

Company Overview

Becton, Dickinson and Company (“BD”) is a medical technology company engaged principally in the manufacture and sale of a broad range of medical supplies, devices, laboratory equipment and diagnostic products used by healthcare institutions, life science researchers, clinical laboratories, industry and the general public. Our business consists of three worldwide business segments—BD Medical (“Medical”), BD Diagnostics (“Diagnostics”) and BD Biosciences (“Biosciences”). Our products are marketed in the United States and internationally through independent distribution channels, directly to end-users and by independent sales representatives. References to years throughout this discussion relate to our fiscal years, which end on September 30.

BD management operates the business consistent with the following core strategies:

- To increase revenue growth by focusing on products that deliver greater benefits to patients, healthcare workers and researchers;
- To improve operating effectiveness and balance sheet productivity; and,
- To strengthen organizational and associate capabilities in the ever-changing healthcare environment.

In assessing the outcomes of these strategies and BD’s financial condition and operating performance, management generally reviews quarterly forecast data, monthly actual results, segment sales and other similar information. We also consider trends related to certain key financial data, including gross profit margin, selling and administrative expense, investment in research and development, and cash flows.

The results of our strategies are reflected in our fiscal 2007 financial and operational performance. Worldwide revenues in 2007 of \$6.4 billion increased 11% from the prior year and reflected volume increases of approximately 8%, an estimated increase due to favorable foreign currency translation of 3%, and price increases of less than 1%. U.S. revenues increased 11% to \$3.0 billion. International revenues increased 11% to \$3.3 billion with an estimated 5 percentage points of such growth coming from the favorable impact from foreign currency. For a discussion of the financial impact of exchange rate fluctuations and the ways and extent to which we attempt to mitigate such impact, see “Financial Instrument Market Risk” below.

Consistent with our strategy to provide products that deliver greater benefits to healthcare workers, and recognizing the issues surrounding sharps-related injuries, BD has developed a wide array of safety-engineered devices that are designed to reduce the incidence of needlestick injuries and exposure to bloodborne pathogens. These products are offered through our Medical and Diagnostics segments. Sales in the United States of safety-engineered devices grew 7% to \$982 million in 2007, from \$917 million in 2006. International sales of safety-engineered devices grew 26% to \$409 million in 2007 from \$324 million in 2006. In 2008, we expect sales of safety-engineered devices to increase about 8% in the United States and 20% internationally.

Income from Continuing Operations was \$856 million, or \$3.36 per diluted share, in 2007 as compared with \$815 million, or \$3.18 per diluted share, in 2006. Comparisons of Income from Continuing Operations between 2007 and 2006 are affected by the following significant items that are reflected in our financial results:

2007

- In December 2006, we acquired TriPath Imaging, Inc. (“TriPath”). TriPath develops, manufactures, markets and sells innovative solutions to improve the clinical management of cancer, including detection, diagnosis, staging and treatment. In connection with the acquisition, we incurred a pre-tax non-cash charge of \$115 million, or \$.45 per diluted share, for acquired in-process research and development.
- In December 2006, we sold the blood glucose monitoring (“BGM”) product line. Following the sale, prior period Consolidated Statements of Income and Cash Flows were restated to separately present the results of the BGM product line as discontinued operations.

2006

- In February 2006, we acquired GeneOhm Sciences, Inc. (“GeneOhm”). In connection with the acquisition, we incurred a pre-tax non-cash charge of \$53 million, or \$.21 per diluted share, for acquired in-process research and development.

Our ability to sustain our long-term growth will depend on a number of factors, including our ability to expand our core business (including geographical expansion), develop innovative new products with higher gross profit margins across our business segments, and continue to improve operating efficiency and organizational effectiveness. Numerous factors can affect our ability to achieve these goals including, without limitation, economic conditions in the United States and elsewhere, increased competition and healthcare cost containment initiatives.

We believe several important factors relating to our business tend to reduce the impact on BD of any potential economic or political events in countries in which we do business, including the effects of possible healthcare system reforms. For example, since many of our products are used in essential medical care, demand for such products tends not to be significantly affected by economic fluctuations. Other factors include the international nature of our business and our ability to meet the needs of the worldwide healthcare industry with cost-effective and innovative products.

In 2007, general inflation did not have a material impact on our overall operations. However, it is possible that general inflation rates will rise in 2008 and beyond, and could have a greater impact on worldwide economies and, consequently, on BD. BD purchases supplies of resins, which are oil-based components used in the manufacture of certain products. During 2007, we incurred slightly higher resin purchase costs than the prior year, primarily due to increases in world oil prices during the late summer 2006. Such increases did not have a significant impact on our 2007 operating results. Any significant increases in resin purchase costs could impact future operating results.

Our anticipated revenue growth over the next three years is expected to come from the following:

- Business growth and expansion among all segments; and
- Development in each business segment of new products and services that provide increased benefits to patients, healthcare workers and researchers.

Results of Continuing Operations

Medical Segment

Medical revenues in 2007 of \$3.4 billion increased \$314 million, or 10%, over 2006, which includes an estimated impact of unfavorable foreign currency translation of 3 percentage points.

The following is a summary of revenues by organizational unit:

(millions of dollars)	2007	2006	Estimated Foreign	
			Total Change	Exchange Impact
Medical Surgical Systems	\$1,864	\$1,749	7%	2%
Diabetes Care	696	657	6%	2%
Pharmaceutical Systems	792	640	24%	6%
Ophthalmic Systems	69	62	11%	4%
Total Revenues*	\$3,421	\$3,107	10%	3%

* Amounts may not add due to rounding.

Medical revenues reflect the growth of the Pharmaceutical Systems unit and the continued global conversion to safety-engineered products. The Pharmaceutical Systems unit grew by 24%, reflecting the increased use of prefillable syringes by pharmaceutical companies to market new vaccines and bio-tech drugs, especially in the United States. Revenue growth in the Medical Surgical Systems unit was primarily driven by the growth in safety-engineered products and prefilled flush syringes. Sales of safety-engineered products increased 6% in the United States and 30% internationally. For 2008, we expect the full-year revenue growth for the Medical Segment to be about 8%.

Medical operating income was \$972 million, or 28.4% of Medical revenues, in 2007, as compared with \$864 million, or 27.8% in 2006. The increase in operating income as a percentage of revenues reflects gross margin improvement from increased sales of products that have higher overall gross profit margins, in particular, safety-engineered products and pen needles, as well as favorable manufacturing efficiencies associated with higher volumes and increased leverage on selling and administrative expenses. These improvements were slightly offset by manufacturing start-up costs. See further discussion on gross profit margin below. Selling and administrative expense as a percent of Medical revenues in 2007 declined to 18.9% of revenues from 19.6% of revenues in 2006, primarily due to tight expense controls over base spending. Research and development expenses in 2007 increased \$16 million, or 17%, reflecting continued investment in the development of new products and platforms, and included investments in additional resources to enhance our product development process.

Diagnostics Segment

Diagnostics revenues in 2007 of \$1.9 billion increased \$190 million, or 11%, over 2006, which reflected an estimated favorable impact of foreign currency translation of about 2 percentage points.

The following is a summary of revenues by organizational unit:

(millions of dollars)	2007	2006	Estimated Foreign	
			Total Change	Exchange Impact
Preanalytical Systems	\$1,007	\$ 928	9%	3%
Diagnostic Systems	898	787	14%	2%
Total Revenues	\$1,905	\$1,715	11%	2%

Revenue growth in the Preanalytical Systems unit was driven by the continued conversion to safety-engineered products, which accounted for sales of \$718 million as compared with \$627 million in the prior year. Sales of safety-engineered products reflected growth of 9% in the United States, which benefited from *BD Vacutainer* Push Button Blood Collection Set conversion activity, and 25% internationally. The Diagnostics Systems unit experienced solid worldwide sales of its automated diagnostic platforms, including the molecular *BD ProbeTec* and *BD Viper* systems, along with solid growth of its *BD BACTEC* blood culture and TB systems and the *BD Phoenix* ID/AST platform. Those platforms reported combined incremental sales of \$35 million over 2006. In addition, the Diagnostic Systems revenue growth includes \$88 million of revenues from TriPath and \$13 million of incremental revenues from GeneOhm. Sales of flu diagnostic tests declined \$36 million in fiscal 2007 compared with 2006, primarily due to relatively mild flu seasons in both the United States and Japan and the termination of our supply arrangement with our Japanese supplier. For 2008, we expect full year revenue growth for the Diagnostics Segment to be about 9%.

Diagnostics operating income was \$343 million, or 18.0% of Diagnostics revenues in 2007, compared with \$390 million, or 22.8% in 2006. Segment operating income reflects the in-process research and development charges of \$115 million in 2007 related to the TriPath acquisition and \$53 million in 2006 related to the GeneOhm acquisition. The Diagnostics Segment experienced a slight improvement in gross profit margin from sales growth of products that have higher overall gross profit margins, in particular, safety-engineered products and the *BD ProbeTec* system. These improvements were slightly offset by manufacturing start-up costs. See further discussion on gross profit margin below. Selling and administrative expense as a percent of Diagnostics revenues in 2007 was higher than the comparable amount in 2006 primarily due to the impact of TriPath and GeneOhm. Research and development expense increased \$33 million, or 39%, reflecting new spending associated with these two acquisitions and overall increased investment in new product development.

Biosciences Segment

Biosciences revenues in 2007 of \$1.0 billion increased \$118 million, or 13%, over 2006, which reflected an estimated impact of favorable foreign currency translation of 3 percentage points.

The following is a summary of revenues by organizational unit:

(millions of dollars)	2007	2006	Total Change	Estimated
				Foreign Exchange Impact
Immunocytometry Systems	\$ 588	\$503	17%	3%
Discovery Labware	278	256	9%	2%
Pharmingen	168	157	7%	2%
Total Revenues	\$1,034	\$916	13%	3%

Revenue growth in the Immunocytometry Systems unit reflects strong sales of instruments and flow cytometry reagents, driven by increased demand for research analyzers and clinical reagents. Revenue growth in the Discovery Labware unit reflects strong sales of bionutrients and overall market growth. For 2008, we expect the full year revenue growth for the Biosciences Segment to be about 8 to 9%.

Biosciences operating income was \$259 million, or 25.0% of Biosciences revenues in 2007, compared with \$222 million, or 24.2% in 2006. Segment operating income includes an in-process research and development charge of \$7 million in 2007. The increase in operating income, as a percentage of revenues, reflects gross profit improvement from relatively higher sales growth of products that have higher overall gross profit margins and the favorable impact of foreign currency translation. These improvements were offset by manufacturing start-up costs. See further discussion on gross profit margin below. Selling and administrative expense as a percentage of Biosciences revenues was 24.0% versus 25.3% in 2006. Higher sales and continued tight expense control were the key contributors to the increased expense leverage. Research and development expense in 2007 increased \$7 million, or 9.0%, reflecting spending on new product development and advanced technology, particularly in the Immunocytometry Systems unit.

Geographic Revenues

Revenues in the United States in 2007 of \$3.0 billion increased 11%. U.S. sales of safety-engineered devices were approximately \$982 million in 2007, compared with \$917 million in 2006. Growth was also led by strong sales of prefilled flush syringes, prefillable syringes and immunocytometry instruments and reagents. U.S. revenue growth also included \$88 million of revenues from TriPath.

Revenues outside the United States in 2007 increased 11% to \$3.3 billion, reflecting an estimated impact of favorable foreign currency translation of 5 percentage points. Growth was led by solid sales in our European, Asia Pacific and Canadian regions in 2007. International sales of safety-engineered devices were approximately \$409 million in 2007, compared with \$324 million in 2006.

Gross Profit Margin

Gross profit margin was 51.7% in 2007, compared with 51.3% in 2006. Gross profit margin in the current year as compared with the prior year reflected an estimated 0.6% improvement relating to increased sales of products with relatively higher margins as well as productivity gains. These improvements were partially offset by an estimated 0.2% impact from manufacturing start-up costs. We expect gross profit margin in 2008 to be about the same as in 2007. Expected improvements are anticipated to be offset by increased resin and steel costs as well as manufacturing start-up costs in 2008.

Operating Expenses

Selling and administrative expense was \$1.6 billion in 2007 compared with \$1.4 billion in 2006, or 25.2% of revenues in both years. Aggregate expenses for 2007 reflect base spending increases of \$62 million and expenses of \$40 million associated with the GeneOhm and TriPath operations. Increases in selling and administrative expense in 2007 also reflected the absence of proceeds from insurance settlements of \$17 million received in the prior year in connection with our previously-owned latex glove business, as well as an unfavorable foreign exchange impact of \$35 million. Selling and administrative expense as a percentage of revenues is expected to decrease, on a reported basis, by about 70 basis points for 2008.

Research and development ("R&D") expense in 2007 was \$360 million, or 5.7% of revenues, compared with \$302 million, or 5.3% of revenues, in 2006. The increase in R&D expenditures includes spending for new programs in each of our segments, as previously discussed. R&D expense is expected to increase about 11% for 2008.

Operating Income

Operating margin in 2007 was 18.9% of revenues, compared with 19.9% in 2006. Operating income of \$1.2 billion in 2007 reflected \$122 million of acquired in-process R&D charges, as further discussed above. Operating income of \$1.1 billion in 2006 included \$53 million of acquired in-process R&D charges, partially offset by \$17 million of insurance settlement proceeds, as discussed above. We expect operating margin to increase 240 to 250 basis points, with 190 basis points attributable to the acquired in-process R&D charges in 2007.

Non-Operating Expense and Income

Interest expense was \$46 million in 2007, compared with \$66 million in 2006. The decrease reflected lower debt and higher levels of capitalized interest. Interest income was \$46 million in 2007, compared with \$59 million in 2006, resulting from lower cash balances.

Income Taxes

The effective tax rate in 2007 was 28.9% compared with the prior year's rate of 27.6%. The 2007 rate reflected the non-deductibility of the acquired in-process R&D charges of \$122 million, which were partially offset by the impact of approximately 0.3% resulting from the retroactive reinstatement of the research and experimentation tax credit. The 2006 rate reflected the non-deductibility of the acquired in-process R&D charge of \$53 million, as well as the impact relating to the proceeds received from insurance settlements of approximately 0.2%. In 2008, we expect our effective tax rate to be about 27%.

Income and Diluted Earnings per Share from Continuing Operations

Income from continuing operations and diluted earnings per share from continuing operations in 2007 were \$856 million and \$3.36, respectively. The acquired in-process R&D charges decreased income from continuing operations and diluted earnings per share from continuing operations in the aggregate by \$122 million and by \$.48, respectively, in 2007. Income from continuing operations and diluted earnings per share from continuing operations in 2006 were \$815 million and \$3.18, respectively. The acquired in-process R&D charge decreased income from continuing operations and diluted earnings per share from continuing operations by \$53 million and by \$.21, respectively, in 2006.

Discontinued Operations

In September 2006, the Company announced a plan to exit the blood glucose monitoring market. The Company recorded a pre-tax charge of \$63 million in connection with its decision to exit the BGM product line. During the first quarter of 2007, the Company received an unsolicited offer for the purchase of the BGM product line. In December 2006, the Company sold the product line for \$20 million. Following the sale, prior period Consolidated Statements of Income and Cash Flows were restated to separately present the results of the BGM product line as discontinued operations. The September 30, 2006 Consolidated Balance Sheet was not restated. See Note 3 of the Notes to Consolidated Financial Statements for additional discussion.

Financial Instrument Market Risk

We selectively use financial instruments to manage the impact of foreign exchange rate and interest rate fluctuations on earnings. The counterparties to these contracts are highly rated financial institutions. We do not enter into financial instruments for trading or speculative purposes.

We have foreign currency exposures throughout Europe, Asia Pacific, Canada, Japan and Latin America. We face transactional currency exposures that arise when we enter into transactions in non-hyperinflationary countries, generally on an intercompany basis, that are denominated in currencies other than our functional currency. We hedge substantially all such foreign exchange exposures primarily through the use of forward contracts and currency options. We also face currency exposure that arises from translating the results of our worldwide operations to the U.S. dollar at exchange rates that have fluctuated from the beginning of a reporting period. To partially protect against adverse foreign exchange rate movements, we purchase option and forward contracts to hedge certain forecasted sales that are denominated in foreign currencies. Gains or losses on our derivative instruments are largely offset by the gains or losses on the underlying hedged transactions. For foreign currency derivative instruments, market risk is determined by calculating the impact on fair value of an assumed change in foreign exchange rates relative to the U.S. dollar. Fair values were estimated based on market prices, when available, or dealer quotes. The reduction in fair value of our purchased option contracts is limited to the option's fair value. With respect to the derivative instruments outstanding at September 30, 2007, a 10% appreciation of the U.S. dollar over a one-year period would increase pre-tax earnings by \$52 million, while a 10% depreciation of the U.S. dollar would decrease pre-tax earnings by \$10 million.

Comparatively, considering our derivative instruments outstanding at September 30, 2006, a 10% appreciation of the U.S. dollar over a one-year period would have increased pre-tax earnings by \$68 million, while a 10% depreciation of the U.S. dollar would have decreased pre-tax earnings by \$3 million. These calculations do not reflect the impact of exchange gains or losses on the underlying positions that would substantially offset the results of the derivative instruments.

Our primary interest rate exposure results from changes in short-term U.S. dollar interest rates. Our debt and interest-bearing investments at September 30, 2007, are substantially all U.S. dollar-denominated. Therefore, transaction and translation exposure relating to such instruments is minimal. When managing interest rate exposures, we strive to achieve an acceptable balance between fixed and floating rate instruments. We may enter into interest rate swaps to help maintain this balance and manage debt and interest-bearing investments in tandem, since these items have an offsetting impact on interest rate exposure. For interest rate derivative instruments, market risk is determined by calculating the impact to fair value of an assumed change in interest rates across all maturities. Fair values are estimated based on dealer quotes. A change in interest rates on short-term debt and interest-bearing investments is assumed to impact earnings and cash flow, but not fair value because of the short maturities of these instruments. A change in interest rates on long-term debt is assumed to impact fair value but not earnings or cash flow because the interest on such obligations is fixed. Based on our overall interest rate exposure at September 30, 2007 and 2006, a change of 10% in interest rates would not have a material effect on our earnings or cash flows over a one-year period. An increase of 10% in interest rates would decrease the fair value of our long-term debt and interest rate swaps at September 30, 2007 and 2006 by approximately \$37 million and \$39 million, respectively. A 10% decrease in interest rates would increase the fair value of our long-term debt and interest rate swaps at September 30, 2007 and 2006 by approximately \$41 million and \$33 million, respectively.

Liquidity and Capital Resources

Net Cash Flows from Continuing Operating Activities

Net cash provided by continuing operating activities, which continues to be our primary source of funds to finance operating needs and capital expenditures, was \$1.2 billion in 2007, compared with \$1.1 billion in 2006.

Net Cash Flows from Continuing Investing Activities

Net cash used for continuing investing activities in 2007 was \$1.0 billion, compared with \$784 million in 2006. Acquisitions of businesses of \$340 million in 2007 represented the net cash paid for the TriPath acquisition. Capital expenditures were \$556 million in 2007, compared with \$457 million in 2006. Medical capital spending of \$353 million and Diagnostics capital spending of \$114 million in 2007 related primarily to various capacity expansions. Biosciences capital spending of \$73 million in 2007 included spending on manufacturing capacity expansions. In 2008, capital expenditures are expected to be in the \$600 to \$650 million range, reflecting investments in various manufacturing capacity and facility expansions.

Net Cash Flows from Continuing Financing Activities

Net cash used for financing activities was \$726 million in 2007, as compared with \$342 million in 2006, and included the repurchase of shares of our common stock for approximately \$450 million, compared with approximately \$449 million in 2006. At September 30, 2007, approximately 11.1 million common shares remained available for purchase, consisting of 1.1 million shares remaining under a November 2005 Board of Directors' authorization to repurchase up to 10 million common shares, plus an additional 10 million shares that were authorized for repurchase by the Board of Directors in July 2007. For 2008, we expect that cash used to repurchase common shares will be about \$450 million. Total debt at September 30, 2007, was \$1.2 billion compared with \$1.4 billion at September 30, 2006. Short-term debt decreased to 18% of total debt at year-end, from 31% at the end of 2006. Floating rate debt was 36% of total debt at the end of 2007 and 46% at the end of 2006. Our weighted average cost of total debt at the end of 2007 was 5.7%, up from 5.5% at the end of 2006. Debt-to-capitalization at year-end improved to 20.9% from 25.8% last year.

We have in place a commercial paper borrowing program that is available to meet our short-term financing needs, including working capital requirements. Borrowings outstanding under this program were \$200 million at September 30, 2007. We maintain a \$1.0 billion syndicated credit facility in order to provide backup support for our commercial paper program and for other general corporate purposes. This credit facility expires in December 2012 and includes a single financial covenant that requires BD to maintain an interest expense coverage ratio (ratio of earnings before income taxes, depreciation and amortization to interest expense) of not less than 5-to-1 for the most recent four consecutive fiscal quarters. On the last eight measurement dates, this ratio had ranged from 17-to-1 to 23-to-1. There were no borrowings outstanding under this facility at September 30, 2007. In addition, we have informal lines of credit outside the United States.

At September 30, 2007, our long-term debt was rated "A2" by Moody's and "A+" by Standard and Poor's, and our commercial paper ratings were "P-1" by Moody's and "A-1" by Standard and Poor's. Given the availability of the various credit facilities and our strong credit ratings, we continue to have a high degree of confidence in our ability to refinance maturing short-term and long-term debt, as well as to incur substantial additional debt, if required.

BD's ability to generate cash flow from operations, issue debt, enter into other financing arrangements and attract long-term capital on acceptable terms could be adversely affected in the event there was a material decline in the demand for BD's products, deterioration in BD's key financial ratios or credit ratings or other significantly unfavorable changes in conditions. While a deterioration in the Company's credit ratings would increase the costs associated with maintaining and borrowing under its existing credit arrangements, such a downgrade would not affect the Company's ability to draw on these credit facilities, nor would it result in an acceleration of the scheduled maturities of any outstanding debt.

Contractual Obligations

In the normal course of business, we enter into contracts and commitments that obligate us to make payments in the future. The table below sets forth BD's significant contractual obligations and related scheduled payments:

(millions of dollars)	Total	2009 to 2008	2011 to 2010	2013 and 2012	Thereafter
Short-term debt	\$ 208	\$208	\$ —	\$ —	\$ —
Long-term debt ^(A)	1,594	54	301	85	1,154
Operating leases	153	46	59	32	16
Purchase obligations ^(B)	365	296	50	19	—
Total^(C)	\$2,320	\$604	\$410	\$136	\$1,170

(A) Long-term debt obligations include expected principal and interest obligations, including interest rate swaps. The interest rate forward curve at September 30, 2007 was used to compute the amount of the contractual obligation for variable rate debt instruments and swaps.

(B) Purchase obligations are for purchases made in the normal course of business to meet operational and capital requirements.

(C) Required funding obligations for 2008 relating to pension and other postretirement benefit plans are not expected to be material.

2006 Compared With 2005

Worldwide revenues in 2006 of \$5.7 billion increased 7% from 2005 and reflected estimated volume increases of 7%, an estimated decrease due to unfavorable foreign currency translation of 1%, and estimated price increases of less than 1%.

Medical Segment

Medical revenues in 2006 of \$3.1 billion increased \$222 million, or 8%, over 2005.

The following is a summary of revenues by organizational unit:

(millions of dollars)	2006	2005	Estimated Foreign	
			Total Change*	Exchange Impact
Medical Surgical Systems	\$1,749	\$1,661	5%	—
Diabetes Care	657	600	9%	(1%)
Pharmaceutical Systems	640	563	14%	(3%)
Ophthalmic Systems	62	60	3%	(2%)
Total Revenues*	\$3,107	\$2,884	8%	(1%)

* Amounts may not calculate due to rounding.

Medical revenue growth was driven by the continued conversion to safety-engineered products, which accounted for sales of \$613 million, as compared with \$571 million in the prior year, reflecting growth of 6% in the United States and 16% internationally. Revenue growth in the Medical Surgical Systems unit of this segment was primarily driven by the growth in safety-engineered products and prefilled flush syringes. Revenue growth in the Pharmaceutical Systems unit was driven by a 26% increase in sales in the United States. The Diabetes Care unit's revenue growth reflected strong sales of pen needles worldwide.

Medical operating income was \$864 million, or 27.8% of Medical revenues, in 2006, as compared with \$748 million, or 25.9% in 2005. The Segment's gross profit margin in 2006 reflected improvement associated with relatively higher sales growth of products that have higher overall gross profit margins, in particular, safety-engineered products and pen needles, as well as favorable manufacturing efficiencies associated with higher volumes. See further discussion on gross profit margin below. Selling and administrative expense as a percent of Medical revenues in 2006 was slightly lower compared with 2005, primarily due to tight expense controls over base spending. Research and development expense in 2006 increased \$7 million, or 8%, reflecting continued investment in the development of new products and platforms.

Diagnostics Segment

Diagnostics revenues in 2006 of \$1.7 billion increased \$83 million, or 5%, over 2005, which reflected an estimated unfavorable impact of foreign currency translation of about 1 percentage point.

The following is a summary of revenues by organizational unit:

(millions of dollars)	2006	2005	Estimated Foreign	
			Total Change	Exchange Impact
Preanalytical Systems	\$ 928	\$ 855	9%	—
Diagnostic Systems	787	777	1%	(1%)
Total Revenues	\$1,715	\$1,632	5%	(1%)

Revenue growth in the Preanalytical Systems unit was driven by the continued conversion to safety-engineered products, which accounted for sales of \$627 million, as compared with \$543 million in 2005. Sales of safety-engineered products reflected growth of 13% in the United States, which benefited from *BD Vacutainer* Push Button Blood Collection Set conversion activity, and 20% internationally. The Diagnostic Systems unit experienced solid worldwide sales of its automated diagnostic platforms, including the molecular *BD ProbeTec* ET, *BD BACTEC*, and the *BD Phoenix* ID/AST. These platforms reported combined incremental sales of \$33 million over 2005. Revenues for GeneOhm, which was acquired in February 2006, totaled \$8 million. Sales of flu diagnostic tests declined by approximately \$11 million in fiscal 2006 compared with 2005, primarily due to a relatively mild flu season in both Japan and the United States.

Diagnostics operating income was \$390 million, or 22.8% of Diagnostics revenues, in 2006, compared with \$403 million, or 24.7%, in 2005. Segment operating income for 2006 reflects the acquired in-process research and development charge of \$53 million as well as the operating results of GeneOhm, which in the aggregate, reduced operating income as a percentage of Diagnostics revenues by approximately 5%. The Diagnostics Segment experienced slight gross profit margin improvement reflecting higher prices and productivity, which was substantially offset by the impact of the recently acquired GeneOhm products, which have lower overall gross profit margins, and lower sales growth of flu diagnostic products, which have higher overall gross profit margins. See further discussion on gross profit margin below. Selling and administrative expense as a percent of Diagnostics revenues in 2006 was lower compared with 2005 primarily due to tight controls on spending, which more than offset the incremental GeneOhm expenses. Research and development expense in 2006 increased \$6 million, or 7%, reflecting new spending for product development associated with the GeneOhm acquisition.

Biosciences Segment

Biosciences revenues in 2006 of \$916 million increased \$92 million, or 11%, over 2005, which reflected an estimated impact of unfavorable foreign currency translation of 1 percentage point.

The following is a summary of revenues by organizational unit:

(millions of dollars)	2006	2005	Total Change*	Estimated
				Foreign Exchange Impact
Immunocytometry Systems	\$503	\$452	11%	(1%)
Discovery Labware	256	231	11%	(1%)
Pharmingen	157	141	12%	(1%)
Total Revenues	\$916	\$824	11%	(1%)

* Amounts may not calculate due to rounding.

Revenue growth in the Immunocytometry Systems unit reflected strong sales of instruments and flow cytometry reagents, driven by increased demand for research and clinical analyzers. Revenue growth rates in the Immunocytometry Systems and Pharmingen units were favorably impacted by the adverse effect a cancellation of a distribution agreement had on revenues in 2005. As a result of an inventory repurchase obligation to this distributor upon termination of the arrangement, certain sales made to this distributor in the latter part of 2005 (\$5 million in Immunocytometry Systems and \$12 million in Pharmingen) were not recognized as revenue. In addition, sales in 2006 were favorably impacted by higher average selling prices as a result of terminating the arrangement. Revenue growth in the Discovery Labware unit resulted primarily from strong sales of bionutrients and market share gains.

Biosciences operating income was \$222 million, or 24.2% of Biosciences revenues in 2006, compared with \$186 million, or 22.5% in 2005. The increase in operating income, as a percentage of revenues, reflects gross profit improvement from the favorable impact of terminating a distribution agreement in 2005, increased operating efficiencies, as well as relatively higher sales growth of products that have higher overall gross profit margins. See further discussion on gross profit margin below. Selling and administrative expense as a percent of Biosciences revenues was lower compared with 2005, primarily due to higher revenues and the absence of \$8 million of costs incurred in 2005 associated with the termination of the distribution agreement, mentioned above. Research and development expense in 2006 increased \$8 million, or 13%, reflecting spending on new product development and advanced technology, particularly in the Immunocytometry Systems unit and bioimaging products.

Geographic Revenues

Revenues in the United States in 2006 of \$2.7 billion increased 9%. U.S. sales of safety-engineered devices were approximately \$917 million in 2006, compared with \$842 million in 2005. Growth was also led by strong sales of diabetes care products, prefilled flush syringes and prefillable syringes. Revenues of immunocytometry instruments and reagents also demonstrated good growth.

Revenues outside the United States in 2006 increased 6% to \$3 billion, reflecting an estimated impact of unfavorable foreign currency translation of 2 percentage points. Growth was led by strong sales in our Asia Pacific, Canadian and European regions in 2006. International sales of safety-engineered devices were approximately \$324 million in 2006, compared with \$273 million in 2005.

Gross Profit Margin

Gross profit margin was 51.3% in 2006, compared with 50.9% in 2005. Gross profit margin in 2006 reflected an estimated 1.0% improvement relating to increased sales growth of products with relatively higher margins and to productivity gains. These improvements were partially offset by an estimated 0.2% impact from foreign currency translation, an estimated 0.3% unfavorable impact of higher raw material costs and 0.1% relating to an increase in share-based compensation.

Operating Expenses

Selling and administrative expense of \$1.4 billion in 2006 was 25.2% of revenues, compared with \$1.4 billion or 26.0% of revenues in 2005. Aggregate expenses for 2006 reflect base spending increases of \$49 million and expenses associated with recent acquisitions, primarily GeneOhm, of \$17 million. Selling and administrative expense in 2006 also reflected increases primarily in share-based compensation expense of \$25 million. These increases were partially offset by a favorable foreign exchange impact of \$13 million and by proceeds from insurance settlements of \$17 million received in connection with our previously-owned latex glove business.

Research and development expense in 2006 was \$302 million, or 5.3% of revenues, compared with \$268 million, or 5.0% of revenues, in 2005. The increase in R&D expenditures reflected spending for new programs in each of our segments, as previously discussed.

Non-Operating Expense and Income

Interest expense was \$66 million in 2006, compared with \$56 million in 2005. The increase reflected higher debt levels and the impact of higher interest rates on floating rate debt and on fixed-to-floating interest rate swap transactions. Such swap transactions consist of fair value hedges of certain fixed-rate instruments under which the difference between fixed and floating interest rates is exchanged at specified intervals. Interest income was \$59 million in 2006, compared with \$36 million in 2005, and reflected higher interest rates and cash balances.

Income Taxes

The effective tax rate in 2006 was 27.6% and reflected the unfavorable impact of the non-deductibility of the acquired in-process R&D charge. The effective tax rate in 2005 was 31.3% and reflected a 7.7% increase relating to the charge in 2005 attributable to the planned repatriation of earnings in 2006 under the American Jobs Creation Act of 2004. In addition, the effective tax rate in 2005 reflected a 1.0% benefit due to the reversal of tax accruals in connection with the conclusion of tax examinations in four non-U.S. jurisdictions.

Income and Diluted Earnings per Share from Continuing Operations

Income from continuing operations and diluted earnings per share from continuing operations in 2006 were \$815 million and \$3.18, respectively. The in-process R&D charge decreased income from continuing operations and diluted earnings per share from continuing operations by \$53 million and by \$.21 in 2006. Income from continuing operations and diluted earnings per share from continuing operations in 2005 were \$713 million and \$2.73, respectively. The tax repatriation charge decreased income from continuing operations by \$77 million and diluted earnings per share from continuing operations by \$.30 in 2005.

Liquidity and Capital Resources

Net Cash Flows from Continuing Operating Activities

Net cash provided by continuing operating activities was \$1.1 billion in 2006, reduced from \$1.2 billion in 2005, reflecting higher inventory levels and higher income tax payments, including taxes associated with the repatriation of earnings, as discussed further below.

Net Cash Flows from Continuing Investing Activities

Net cash used for continuing investing activities in 2006 was \$784 million, compared with \$380 million in 2005. Acquisitions of businesses of \$231 million in 2006 represented the net cash paid for the GeneOhm acquisition. Capital expenditures were \$457 million in 2006, compared with \$316 million in 2005. Medical capital spending of \$269 million and Diagnostics capital spending of \$105 million related primarily to various capacity expansions. Biosciences capital spending of \$39 million included spending on manufacturing capacity expansions.

Net Cash Flows from Continuing Financing Activities

Net cash used for financing activities was \$342 million in 2006, as compared with \$516 million in 2005, and included the repurchase of shares of our common stock for approximately \$449 million, compared with approximately \$550 million in 2005. Total debt at September 30, 2006, was \$1.4 billion compared with \$1.3 billion at September 30, 2005. Short-term debt increased to 31% of total debt at year-end, from 16% at the end of 2005. Floating rate debt was 46% of total debt at the end of 2006 and 41% at the end of 2005. Our weighted average cost of total debt at the end of 2006 was 5.5%, up from 5.3% at the end of 2005, due to higher short-term interest rates. Debt-to-capitalization at year-end improved to 25.8% in 2006 from 27.1% in 2005.

The American Jobs Creation Act of 2004 (the "AJCA") was signed into law in October 2004. The AJCA creates a temporary incentive for U.S. multinationals to repatriate accumulated income earned outside the United States. As a result of the passage of the AJCA, we repatriated approximately \$1.3 billion in 2006 in accordance with our planned repatriation under the AJCA. Uses of the repatriated funds include cash expenditures for compensation and benefits to existing and newly hired U.S. workers, U.S. infrastructure and capital investments and other activities as permitted under the AJCA.

Critical Accounting Policies

The preparation of the consolidated financial statements requires management to use estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, as well as the disclosure of contingent assets and liabilities at the date of the consolidated financial statements. Some of those judgments can be subjective and complex and, consequently, actual results could differ from those estimates. Management bases its estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. For any given estimate or assumption made by management, it is possible that other people applying reasonable judgment to the same facts and circumstances could develop different estimates. Actual results that differ from management's estimates could have an unfavorable effect on our consolidated financial statements. Management believes the following critical accounting policies reflect the more significant judgments and estimates used in the preparation of the consolidated financial statements.

Revenue Recognition

Revenue from product sales is recognized when title and risk of loss pass to the customer. We recognize revenue for certain instruments sold from the Biosciences segment upon installation at a customer's site. Based upon terms of the sales agreements, the Biosciences segment recognizes revenue in accordance with Emerging Issues Task Force No. 00-21, "Revenue Arrangements with Multiple Deliverables." These sales agreements have multiple deliverables, and as such are divided into separate units of accounting. Revenue is recognized upon the completion of each deliverable based on the relative fair values of items delivered.

BD's domestic businesses sell products primarily to distributors who resell the products to end-user customers. We provide rebates to distributors that sell to end-user customers at prices determined under a contract between BD and the end-user customer. Provisions for rebates, as well as sales discounts and returns, are accounted for as a reduction of revenues when revenue is recognized.

Impairment of Assets

Pursuant to SFAS No. 142, “Goodwill and Other Intangible Assets,” goodwill and indefinite-lived intangible assets are subject to impairment reviews at least annually, or whenever indicators of impairment arise. Intangible assets other than goodwill and indefinite-lived intangible assets and other long-lived assets are reviewed for impairment in accordance with SFAS No. 144, “Accounting for the Impairment or Disposal of Long-Lived Assets.” Impairment reviews are based on a cash flow approach that requires significant management judgment with respect to future volume, revenue and expense growth rates, changes in working capital use, appropriate discount rates and other assumptions and estimates. The estimates and assumptions used are consistent with BD’s business plans. The use of alternative estimates and assumptions could increase or decrease the estimated fair value of the asset, and potentially result in different impacts to BD’s results of operations. Actual results may differ from management’s estimates.

Investments

We hold equity interests in companies having operations or technology in areas within or adjacent to BD’s strategic focus. For some of these companies that are publicly traded, market prices are available. However, for those companies that are not publicly traded, fair value is difficult to determine. We write down an investment when management believes an investment has experienced a decline in value that is other than temporary. Future adverse changes in market conditions or poor operating results of the underlying investments could result in an inability to recover the carrying value of the investments, thereby possibly requiring impairment charges in the future.

Tax Valuation Allowances

BD maintains valuation allowances where it is more likely than not that all or a portion of a deferred tax asset will not be realized. Changes in valuation allowances are included in our tax provision in the period of change. In determining whether a valuation allowance is warranted, management evaluates factors such as prior earnings history, expected future earnings, carryback and carryforward periods, and tax strategies that could potentially enhance the likelihood of realization of a deferred tax asset.

Contingencies

We are involved, both as a plaintiff and a defendant, in various legal proceedings that arise in the ordinary course of business, including, without limitation, product liability, antitrust, and environmental matters, as further discussed in Note 12 of the Notes to Consolidated Financial Statements. We assess the likelihood of any adverse judgments or outcomes to these matters as well as potential ranges of probable losses. In accordance with U.S. generally accepted accounting principles, we establish accruals to the extent probable future losses are estimable (in the case of environmental matters, without considering possible third-party recoveries). A determination of the amount of accruals, if any, for these contingencies is made after careful analysis of each individual issue and, when appropriate, is developed after consultation with outside counsel. The accruals may change in the future due to new developments in each matter or changes in our strategy in dealing with these matters.

Given the uncertain nature of litigation generally, we are not able in all cases to estimate the amount or range of loss that could result from an unfavorable outcome of the litigation to which we are a party. In view of these uncertainties, we could incur charges in excess of any currently established accruals and, to the extent available, excess liability insurance. Accordingly, in the opinion of management, any such future charges, individually or in the aggregate, could have a material adverse effect on BD’s consolidated results of operations and consolidated net cash flows.

Benefit Plans

We have significant net pension and postretirement benefit costs that are measured using actuarial valuations. Inherent in these valuations are key assumptions including discount rates and expected return on plan assets. We evaluate these key assumptions at least annually on a plan- and country-specific basis. We consider current market conditions, including changes in interest rates and market returns, in selecting these assumptions. Changes in the related net pension and post-retirement benefits costs may occur in the future due to changes in assumptions.

The discount rate is selected to reflect the prevailing rate on September 30 based on investment grade bonds and other factors. Specifically, for the U.S. pension plan, we use an actuarially-determined yield curve to determine the discount rate. We increased our discount rate for the U.S. pension and postretirement plans at September 30, 2007 from 5.95% to 6.35% and increased the rate at September 30, 2006 from 5.5% to 5.95%.

To determine the expected long-term rate of return on pension plan assets, we consider the historical and expected returns on various plan asset classes, as well as current and expected asset allocations. At September 30, 2007, the one-year rate of return on assets for our U.S. pension plans was 14.6%, the five-year rate of return was 13.0%, and the ten-year rate of return was 6.5%. We believe that these results, in connection with our current and expected asset allocation, support our assumed long-term return of 8.0% on those assets.

Sensitivity to changes in key assumptions for our U.S. pension and postretirement plans are as follows:

- Discount rate—A change of plus (minus) 25 basis points, with other assumptions held constant, would have an estimated \$7 million favorable (unfavorable) impact on the total U.S. net pension and postretirement benefit plan cost.
- Expected return on plan assets—A change of plus (minus) 25 basis points, with other assumptions held constant, would have an estimated \$2 million favorable (unfavorable) impact on U.S. pension plan cost.

Stock-Based Compensation

Compensation cost relating to share-based payment transactions is recognized in net income using a fair value measurement method, in accordance with SFAS No. 123(R). SFAS No. 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the statement of operations as compensation expense (based on their fair values) over the vesting period of the awards. We determine the fair value of certain share-based awards using a lattice-based binomial option valuation model that incorporates certain assumptions, such as the risk-free interest rate, expected volatility, expected dividend yield and expected life of the options. See Note 13 of the Notes to Consolidated Financial Statements for additional discussion.

Cautionary Statement Regarding Forward-Looking Statements

BD and its representatives may from time-to-time make certain forward-looking statements in publicly released materials, both written and oral, including statements contained in this report and filings with the Securities and Exchange Commission and in our other reports to shareholders. Forward-looking statements may be identified by the use of words such as “plan,” “expect,” “believe,” “intend,” “will,” “anticipate,” “estimate” and other words of similar meaning in conjunction with, among other things, discussions of future operations and financial performance, as well as our strategy for growth, product development, regulatory approvals, market position and expenditures.

All statements that address operating performance or events or developments that we expect or anticipate will occur in the future—including statements relating to volume growth, sales and earnings per share growth and statements expressing views about future operating results—are forward-looking statements.

Forward-looking statements are based on current expectations of future events. The forward-looking statements are, and will be, based on management’s then-current views and assumptions regarding future events and operating performance, and speak only as of their dates. Investors should realize that if underlying assumptions prove inaccurate or unknown risks or uncertainties materialize, actual results could vary materially from our expectations and projections. Investors are therefore cautioned not to place undue reliance on any forward-looking statements. Furthermore, we undertake no obligation to update or revise any forward-looking statements whether as a result of new information, future events and developments or otherwise.

The following are some important factors that could cause our actual results to differ from our expectations in any forward-looking statements:

- Regional, national and foreign economic factors, including inflation and fluctuations in interest rates and foreign currency exchange rates and the potential effect of such fluctuations on revenues, expenses and resulting margins, as well as competition in certain markets.
- We operate in a highly competitive environment. New product introductions by our current or future competitors (for example, new forms of drug delivery) could adversely affect our ability to compete in the global market. Patents attained by competitors, particularly as patents on our products expire, may also adversely impact our competitive position. Certain competitors have established manufacturing sites or have contracted with suppliers in low-cost manufacturing locations as a means to lower their costs. New entrants may also appear.
- Changes in domestic and foreign healthcare industry practices and regulations resulting in increased pricing pressures, including the continued consolidation among healthcare providers; trends toward managed care and healthcare cost containment; and government laws and regulations relating to sales and promotion, reimbursement and pricing generally.
- The effects, if any, of governmental and media activities regarding the business practices of group purchasing organizations, which negotiate product prices on behalf of their member hospitals with BD and other suppliers.

- Fluctuations in the cost and availability of oil-based resins and other raw materials and the ability to maintain favorable supplier arrangements and relationships (particularly with respect to sole-source suppliers) and the potential adverse effects of any disruption in the availability of such raw materials.
- Our ability to obtain the anticipated benefits of restructuring programs, if any, that we may undertake.
- Adoption of or changes in government laws and regulations affecting domestic and foreign operations, including those relating to trade, monetary and fiscal policies, taxation, environmental matters, sales practices, price controls, licensing and regulatory approval of new products, regulatory requirements for products in the postmarketing phase, or changes in enforcement practices with respect to any such laws and regulations. In particular, environmental laws, particularly with respect to the emission of greenhouse gases, are becoming more stringent throughout the world, which may increase our costs of operations or necessitate changes in our manufacturing plants or processes.
- Fluctuations in U.S. and international governmental funding and policies for life sciences research.
- Difficulties inherent in product development, including the potential inability to successfully continue technological innovation, complete clinical trials, obtain regulatory approvals in the United States and abroad, obtain coverage and adequate reimbursement for new products, or gain and maintain market approval of products, as well as the possibility of encountering infringement claims by competitors with respect to patent or other intellectual property rights, all of which can preclude or delay commercialization of a product.
- Pending and potential litigation or other proceedings adverse to BD, including antitrust claims, product liability claims, patent infringement claims and the availability or collectibility of insurance.
- The effects, if any, of adverse media exposure or other publicity regarding BD's business or operations.
- Our ability to achieve earnings forecasts, which are generated based on projected volumes and sales of many product types, some of which are more profitable than others. There can be no assurance that we will achieve any projected level or mix of product sales.
- The effect of market fluctuations on the value of assets in BD's pension plans and the possibility that BD may need to make additional contributions to the plans as a result of any decline in the value of such assets.
- Our ability to effect infrastructure enhancements and incorporate new systems technologies into our operations.
- Product efficacy or safety concerns resulting in product recalls, regulatory action on the part of the U.S. Food and Drug Administration (or foreign counterparts) or declining sales.
- Economic and political conditions in international markets, including civil unrest, terrorist activity, governmental changes, restrictions on the ability to transfer capital across borders and expropriation of assets by a government.
- The effects of natural disasters, including hurricanes or pandemic diseases, on our ability to manufacture our products, particularly where production of a product line is concentrated in one or more plants, or on our ability to source components from suppliers that are needed for such manufacturing.
- Our ability to penetrate developing and emerging markets, which also depends on economic and political conditions, and how well we are able to acquire or form strategic business alliances with local companies and make necessary infrastructure enhancements to production facilities, distribution networks, sales equipment and technology.
- The impact of business combinations, including acquisitions and divestitures, both internally for BD and externally in the healthcare industry.
- Issuance of new or revised accounting standards by the Financial Accounting Standards Board or the Securities and Exchange Commission.

The foregoing list sets forth many, but not all, of the factors that could impact our ability to achieve results described in any forward-looking statements. Investors should understand that it is not possible to predict or identify all such factors and should not consider this list to be a complete statement of all potential risks and uncertainties.