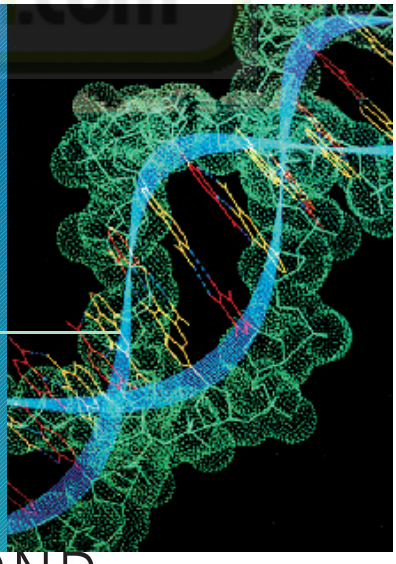
SUN
PHARMACEUTICAL
INDUSTRIES LTD.

ANNUAL REPORT 2005-2006



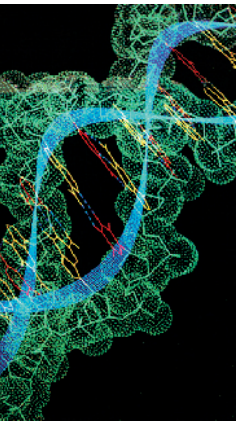
LOOKING BEYOND

LOOKING BEYOND

The covers depicts an artist's impression of a DNA as determined by neutron scattering.

Reaching beyond the apparent, to understand how it all works together, to take this learning to the next stage.

The Human Genome Project, a mammoth exercise in elucidation, has offered a complete DNA blueprint of thousands of genes that code for enzymes, hormones and structural proteins in the human body. The challenge now is to link this structure, to determine form and function; using precise tools such as neutron scattering. A precisely focused neutron beam can help pinpoint the atoms such as C, H, O, N, K and their 3D arrangement in a large molecular structure.



As a term, neutron scattering is a misnomer of sorts. The dictionary defines scattering as: to separate, to go in different directions, to disperse- a dissipation of effort. The encyclopedia hints at focus, concentration. It defines scattering as a physical process where some form of radiation is forced to shift or deviate from a straight path by non-uniformities it encounters in the medium through which it passes. Minuscule changes in energy levels on collision are then used to derive the kind of particle and its arrangement in space.

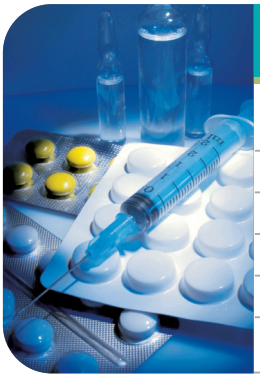
Using these data to piece the puzzle together. Data that can help create better medicines tomorrow. Or suggest totally new ways of treatment.

Insights such as these are the inspiration for the new research company, SPARC. With the same genetic make up and drive for growth. Taking research understanding beyond the obvious, to the next stage.

Summary

- Revenues for the year ending March 31,2006 up 36%.
- Formulations were 84% of the revenues, in line with our objective of being a formulations driven company.
- Domestic formulations, the sales of speciality prescription brands in India, at 55% of revenues, with 41% growth.
- International formulations were 29% of revenues, a growth of 37%.
- The export of speciality API was 11% of revenues, backed by increasing sales of APIs to regulated markets.
- Exports of branded prescription products (non-US markets) grew 54%, across 26 markets.
- US: Sales at Caraco for the year ending March 31,2006, up 29%, with increasing sales of its key product lines, and its first-ever para 4 win, Ultracet.
- Plans at an advanced stage to demerge innovative R&D projects into a separate company. This company will be listed.

(Rs. Mill)



Sales Breakup by type	Mar 06	Mar 05
Domestic Formulations	**9596**	**6799.8**
Domestic Bulk	**815**	**908.2**
Domestic Others	**3**	**8.3**
Export Formulations	**5036**	**3680.7**
Export Bulk	**1888**	**1344.7**
Export Others	**34**	**2.0**

All financial numbers are for the consolidated results unless otherwise mentioned specifically.

- 31 APIs were developed and scaled up. With this, in all, a total of 35 filings await approval, including filings in the areas of anticancers, steroids, hormones and peptides.
- At our Karkhadi site (the erstwhile Phlox Pharma), expansions completed to create a cephalosporins facility that is FDA compliant and can make both sterile and non-sterile API and dosage forms.

- A 170 acre site in Tiszavasvari, Hungary, acquired from Valeant Pharma in end 2005 for vertical integration in controlled substances. This 600KL manufacturing capacity, in one shot, doubles the API capacity at Sun Pharma.
- A site at Cranbury, NJ, USA, acquired to manufacture controlled substance dosage forms, bringing in state of the art manufacturing suites meeting international regulatory standards.
- A site at Bryan, Ohio, USA, acquired to make semi-solids, pastes and liquids, and work begun on capacity increases and streamlining operations.

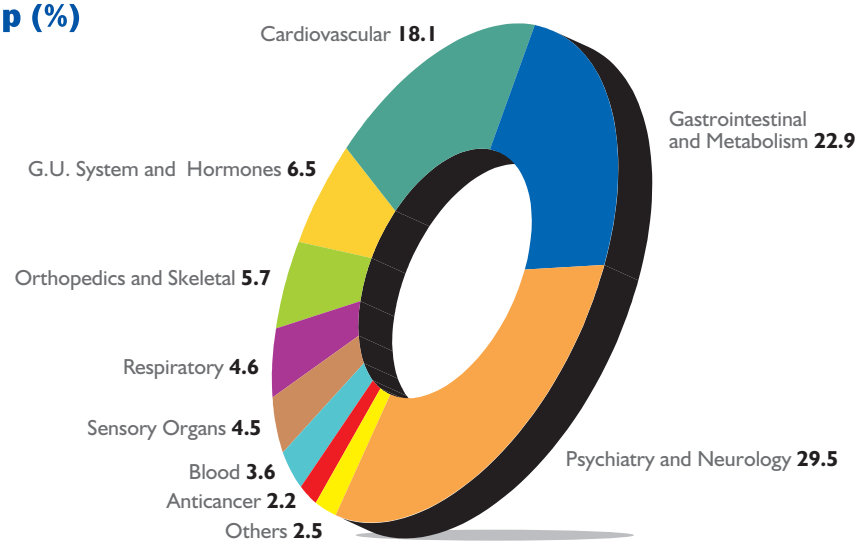
Divisionwise representative strength

Sun	263
Ortus	60
Azura LS	174
Arian	178
Azura CC	18
Avior	161
Symbiosis	95
Synergy	115
Sirius	93
Onco	66
Spectra	231
Inca	107
Solares	249
Radiant	82
Milmet	73
Avesta	72
Inst. Sales	22

Refers to the no. of reps. other than in divisions that directly have FLMs.

C-MARC Ranks	NOV 02 to FEB 03	MAR 04 to JUN 04	MAR 04 to JUN 05	NOV 05 to FEB 06
Psychiatrists	1	1	1	1
Neurologists	1	1	1	1
Cardiologists	3	1	1	1
Ophthalmologists	4	3	1	1
Diabetologists	3	4	2	1
Gastroenterologists	3	2	2	2
Orthopedics	6	4	3	2
Oncologists	6	8	3	4
Chest Physicians	4	4	5	5
Consultant Physicians	5	5	5	5
Gynaecologists	11	7	8	5

Therapy wise break-up (%)

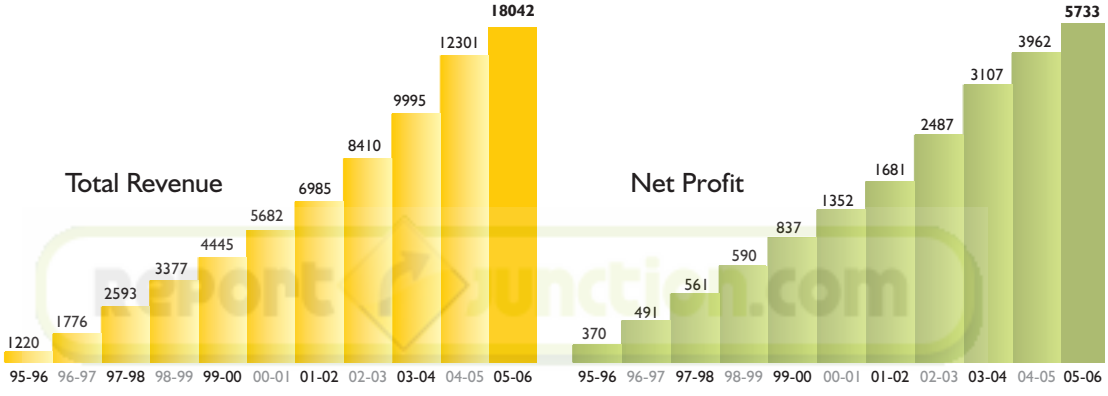


Core therapy areas continue to show double-digit growth

(Mar 2006 MAT data from IMS-ORG Retail Store Audit)

Company Performance

Domestic formulations, the sales of speciality prescription brands in India, were 55% of revenues, with 41% growth. This year, 32 products were brought to market, topping our product baskets across divisions. 11of these products used difficult technologies or had complex drug delivery technology to make them more patient-friendly.



(Rs. in millions) Consolidated results from 2001-02 onwards.

Drug Delivery Systems

- XL/CR including gastric retention systems, multiparticulate systems
- Month/week long biodegradable depots
- Liposomal drug delivery
- Ophthalmic gels
- CR/ SR
- Mouth dissolving
- Dry Powdered Inhalers
- Metered dose inhalers
- Nasal sprays
- Peptide based Injectables
- HFA Inhalers
- Transdermal DDS

CMARC's speciality list

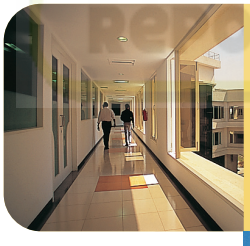
In core therapy areas where we are ranked at number 1- psychiatry, neurology, cardiology, diabetology, ophthalmology, diabetology (a new addition to this list)- we continue to retain top rank with specialists and add market share in fairly competitive markets. In seven of the twelve therapy areas that we are present in, we rank among the top 3 companies. These rankings continue to endorse the advantage of focus on customers in specific therapy areas. Market share increase was also seen in therapy areas of relatively recent presence like gynecology and oncology. This increase in rankings is supported by strong execution on the ground, patient friendly products, and the introduction of products with technical complexity.

Research and Development

Looking Beyond : from product development to innovation

This year too, there was a continuation of early-stage outlicensing deals that involved Indian companies and the transfer of intellectual property. In recognition of the high quality skill base available in India, and flexibility to shift parts of large projects across continents as also reduce costs substantially, a large number of European and US companies set up R&D centers in India. This move, with the other emergent trend of buying existing API units or setting up greenfield API units in India, will offer companies from the regulated markets an opportunity to compete on the same cost base and access the same expertise. This also implies that the competition for talent is increasing as also the pressure on resources required to remain world-class.

Last year, in our report to you, we had highlighted about the addition of about 250,000 sq ft of research floor area across two high capability sites, SPARC or the Sun Pharma Advanced Research Center, in Baroda and in Mumbai. As more labs were commissioned, the number of labs has increased from 137 last year, to 161.



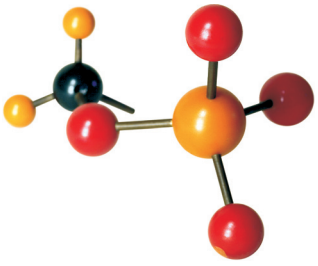
This year, a new state-of-the-art 25,000 sq ft bioequivalence center with a well established clinical pharmacology unit, equipped with 78 beds was set up at the R&D campus in Baroda. This has specially demarcated areas for clinical investigation, emergencies, sample processing, diagnostics, and archives as required as per GLP practices.

SPARC, Baroda

Our focus for the short term is on projects for India and the neighboring markets. This year, SPARC helped to bring to market 32 products in India, of which 11 were based on a delivery system advantage or complex development technology.

In addition, as we slowly ramp up in international markets, new filings were made in international markets to offer a pipeline that supports our current product basket. The number of active registrations stood at 463, with 730 products being marketed.

Some of these international filings are for complex delivery system based products, like the anticancer liposomal doxorubicin Lipodox, and Lupride, the one and three-month depot injectable used in cancer and fertility treatments.



As we roll out these products across select international markets, we stay prepared to take them to the US market over the next few years. We have several similar delivery-system based products in our development pipeline. We expect that registering these complex products across markets will help us differentiate our product offering and help build customer relationships.

Between Sun Pharma and Caraco, 44 products have been filed with the USFDA and are awaiting approval, building a strong pipeline that will drive our US business going ahead. A strong intellectual property cache has been built up, with 56 patents received, another 339 filed and awaiting approval.

Significant advances on filings for the API business were also made during the year, with 24 approvals and 35 filings awaiting approval for US and Europe. Some of these filings support our ANDA plans and will enable us to compete as an integrated company in the injectable /peptide/ steroid/ anticancer areas, in which we have identified several opportunities.

We have good progress to report on our innovation based projects. One new chemical entity or new molecule (NCE) has successfully completed Phase 1 and will enter Phase 2 over the next few months. Two NDDS projects will also enter phase 2 trials shortly. A decent pipeline of research projects is in place, and these projects will be transferred to the demerged research company, that is, Sun Pharma Advanced Research Company Ltd.

This year, on account of innovation-based projects going into trials, higher costs associated with complex ANDAs, and the sustained pace of new product introductions in India, the R&D spend was 11.7% of turnover.

The next step

Formulations development Lab, SPARC

Demerger of R&D

In a revolutionary step in the Indian Pharma industry, and in a step that does not have too many parallels worldwide, we recently announced the demerger of the innovative part of our R&D, pending regulatory and legal clearances. This move would effectively place the NCE and NDDS projects, resources, and the teams working on these, in a separate company. This company would be listed on the stock exchanges in India. The current shareholders of Sun Pharma would receive the same number of shares in the new company, of paid up value of Rs 1 each in the resulting company (as against paid up of Rs 5 each in Sun Pharma). We believe our projects in these areas have reached a stage where with the right attention and resource commitment, they can reach their potential. Innovation based projects have longer timeframes, require extensive funding and the style of working of the scientists too, tends to be more open ended, unlike the time bound approach for generics. The likelihood of these projects reaching market is also very different compared to the certainty associated with product development or process development-based projects. While we hive off these projects into a separate company with resources, funding and people, we expect to increase investments in projects for generic markets including India and the US.

Indian Markets

Looking Beyond : speciality therapy leadership

The Rs. 26,000 cr. market for prescription products in India is growing at 16%. As this market moves from a developing nation market where the larger therapy segments are those of antibiotics, tonics and vitamins to a more mature market , where lifestyle and chronic therapy areas are the larger segments (table 1) , it is likely that speciality areas will continue to grow at above market growth rates.

Table 1: **Top therapeutic areas globally (March 2006 MAT)**

1	Cholest/Trigly Reducers	6	Anti-Epileptics
2	Anti-ulcerants	7	Oral Antidiabetics
3	Antidepressants	8	Angiotensin Antagonists
4	Anti-Psychotics	9	Platelet Agg Inhibitors
5	Calcium Antagonists	10	Narcotic Analgesics

Speciality therapy areas continue to be the largest and fastest growing in the developed markets.

IMS Health

Improving socioeconomic demographics have had a direct impact on the market size, affordability, and awareness of chronic ailments in India as in other developing markets.

A change is likely in the current pricing control policy in the country. As per the draft policy, the parameters for inclusion from mass consumption or monopoly drugs may change to include drugs that are essential in nature such as chronic therapy area drugs. This move will also increase the number of drugs that are under price control from the current 74 to over 350. Such a move could be a major threat to the sector, as more than 50% of the market could then be under price control, though we believe it is unlikely this will be implemented as proposed.

In the Indian market, there has been increasing competitive interest in chronic therapy areas, from large Indian and multinational as well as regional companies. There have been some signs of growth from multinationals as they begin to introduce new products in India. For some multinational companies, the introduction of new products in India was fairly close to international launch, unlike their approach earlier, which in our view indicates a new seriousness from these companies. Increasing competition translates into higher promotional costs across the sector, and impacts margins. Smaller and regional companies that are not adequately covered by the IMS-ORG continued to make their presence felt, and some of these brands made inroads in larger markets too, particularly for acute therapy products. We continue to take the challenge posed by both these segments multinationals and smaller companies, seriously.

India Market data from IMS-ORG Retail Store Audit.

The year 2006 was the second year with the same intellectual property protection in India as in other world markets. In 2005, a new patent act was put in place to make India TRIPS compliant, with safeguards that protect patient interest and prevent evergreening on nonsubstantial grounds. In a country where healthcare costs are borne by the patient, and the public healthcare system is largely ineffective or inadequate, we believe it is in the country's best interests to create a patent system that complies with international requirements but does not exceed its brief. The recent stand taken by the government on data protection and the requirement that a patent apply to a new product- not to a crystalline form or a variation of an already existing product, is a step towards ensuring fair access for people.

With patent norms in India now similar to those globally, there is a concern that new products based on post-1995 research may not be available for introduction in the Indian market going ahead. We believe we have an adequate number of interesting new products lined up introduction for the next few years, based on pre-1995 patents. Since new chemical entity patents filed after 1995 would be the property of the patent holder or licensee, it is possible that going ahead, this pipeline would slowly dry out. However, we expect to use our standing with specialists to license-in products while we work to bring the products of our own research to market.

On the whole, speciality brands continued to witness higher than industry growth, although there were product-specific exceptions. Increasing awareness of treatments and the availability of medication, especially in the areas of mental health and neurology, have helped address some of the fears / stigma associated with treatment. During the course of the year, a number of news items that have received much attention have helped to highlight some of these psychiatric ailments and the dangers of leaving them undiagnosed and untreated.

Pharmacokinetics Labs, SPARC, Baroda

US Generics

Looking Beyond : leveraging the speed of product development

In our expectation, the $27 billion US generic market will continue to remain competitive, with pricing pressure/ cost containment, and increasing market size on account of the new Medicare Bill. The year witnessed tactics by larger pharma companies to limit the entry of generics for important products- tightly contested patent challenges, out of court settlements and the entry of authorized generics. We expect the competition for blockbuster molecules that will go off patent this year, to be quite intense. We believe an ability to compete with the right product mix across dosage forms, with vertical integration for some important products, will strengthen a company's ability to compete in the US generic market. This ability to source APIs in-house will also translate into a cost and time advantage. We believe that the rush of filings and the entry of new competitors, several of which are integrated into API, will translate into intense pricing pressure, as companies try to build market share.

Caraco closed the year ending 31 March 2006 with sales of $82.8 mill, growing at 29%, one of the few in the sector to show strong numbers despite continuing pricing pressure in key products.

Our US presence continues to be one of the fastest growing parts of our business, and one that we strengthened considerably in the past year by acquiring two more facilities in mainland USA.