beds**

**Leader in clinical, revenue cycle, and resource management solutions**

**More "Best in KLAS" products than any other vendor**

**#1 in robotic hospital pharmacy dispensing**

**#1 in bedside scanning**

# Strong, Long-term Customer Relationships with Market Leaders



Vanderbilt University Medical Center



Omnicare



Empowering Healthcare

# FY05 Consolidated Financial Results

(\$ and shares in millions, except EPS)

	Q2			Six Months		
	FY04	FY05		FY04	FY05	
Revenues	\$ 16,810	\$ 19,934	19%	\$ 33,334	\$ 39,121	17%
Gross Profit	812	735	-9%	1,598	1,587	-1%
Gross Profit Margin	4.83%	3.69%	(114) bp	4.79%	4.06%	(73) bp
Operating Income	227	129	-43%	479	390	-19%
Operating Income Margin	1.35%	0.65%	(70) bp	1.44%	1.00%	(44) bp
Net Income	157	86	-45%	312	250	-20%
Diluted EPS	\$ 0.53	\$ 0.29	-45%	\$ 1.05	\$ 0.84	-20%
Weighted Average Shares	300	300		299	300	

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# Our View of Healthcare

# Trends Driving Healthcare Growth

## Focus on quality of care

- Reduce medical errors
- Adopt clinical protocols/ evidence-based medicine

## Increased pressure on payors

- Payors taking on more risk
- Limitations on use of managed care tools
- Employer pressures on double-digit premium increases

## Outpatient and chronic disease management

- Chronic disease management
- Case management
- Manage high-cost diseases in small populations

## Continued improvements in operational and administrative efficiency

- Automation to overcome labor shortages
- Electronic claims and eligibility
- Online prescription and lab transmissions
- Streamlined pre-authorization

## Continued use of new drugs, but increased pricing scrutiny

- Biotech pipeline expansion
- New drug delivery mechanisms
- Rapid growth in generics
- Regulatory pressures on pricing

## Increased consumerism

- Unhappy consumers
- Better informed consumers

# Improved U.S. Healthcare by 2010

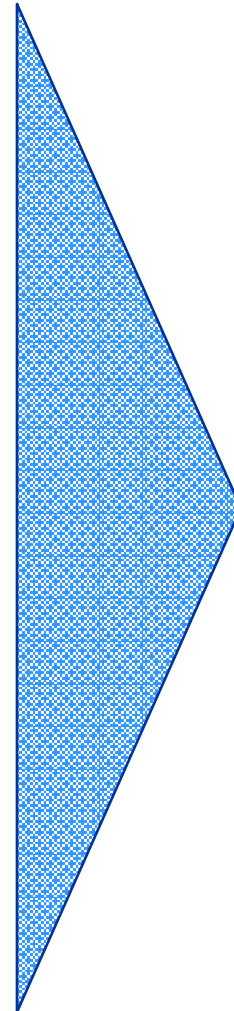
**Informed clinical  
practice**

**Interconnection**

**Improved safety  
and efficiency**

**Personalized care**

**Population health  
initiatives**



**CULTURE  
CHANGE  
in the  
delivery of  
healthcare**

# McKesson's Strategy

To bring together clinical knowledge, process expertise, technology, and the resources of a *Fortune 16* company to fundamentally change the cost and quality of healthcare.



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# **How Our Businesses Are Currently Performing**

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# Pharmaceutical Solutions

# FY05 Financial Results – Pharmaceutical Solutions

(\$ in millions)

	Q2			Six Months		
	FY04	FY05		FY04	FY05	
<b>Revenues</b>						
U.S. direct distribution & services	\$ 9,655	\$ 11,638	21%	\$ 18,990	\$ 22,649	19%
U.S. sales to customers' warehouses	5,058	6,021	19%	10,222	11,938	17%
Subtotal	14,713	17,659	20%	29,212	34,587	18%
Canada distribution & services	1,070	1,258	18%	2,114	2,510	19%
Total Pharmaceutical Solutions	\$ 15,783	\$ 18,917	20%	\$ 31,326	\$ 37,097	18%
Gross Profit	509	432	-15%	1,027	992	-3%
Gross Profit Margin	3.22%	2.28%	(94) bp	3.28%	2.67%	(61) bp
Operating Expense	294	287	-2%	553	562	2%
Operating Profit	222	151	-32%	487	441	-9%
Operating Profit Margin	1.40%	0.80%	(60) bp	1.55%	1.19%	(36) bp

# Pharmaceutical Solutions

## Q2 Highlights

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- **Above market U.S. revenue growth of 20%**
  - **First full quarter of VA business with annualized revenues in excess of \$3.5B, better than expected profitability**
  - **AdvancePCS volume of Caremark implemented in August with annualized revenues of \$2B**
- **Continued strong growth in Canada of 18%**
- **Fewer than expected price increases significantly reduces operating profit**

# U.S. Pharmaceutical Distribution Environment

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- **35-year evolution in manufacturer economics**
  - Historical economics evolved to dependence on pharmaceutical price inflation for major source of compensation
  - Changes underway in healthcare may impact pharmaceutical pricing
- **Customer pricing model established on inflation-based profit opportunities**

# Value of Drug Distribution

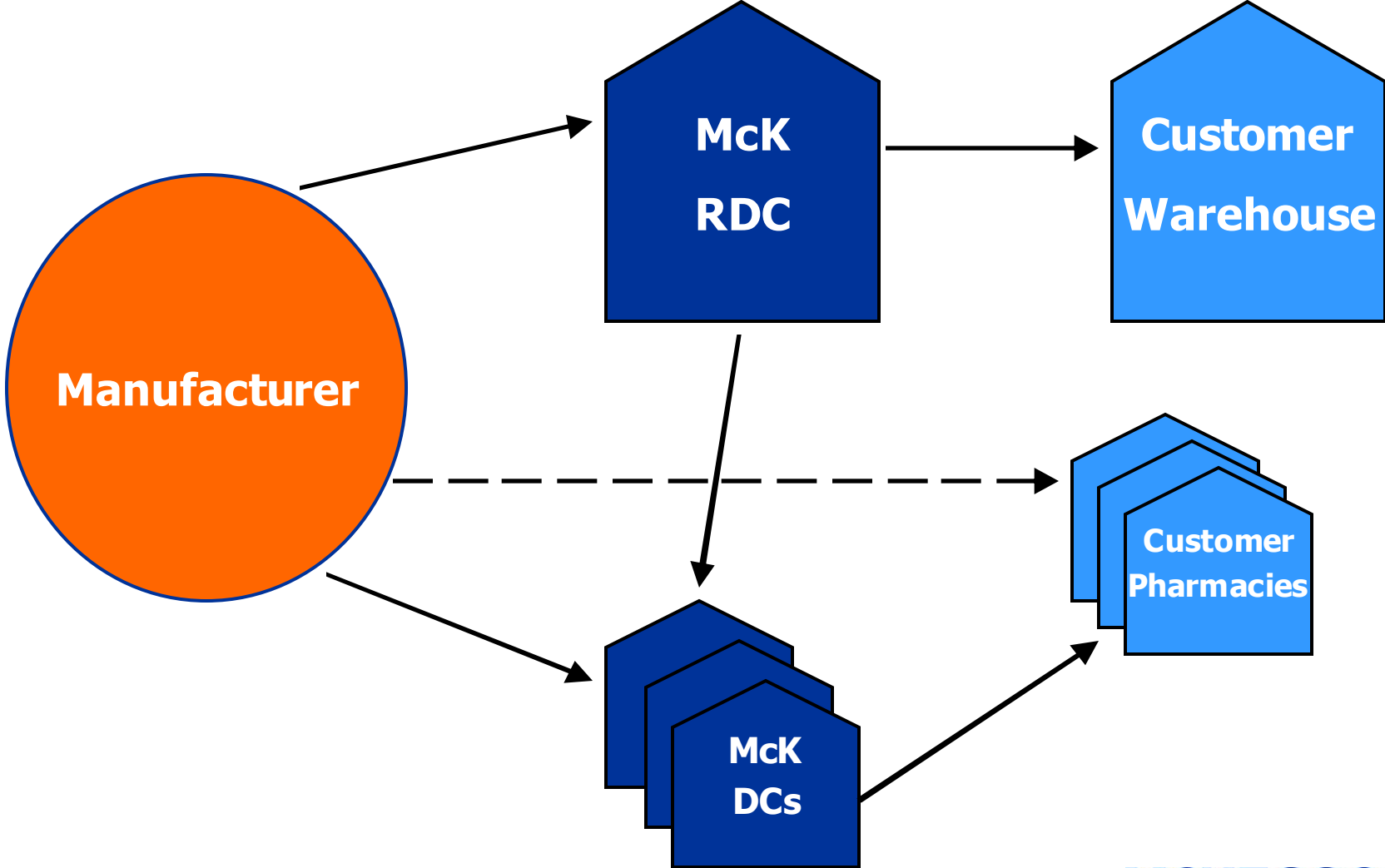
## Industry

- Booz-Allen study shows \$10.5 B in added annual expense to replicate distributor network/service

## McKesson

- Next day delivery to 23,000 pharmacies with 99.1% fill rate
- 45,000 SKUs
- 129,000 invoices per day
- 150,000 contracts involving \$20 B in annual chargebacks
- >\$400 M additional invested over the past 4 years

# McKesson Pharmaceutical Product Flow



# Progress with Manufacturers

- Collaborative strategy designed to deliver more predictable core distribution fees based on value provided
- Phase 1: Focus on securing an appropriate level of compensation with less product sourcing
  - Compensation from largest manufacturers still tied to the timing and magnitude of price increases
- Phase 2: Focus on maintaining appropriate compensation while gaining predictability by reducing dependence on price inflation
- Achieve significant progress by January 1 and substantially complete the process by March 31, 2005 fiscal year end

# Progress with Manufacturers

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## PHASE 1: APPROPRIATE COMPENSATION

August 2003 to August 2004

	<u>% Complete</u>	<u>Result</u>
All companies	80%	New IMAs and CDAs reflect value of service provided
Largest companies		Compensation still tied to price inflation

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## PHASE 2: PREDICTABLE COMPENSATION

September 2004 to March 2005

	<u>% Complete</u>	<u>Result</u>
All companies	>80%	New agreements based on FFS and/or guarantees
Largest companies	25%	About a dozen remaining

# Pharmaceutical Distribution Margin Drivers

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2% Cash  
Discount

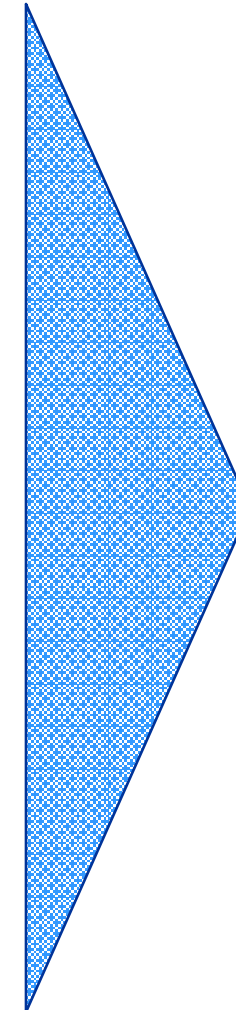
Generics

Buy  
Profit\*

-

Sell  
Margin

Operating  
Expenses



Margin has  
fluctuated  
very little  
over the  
past 35  
years

# Pharmaceutical Solutions

## Operating Margin

- Over the past 15 years, we have experienced significant changes in the marketplace, price increases ranging between 1.7% and 8.5%, yet operating margin has fluctuated little between a narrow range
- European distributors that face entirely different market factors have similar operating margins



**Operating margin for direct store sales has been generally between 2% and 2.5% = 1.5% to 2% including warehouse sales**

# Improve Existing Customer Profitability

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- **Improving compliance and efficiency across customer base**
  - **Focus on securing prime vendor relationships exclusively**
  - **Enforce contract terms (e.g., generic compliance)**
  - **Charge for additional services (e.g. emergency shipments, minimum order size, etc.)**

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# Medical-Surgical Solutions

# FY05 Financial Results – Medical-Surgical Solutions

(\$ in millions)	Q2			Six Months		
	FY04	FY05		FY04	FY05	
Revenues	\$ 716	\$ 714	--	\$ 1,426	\$ 1,421	--
Gross Profit	151	162	7%	297	321	8%
Gross Profit Margin	21.13%	22.69%	156 bp	20.85%	22.57%	172 bp
Operating Profit	25	18	-31%	51	46	-10%
Operating Profit Margin	3.53%	2.45%	(108) bp	3.58%	3.24%	(34) bp

# Medical-Surgical Solutions

## Q2 Highlights

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- Continued strong growth from alternate site customers
- Quarter's results impacted primarily by increased litigation reserve
- New 3-year, \$150 million agreement with Adventist Health includes Optyx state-of-the-art analytical service

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# McKesson Provider Technologies

# FY05 Financial Results – Provider Technologies

(\$ in millions)

	Q2			Six Months		
	FY04	FY05		FY04	FY05	
<b>Revenues</b>						
Software & software systems	\$ 67	\$ 50	-26%	\$ 113	\$ 101	-11%
Services	217	228	5%	421	451	7%
Hardware	27	26	-7%	48	52	9%
<b>Total Provider Technologies</b>	<b>\$ 311</b>	<b>\$ 304</b>	<b>-2%</b>	<b>\$ 582</b>	<b>\$ 604</b>	<b>4%</b>
<b>Gross Profit</b>	<b>152</b>	<b>141</b>	<b>-7%</b>	<b>274</b>	<b>274</b>	<b>--</b>
<b>Gross Profit Margin</b>	<b>48.65%</b>	<b>46.48%</b>	<b>(217) bp</b>	<b>47.04%</b>	<b>45.42%</b>	<b>(162) bp</b>
<b>Operating Profit</b>	<b>37</b>	<b>19</b>	<b>-48%</b>	<b>42</b>	<b>34</b>	<b>-20%</b>
<b>Operating Profit Margin</b>	<b>11.95%</b>	<b>6.32%</b>	<b>(563) bp</b>	<b>7.20%</b>	<b>5.55%</b>	<b>(165) bp</b>

# Provider Technologies

## Q2 Highlights

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- **Software bookings up strongly**
- **Revenues reflect continued strong demand for clinical solutions but complexity of installations**
- **Percentage of Completion (POC) is increasing as a percent of revenue**
- **Demand for revenue cycle and resource management solutions remains flat**
- **Government focus on HIT may drive future growth opportunities**

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# Summary

# What McKesson Represents

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- **Core pharmaceutical business positioned for sustained growth with a strategy in place to address industry evolution**
- **Additional businesses poised to take advantage of new and expanding opportunities in healthcare**
- **Track record of financial performance**
  - **Consistent annual EPS growth despite challenges**
  - **Increasing cash flow**
  - **Strong balance sheet provides financial flexibility**
  - **Commitment to financial transparency**

# Outlook

- **FY05 expectation: \$2.00 to \$2.20 per share**
  - **Pharmaceutical Solutions earnings continue to depend on price increases through fiscal year end**
  - **Expectation assumes that volume-weighted U.S. pharmaceutical price increases in Q3 and Q4 will be within the historical range, and that the magnitude of price increases will be comparable to the recent past**



**Create Value for Suppliers, Customers and Shareholders**

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