Letter to the Shareholders

As we all know, this last year's great achievement was the launch of Celexa™ in September, 1998. It is already our largest product and it is likely that it will ultimately more than double our sales, and take us well past a billion dollars in volume—still modest for a pharmaceutical company, but enough to enrich shareholders and employee option holders, perhaps more than some larger companies. Sales of Celexa in the quarter ended December 31, 1998 were $20,885,000. In the quarter ended March 31, 1999 sales were $50,011,000, and we expect that sales in this quarter ending June 30, 1999 will be well ahead of the previous quarters. Already over 100,000 physicians have written prescriptions for Celexa, and 75% have written it multiple times. Most impressive of all, Celexa's total number of prescriptions has exceeded that of every other selective serotonin reuptake inhibitor (SSRI) over the same period after introduction. And this result is all the more remarkable because Celexa, being the last entry, has to draw its prescriptions principally from three established highly promoted competitive products.

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The reason for this success lies ultimately in the virtues of the product itself, and the fact that they have been effectively communicated to physicians. Quite simply, Celexa is perceived as a product with minimal side effects, less drug interaction and possibly faster onset of action. There are many patients whose depression is alleviated by Celexa who have previously not been able to find relief from any available antidepressants, either because of the lack of effectiveness or because of intolerable side effects. In fact, Celexa, as we expected, was often first used by physicians for their recalcitrant patients and it was its success with these harder to treat patients that has led so many physicians to prescribe Celexa for more and more of their patients. Indeed, the many anecdotal experiences that have been communicated to us have been very moving. There is a satisfaction beyond profits in the heartwarming experience of participating in bringing relief to the unfortunate people suffering so greatly from their depression.

No drug is perfect for everyone, and so pharmaceutical companies are constantly attempting to improve their products so that the profile, even of the best product, is made even better. The object is to serve a still larger patient group with even more and earlier effectiveness and with even less or no side effects for those patients, even if a limited number, who may suffer from side effects. And that is what we and our Danish licensor, H. Lundbeck A/S, are attempting with Celexa. The results thus far, although very early, indicate that we may be successful. Celexa is a racemate, which is to say that it consists of a mixture of two types of molecules, which are mirror images of each other. Sometimes one of two mirror image molecules, called an enantiomer, has different effects

than the other molecule because of differing binding properties to the target cells in the body. And sometimes, therefore, one of the enantiomers may have a purity and breadth of benefit that surpasses the racemate form. We and Lundbeck have successfully separated the Celexa enantiomers and, after promising pharmacological studies, we are planning for studies in patients later this year. The active enantiomer has the additional advantage of patent protection until 2009.

The launch of Celexa presented an extraordinary challenge for Forest which had only 650 sales representatives and total sales of under $500,000,000. It was a daunting undertaking for us to launch a product in a five billion dollar market dominated by three of the most powerful marketers in the industry, each of whom had thousands of sales representatives promoting their product, who were well established with the prescribing physicians, including psychiatrists whom we had never called on before, and who were each spending many tens of millions of dollars in promotion every year. We had the option of just doing the best we could as a small player and obtaining a modest market share—perhaps as much as 5%—using our own limited facilities. That is what our competitors and some investors expected. But we recognized the product's essential virtues and the incomparable opportunity we had in the vast and growing market for depression drugs. We decided therefore to try to make Celexa a truly major product. But we were also aware that the commitment of resources necessary would substantially impair our earnings for several years as well as risk future earnings and share value. And so we sought and achieved two transactions that brought the risk and the impact on our earnings within manageable limits at the cost of sharing some of the future opportunity. At the same time, we were able to preserve the major share of that opportunity for Forest.

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We brought in two partners—a private investment group, and the Parke-Davis Division of the Warner-Lambert Company. The investors provided sixty million dollars which enabled us to both increase our salesforce to 850 representatives and to cover a portion of the clinical study and prelaunch costs of Celexa in exchange for a royalty on Celexa sales with a buy-out option. The transaction with Parke-Davis brought us a highly successful marketing and sales organization to provide a substantial portion of the physician detailing effort, again in exchange for a portion of the opportunity. It was these two transactions involving some risk for both partners but now clearly highly profitable for both, which enabled us to provide Celexa with the support which accounts for its success. The investors provided money—a fungible and impersonal commodity, but Parke-Davis provided people, extraordinarily talented, creative and dedicated marketing and sales personnel, who demonstrated again, in this partnership, why Parke-Davis is rightfully regarded as one of the industry's most successful marketers.

Their sales effort complemented the superlative performance of our own salesforce. In anticipation of the launch of Celexa, we expanded our salesforce to 850 representatives, divided into three salesforces, two to call on primary care physicians and psychiatrists and a specialty salesforce to visit hospitals and specialists including psychiatrists. We realigned representatives' territories, created new divisions and managers and augmented their efforts with a group of specially

trained pharmacists to visit the opinion leading physicians. It was a monumental undertaking, and its successful outcome, in so short a period of time, was a prodigious accomplishment by our marketing and sales departments. And, of course, we had to augment all of our manufacturing, packaging, laboratory and financial personnel and facilities to accommodate the dramatically increased sales levels. All of this was accomplished in an efficient and timely manner. Pending completion of the expansion of our plant in Ireland where Celexa is manufactured, we are operating on a three shift basis, which requires extraordinary management skills and worker commitment. Lundbeck, our licensor and the supplier of bulk drug, has never failed to meet our supply needs while they also increase their manufacturing facilities.

It is interesting, as we enjoy these dynamic developments, to reflect that Forest started in the United States as a generic company. We then became a drug delivery company developing controlled release formulations for other companies using our patented Synchron® technology. We then became our own marketer of smaller licensed products. And we are now a full scale marketer of full scale products, and as we move on to other product opportunities, our continued growth will be facilitated by our still greater marketing prowess and a growing licensing and in-house research capacity.

Of course, not every strategy or product has worked out exactly as we had hoped, and the forces of competition, scientific developments, and marketing and regulatory obstacles have affected us as they have every one else in the industry. No path to success is an unencumbered straight line. Sales of Monurol®, a urinary tract infection antibiotic, have been disappointing, although not because of any flaws in the product. We are still expecting to introduce Infasurf®, a lung surfactant for treating respiratory distress in premature babies, but the delay due to patent and regulatory obstacles has been costly. On the other hand, although Aerobid®, our inhaled corticosteroid for asthma, which for years was our major growth product, has stagnated in the face of serious competition, we expect it to resume its place as a growth product when our new non-CFC forms of Aerobid, with improved taste and delivery, are available within two years. And Tiazac®, our unique formulation of diltiazem for hypertension, is doing exceedingly well, with sales of $132,000,000 in the last fiscal year compared to $86,000,000 in the prior year, and we expect still greater sales this year.

We are well aware that we must maintain a better than average growth rate in earnings and the expectation of continuing that growth rate in order to steadily increase the Company's value. And that obviously requires products to augment and succeed Celexa in several years when its rapid growth is likely to moderate. That is an intense focus in Forest, now more than ever. For the time being, we continue to depend on licensing in products where the basic molecule has been discovered by other companies, and where we may acquire rights at any phase of development, from as early as the identification of a new molecule to as late as after FDA approval. Our perception is that, if anything, our ability to obtain these products is more favorable then ever before because the opportunities are more prolific and we are an even more desirable partner. We have many

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projects under way all the time, most of which, like most research, will not result in marketed products. But some will—more than enough to maintain a favorable growth path along with and succeeding Celexa. With respect to our joint venture with Lundbeck, for example, there are two products discovered by Lundbeck actively being developed. One is a product for urinary incontinence which, based on preclinical work, may have therapeutic efficacy equal to or better than products presently marketed without the undesirable side effects which ultimately discourage many patients from initiating or continuing drug therapy. The other product is an anxiolytic, still early in preclinical testing.

There is one other matter that I feel particularly strongly about. We, like almost every company in every industry these days, are prey to marauding strike suit attorneys who involve us in totally baseless and highly expensive litigation, often class action suits, with the expectation of lucrative settlements benefitting the attorneys and seldom the plaintiffs themselves who frequently have no real grievance to start with except the ones concocted by the attorneys. Of course, there are abusive companies and plaintiffs with genuine losses and suits with genuine merits, and no one would advocate eliminating the opportunity for legal redress. But the abuse of our legal system, particularly in class action litigation, is a calamity which companies have to endure, the burdens of which are ultimately passed on to the general public in higher costs—of health care, for example.

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Our policy has been to resist settling these cases and to litigate them to the bitter end. We have been involved in two such litigations—one which was concluded a few years ago after several years of litigation which was commenced when our stock declined because we announced that unfortunately a product for which we were seeking regulatory approval had to be abandoned because of side effects that developed in Europe where it was already approved. After extensive pretrial discovery and a full trial, the case was dismissed by the court for lack of merit. The other group of cases is the multi-drug antitrust litigation accusing almost all pharmaceutical companies of conspiring together to maintain higher drug prices. I do not actually know what other companies did or did not do although I seriously doubt that such a conspiracy existed among any of them. But I certainly know that we were not party to any conspiracy. I believe the plaintiffs' attorneys knew that they had no credible evidence that we were part of any conspiracy, and that they joined us in this litigation solely to add another pocket from which to extort a settlement. We, together with some of the more intrepid defendants, refused to settle. After millions of dollars of pretrial and trial expenses, the court threw out the case at the trial after the plaintiffs presented their case without even hearing from the defendants because the case was so clearly frivolous. Other defendants had previously settled for a total of $720,000,000, certainly no badge of courage. We subsequently moved for and obtained sanctions against the plaintiffs' attorneys of approximately $2,100,000 because the court found that the plaintiffs' attorneys had deliberately misled it. Clearly there have to be effective methods of curtailing these abusive proceedings which penalize all of us for the benefit of an unprincipled few.

During the last year, there were several changes in the senior management at Forest. After fourteen years, Phil Satow elected to retire as Executive Vice President, Marketing and Sales. Phil virtually created both our marketing and sales departments and led them through their growth to their present eminence, including the extraordinarily successful launch of Celexa. His contribution has been unique and invaluable and Forest will continue to be deeply imprinted with the high standards and achievements he represented. He will continue to serve as a director of Forest. Raymond Stafford, who has been responsible for our European operations, primarily Pharmax in the United Kingdom and Tosara in Ireland, has been elected Forest's Executive Vice President, Global Marketing. He has been employed by Forest since 1987, when we purchased Tosara from him and his partners. Elaine Hochberg, who had been marketing Vice President of our subsidiary, Forest Pharmaceuticals for two years, has been elected Vice President of Forest with principal responsibilities for marketing in the United States. I believe we have in place exceedingly strong marketing management which will skillfully continue the success we have enjoyed under Phil Satow's leadership.

The other significant change is that Ken Goodman has been elected President and Chief Operating Officer and I have become Chairman and continue as Chief Executive Officer. John Eggers has succeeded Ken as Vice President, Finance, and Chief Financial Officer. I have worked with Ken Goodman for nineteen years and there is no achievement of Forest's which is not infused with his keen analytical skills and his wisdom. In a sense he has been the de facto chief operating officer of Forest for years, and we will surely benefit in the future, as we already have, from his brilliant leadership. Larry Olanoff, formerly Senior Vice President, Scientific Affairs, has been elected Executive Vice President, Scientific Affairs. His and his group's achievements in preparing an enormous Celexa submission which had to detail the product's lengthy experience in the many countries in which it had already been approved, and in guiding the submission through the regulatory process, was an admirably professional achievement which was indispensable for the product's success.

The successful operating results we achieve are always the result of people doing something right. The opportunity for Celexa had to be recognized and seized, but it could have been worthless without the planning and execution of multitudes of our employees—scientists, manufacturing, financial, and marketing personnel, as well as our superb salesforce. They have all worked with prodigious effort this last year and we all are deeply indebted to them. It is thrilling to serve such an extraordinary and devoted group of people.

Sincerely,

Howard Solomon
Chairman & Chief Executive Officer

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Howard Solomon, Chairman
and Chief Executive Officer

Ken Goodman, President
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