

2007 Annual Report

Evolution unlocks opportunity

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Watson Pharmaceuticals, Inc., headquartered in Corona, California, is a leading specialty pharmaceutical company that develops, manufactures, markets and distributes brand and generic pharmaceutical products. With one of the broadest product offerings in the United States and a track record of service excellence, Watson has earned a solid reputation as a reliable and low-cost provider of quality pharmaceutical products.

We have accomplished great things in our first two decades. After nearly 24 years at the helm, our founder passed the leadership baton this year, signaling the beginning of a new era in the evolution of our company.

We will continue to evolve our business and adapt our strategy. We will retain those traits that provide us with a competitive advantage: Quality medicines. Superior service. Operational excellence. Building on our strengths, we are determined to create a lasting legacy.

On the horizon:
Watson 2.0

We've built a powerful engine

With \$2.5 billion in revenue, an impressive global supply chain and a tradition of successfully navigating through a constantly changing environment, Watson continues to invest for the future while opportunistically building on its leading position as a top-tier specialty pharmaceutical company with a valuable portfolio of excellent products.

Right on course

Powered by a highly integrated business model, our company has sustained long-term growth and achieved leadership by serving the market with both Generics and Brand product offerings.

Having a diverse portfolio and pipeline helps balance the risks of doing business and has helped our company achieve success in all types of market conditions and industry cycles.

We recently strengthened our business model even further with the addition of a distribution arm that brings us closer to our customers in the pharmacy sector and gives us a unique perspective on how to market and sell our products across all of our businesses.

Entering a new phase of opportunity

Our company was founded by Allen Chao, Ph.D. in 1984, who worked for more than two decades to build a business that could achieve lasting success while delivering life-changing treatments to patients in need.

Remaining active today as chairman of the board of directors, this year Dr. Chao retired from his role as CEO, hiring industry veteran Paul Bisaro to take on the job of leading us forward through “Watson 2.0”—the next phase of growth and transformation for our company.

The foundation for our future is solidly in place. Watson is the fifth largest pharmaceutical company in the United States today (based on prescriptions dispensed). We have a vital and growing Brand business with a solid pipeline. And through our Andabusiness, we are the fourth largest distributor in the United States.

Watson is well positioned for what comes next. And we are intent on pursuing new opportunities to fulfill our mission, achieve our business goals and deliver value to our shareholders.



CORPORATE PROFILE

GENERICS

Our Generics business includes off-patent pharmaceutical products that are therapeutically equivalent to Brand products. This business is driven by products we have internally developed, products we have licensed and products we market for third parties.

BRANDS

Our Brand business includes Watson's lines of Urology, Nephrology and Specialty products. This segment includes patent-protected products and certain trademarked off-patent products that Watson sells and markets as Brand pharmaceutical products.

DISTRIBUTION

Our newest business distributes over 8,000 Generics and select Brand pharmaceutical products manufactured by both Watson and other manufacturers to independent pharmacies, pharmacy chains, hospitals, clinics, physicians' offices and other alternate care facilities in the United States.

We have a deep and diverse product portfolio

Watson brings competitive advantages to market that have helped us achieve leadership as the fifth largest pharmaceutical company in the United States today, based on total prescriptions dispensed. Opportunistic, relevant and profitable, we are resolved to conduct our business in a manner that creates lasting value and makes a positive impact on people everywhere.

Focusing on areas where there is an opportunity to make a difference

Watson has built a long-standing reputation with our trade customers as a trusted resource for competitively priced, high-quality products backed by one of the highest levels of customer service in our industry.

While currently representing only 17 percent of our total revenue, our highly focused Brand business brings diversification to the business mix. We continue to see this part of our business as a critically important link in the Watson value chain.

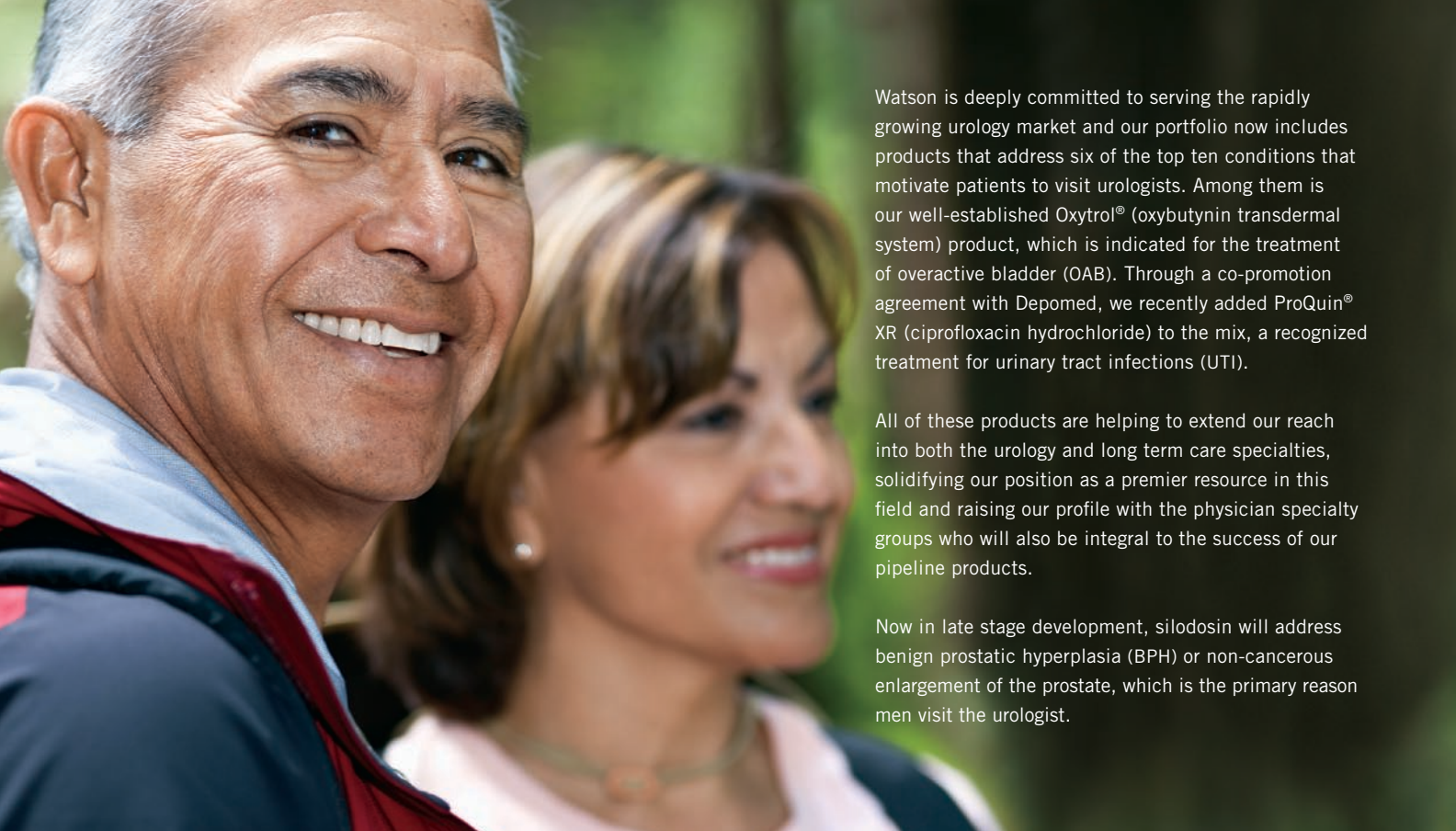
The presence of differentiated, high-margin products in the Brand portfolio provides us with attractive revenue opportunities, while helping to offset potential market fluctuations in our Generics business.

The continually growing Watson Brand portfolio now features more than 25 pharmaceutical product families that are delivering value to physicians and patients and represents a growing contributor to our overall profitability.

We are delivering meaningful choices and exceptional value

Watson's formidable portfolio of Generics products continues to represent the bulk of our business, accounting for 60 percent of total annual revenue. Widely recognized for our leadership position in oral contraceptives and pain management products, our Generics portfolio features more than 150 product families, supplying physicians and pharmacists with multiple treatment options and providing relief to patients in a wide variety of indications.

This unique portfolio, which features many difficult-to-replicate formulations, is a point of differentiation for Watson, distinguishing our company as one of the premier sources for Generics offerings in the United States today.



Watson is deeply committed to serving the rapidly growing urology market and our portfolio now includes products that address six of the top ten conditions that motivate patients to visit urologists. Among them is our well-established Oxytrol® (oxybutynin transdermal system) product, which is indicated for the treatment of overactive bladder (OAB). Through a co-promotion agreement with Depomed, we recently added ProQuin® XR (ciprofloxacin hydrochloride) to the mix, a recognized treatment for urinary tract infections (UTI).

All of these products are helping to extend our reach into both the urology and long term care specialties, solidifying our position as a premier resource in this field and raising our profile with the physician specialty groups who will also be integral to the success of our pipeline products.

Now in late stage development, silodosin will address benign prostatic hyperplasia (BPH) or non-cancerous enlargement of the prostate, which is the primary reason men visit the urologist.

SPOTLIGHT ON UROLOGY

Watson has a long legacy of service in the women's health arena, and we are well known for our oral contraceptive offerings.

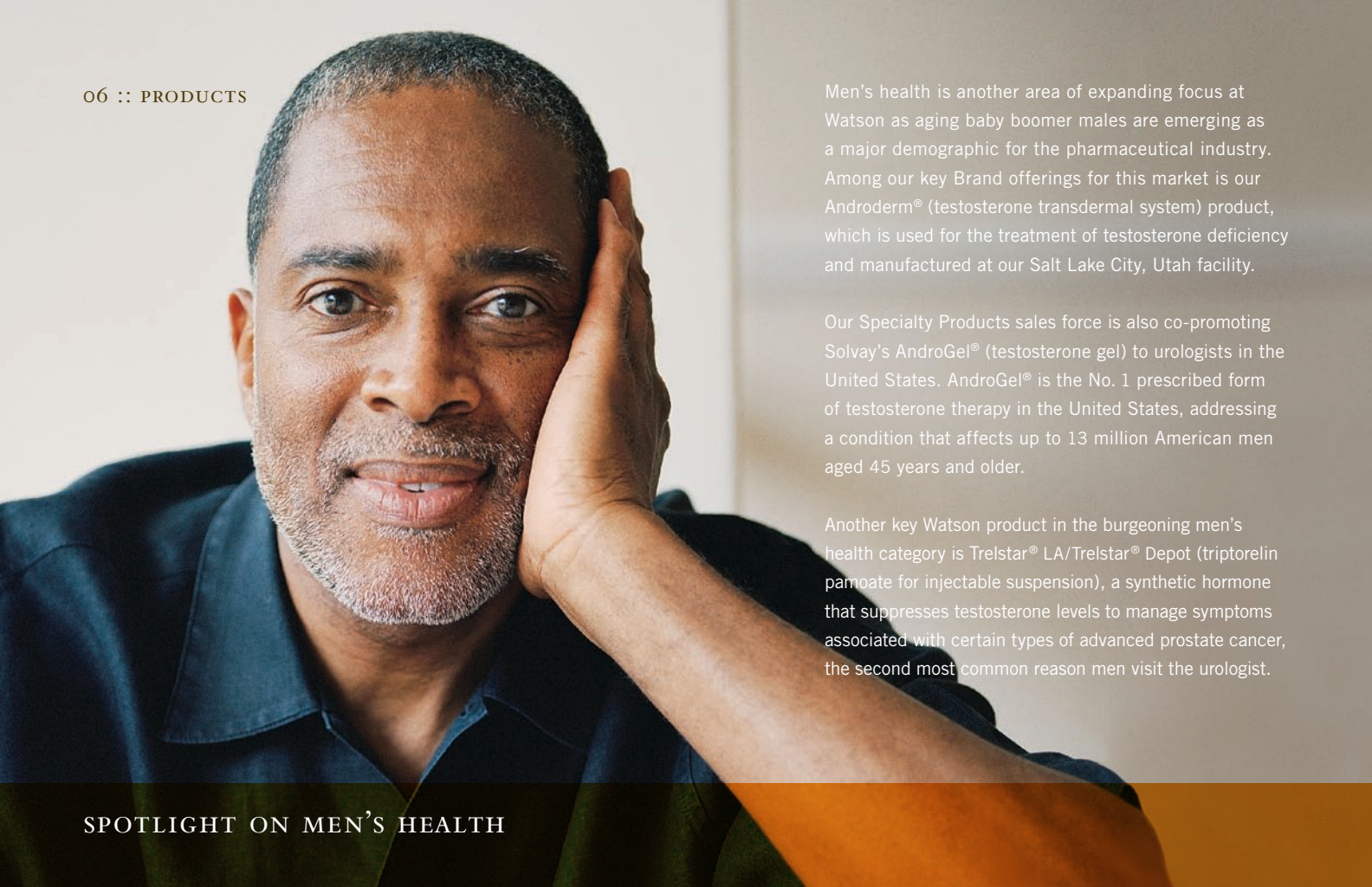
Continually aligning our business with demographic trends, we have become focused in recent years on issues affecting women who have made the passage beyond the childbearing years and are confronting a new set of medical issues.

As part of that effort, we continue to strengthen our ties to the gynecological community, which represents an important and ongoing medical resource for women in every phase of their lives.

Among the initiatives generating excitement this year is our Brand Division's recent agreement to co-promote Tri-Luma® (fluocinonide acetate, hydroquinone, tretinoin), a major treatment for melasma, a skin condition associated with hormonal changes in women. And in our urology pipeline, we are making promising progress with Uracyst® (sodium chondroitin sulfate), our investigational product for the treatment of interstitial cystitis, a painful bladder condition affecting as many as 900,000 women in the United States today.

SPOTLIGHT ON WOMEN'S HEALTH





Men's health is another area of expanding focus at Watson as aging baby boomer males are emerging as a major demographic for the pharmaceutical industry. Among our key Brand offerings for this market is our Androderm® (testosterone transdermal system) product, which is used for the treatment of testosterone deficiency and manufactured at our Salt Lake City, Utah facility.

Our Specialty Products sales force is also co-promoting Solvay's AndroGel® (testosterone gel) to urologists in the United States. AndroGel® is the No. 1 prescribed form of testosterone therapy in the United States, addressing a condition that affects up to 13 million American men aged 45 years and older.

Another key Watson product in the burgeoning men's health category is Trelstar® LA/Trelstar® Depot (triptorelin pamoate for injectable suspension), a synthetic hormone that suppresses testosterone levels to manage symptoms associated with certain types of advanced prostate cancer, the second most common reason men visit the urologist.

SPOTLIGHT ON MEN'S HEALTH



SPOTLIGHT ON NEPHROLOGY

In collaboration with the nephrology community, Watson seeks to improve and extend the lives of patients with kidney disease through development of appropriate pharmaceutical therapies, clinical research, education, and community advocacy. This purpose drives all of our actions, and the results are reflected in the nephrology business continuing to be a significant contributor to the profitability of the company over 15 years after entering the market.

The National Kidney Foundation estimates that over 20 million Americans suffer from various stages of Chronic Kidney Disease (CKD), and over 350,000 of these patients are dependent upon dialysis treatments as a lifesaving therapy. Watson plays an important role in the treatment of iron deficient CKD patients with its IV iron therapies, Ferrlecit® (sodium ferric gluconate complex in sucrose injection) and INFeD® (iron dextran injection). IV iron is an important therapy in treating the debilitating anemia that many CKD patients experience, and recent data suggest that the importance of products like Ferrlecit® and INFeD® is likely to grow in the future, in the nephrology community and other disease states.

Among the factors contributing to our success in the marketplace is the strong technology base we've accumulated through the years and our outstanding global supply chain operations.

Advanced drug delivery technologies

Watson has gained recognition for our ability to take good drugs and make them better, particularly through the application of innovative drug delivery technologies including oral dosage, transdermal and transmucosal products. We have dedicated a number of teams and facilities to the task of ensuring our continued technology leadership in this critical area.

Global centers of excellence

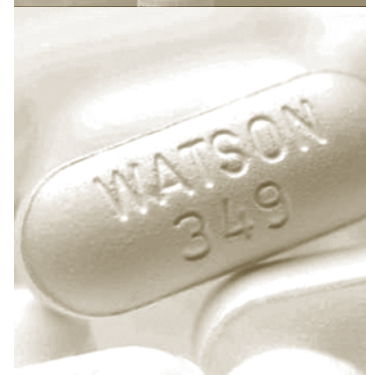
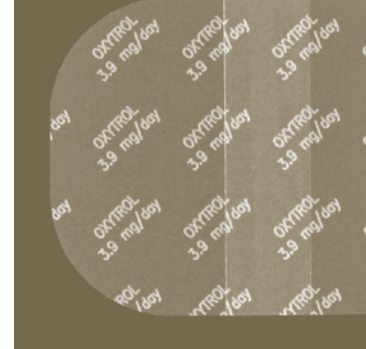
Our global infrastructure includes state-of-the-art research & development (R&D) centers and manufacturing facilities in the United States, Northern Ireland, India and China. In addition to serving as the site of our corporate headquarters, Corona, California is home to Watson's largest R&D center. Among other products, we develop and manufacture controlled substances and hormonal products at this location.

Our R&D and manufacturing facility in Salt Lake City, Utah helps Watson maintain its leadership in transdermal drug delivery systems. In the northeastern region of the United States, our company also operates a solid dose manufacturing facility in Carmel, New York and a transmucosal (gum) manufacturing plant in Copiague, New York.

Our large-scale solid dosage manufacturing and R&D facilities in Davie, Florida are primarily focused on specialty oral controlled-release products. The complex processes associated with bringing these products to market represent a high entrance barrier for our competitors.

As part of our international operations, we recently completed Phase I construction of a high-volume solid dose manufacturing facility in Goa, India. We are currently moving certain immediate-release products to this location to take advantage of the significantly lower cost of goods. In addition, we recently opened a bioanalytical facility in Mumbai, providing us with added flexibility for our Generics clinical study programs.

Adding vertical integration to the mix, we are also now operating active pharmaceutical ingredient (API) manufacturing plants in India, China and Northern Ireland.



At the heart of our business is a fervent commitment to service

Driven to make a contribution to people in need, we strive to build lasting relationships and conduct our business with integrity. Today we are working at every level to maintain our tradition of strong customer service and sales support, while seeking ways to create new value for our customers and our company.

Delivering strong customer service and sales force coverage

Watson's sales and marketing teams play a critical role in building customer loyalty while gaining valuable market insight that shapes our strategy and helps us grow and enhance the Watson brand.

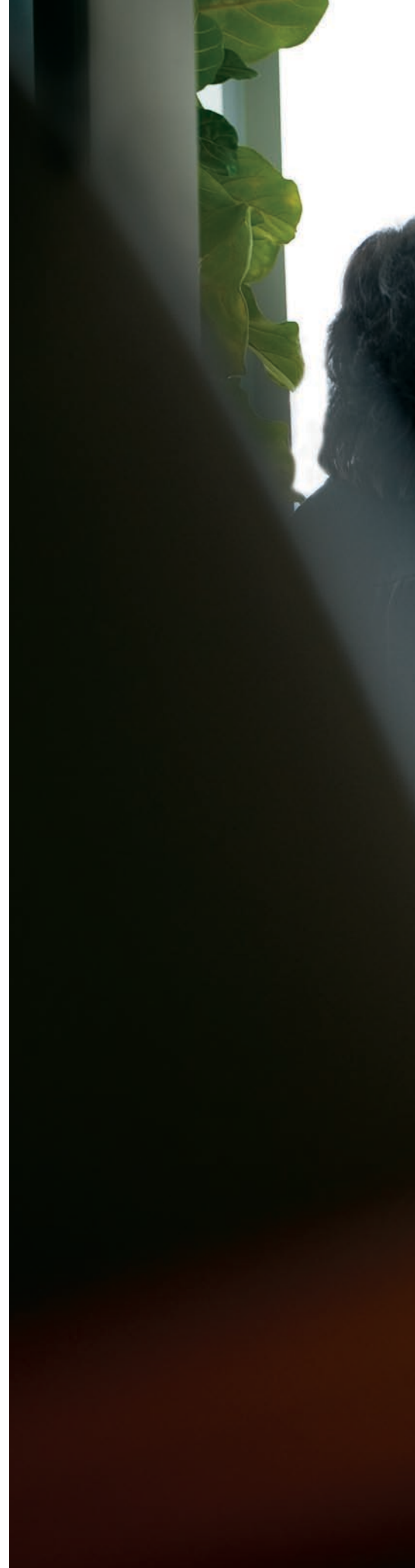
To achieve those goals, we currently employ approximately 350 sales representatives in our Brand business and another 25 people in our Generics business. These energetic and talented individuals call on caregivers and medical institutions with focus in specialty areas such as urology, nephrology, gynecology and primary care. In addition, we call on key customers in the long term care, institutional and government sectors and buyers from chain drug stores, wholesalers and pharmacy benefit managers.

The Watson difference

Watson has been integral to the United States nephrology community for more than 15 years. Our company introduced INFeD® when no other intravenous (IV) iron was available, following up with the first 2nd- generation formulation and the only IV iron product approved for pediatric chronic hemodialysis patients. This year

we sponsored the first study focused on inflammation in dialysis patients. And through our longstanding commitment to Kidney Care Partners, we are working together with patient advocates, healthcare professionals and other industry leaders to improve quality of care for individuals with chronic kidney disease.

As part of our comprehensive approach to meeting the needs of our customers, we also support and engage in activities centered on research, education and advocacy, and are breaking new ground with innovative services. We are a major participant in advocacy groups like the Kidney Care Partners, and we were one of the first in our field to aggregate outcomes data for sharing amongst our customers. It is our hope that through these combined efforts, we are ultimately helping patients live longer and better lives.





In addition to providing resources to help improve clinical outcomes, we provide assistance on practice management issues where appropriate. From providing information hotlines on critical reimbursement issues to counseling office managers on purchasing procedures, we are working to make our customers more efficient and profitable.

Watson is quickly becoming a major force in the field of urology, and our sales and marketing teams in our Brand business are dedicated to realizing that vision.

As is the case in our other customer support programs, our strategy in this sector is to develop meaningful and long-term relationships, taking a partnership approach to serving our customers with an increasingly broad portfolio of treatment options. Through our clinical programs, our highly segmented business development efforts and our expert detail forces, we are making it known that Watson has a deep commitment to the urology community and we plan to be an industry leader for many years to come.

To increase our market breadth, we continue to reach out to others in the industry, forming licensing and co-promotion agreements where there are opportunities to benefit both parties. This strategy paid off in increased revenues from the promotion of several key products this year, notably with AndroGel® and ProQuin® XR in our urology business.

Our Anda Distribution business provides us with unique customer touchpoints

Through a winning combination of outstanding sales representatives and proprietary online ordering technology, our far-reaching Anda/VIP distribution business makes Watson unique among pharmaceutical companies in the United States—accounting for more than 20 percent of total revenue in 2007 and providing us with a direct link to our customers in pharmacies and medical buying centers nationwide.

With over 8,000 products and over 50,000 ship-to locations, Watson is now the fourth largest distributor of pharmaceuticals and has established a presence in nearly every pharmacy in the United States.



Our global R&D organization is dedicated, focused and agile

Leveraging our expertise in drug delivery technology and product development, Watson's steadily expanding internal R&D program fuels future growth by taking promising product candidates through clinical studies. With a robust Brand product pipeline and more than 60 Generics pending approval with the U.S. Food and Drug Administration (FDA), the road ahead looks promising.

A year of milestones

Our global R&D organization had a tremendous year in 2007. In the United States, we received important new product approvals, filed many new Abbreviated New Drug Applications (ANDAs) and achieved successful results in key clinical trials that will pave the way for us to commercialize urology products that are important to the future of our company.

A time of transformation

We are on a path to create a urology portfolio with the potential to transform our Brand business for many years to come. Thanks to the excellent efforts of our R&D teams, we are now in position to file three New Drug Applications (NDAs) with the FDA in 2008, which will provide us with an attractive suite of treatment options addressing the top three reasons for office visits to urologists.

The most common urology condition

This year our R&D organization reported positive results from our Phase 3 studies of silodosin, the first new chemical entity we are studying as a treatment of the prostate disorder known as benign prostatic hyperplasia, or BPH. In early 2008, our NDA for silodosin capsules was accepted for filing by the FDA.

The market for this product is very large. BPH affects about one in every four males in the United States. Prescriptions for this condition are growing at a rate of approximately 17 percent per annum and the size of the market has passed the \$2 billion mark.

The No. 2 condition

In early 2008, we were pleased to report positive results from our Phase 3 study of oxybutynin topical gel as a treatment for patients with overactive bladder (OAB). This puts us on track to file yet another NDA in 2008, and paves the way for a potential commercial launch in 2009.

More common than both diabetes and asthma, OAB affects more than 33 million Americans. The OAB prescription market in the United States is valued at approximately \$1.7 billion.

The No. 3 condition

Further enhancing our position in the field of urology, our partner Debiopharm is developing a long-acting formulation of Trelstar® for advanced prostate cancer. We currently sell this product in a one-month and a three-month formulation. Debiopharm recently completed the Phase 3 program for a six-month formulation and reported successful results. Pending a final analysis of the data, they plan to file an NDA for this formulation in 2008.

Building a strategic portfolio: Brand pipeline

Product	Indication/Therapeutic Target	Market	Phase 1	Phase 2	Phase 3	Filed	Approved
Silodosin	Benign prostatic hyperplasia (BPH)	U.S.	<div></div>	<div></div>	<div></div>	<div></div>	
Oxybutynin topical gel	Overactive bladder (OAB)	U.S.	<div></div>	<div></div>	<div></div>	<div></div>	
Trelstar® 6-month	Advanced prostate cancer	U.S.	<div></div>	<div></div>	<div></div>	<div></div>	
Uracyst®	Interstitial cystitis/painful bladder syndrome	U.S.	<div></div>	<div></div>	<div></div>	<div></div>	

This is a time for making bold moves

The execution of Watson's long-term strategic plan and operational activities are solidly underway. We continue to evolve our business and adapt our strategy. Guided by the principles we were founded upon, we will achieve industry leadership by continuing to build a highly competitive global organization, bringing a broad portfolio of excellent medicines to market and seeking bold new ways to create value for our shareholders.

We have a flexible and evolving plan

Watson has been carefully working to solidify our strong base business, building out our global infrastructure, making operational improvements throughout our organization to create a lean and competitive cost structure. To keep pace with shifting industry dynamics, we are building an offshore presence for our company, expanding our capacity, increasing our flexibility and enabling faster time to market.

In a major milestone for our international strategy, the FDA granted the first product approval at our Goa, India facility in 2007, opening the door for us to step up the pace of our offshore manufacturing program.

Our portfolio is relevant for our customers and the patients they serve

As a specialty pharmaceutical company, we take a focused approach to building our portfolio, concentrating on treatment areas where we have sufficient breadth and depth to achieve impact. Whether it's a brand or generic product, our goal is to provide a broad variety of treatment options in specific categories.

Our push into the urology sector is a case in point. In the specialty areas we focus on, we work hard to understand our customers and meet their needs with a sustained commitment and a partnership approach to doing business.

We are working on many fronts to evolve and grow our depth of offerings

As we execute on our strategic plan for the next phase in the evolution of our business, we plan to balance our Generics portfolio with a mix of cost competitive commodity products, while aggressively developing differentiated products that will give us higher returns.

We have great assets and a talented team

Our company has clearly achieved critical mass in our Generics business. We are building a promising Brand business and we have an impressive Distribution business. In terms of our technological capabilities, we have deep experience with drug delivery systems and have become experts at bringing difficult-to-manufacture products to market. In terms of our people, we employ an energetic and talented workforce with a shared vision for the

future. And we have a highly experienced leadership team, bringing a wide variety of industry expertise and insight to the task of charting our journey forward.

Superior execution will take us to the next level

We have the assets and experience needed to transition Watson to the next level of success. We will continue to be opportunistic, pursuing new partnerships and exploring new geographic markets so we can grow our global footprint. We are passionately committed to maximizing value in all of our operations. And we believe that the skill we've gained in managing both our Generics and Brand businesses makes Watson a nimble competitor and positions us for long-term success on the road ahead.





During 2007 we continued to make progress on our strategic initiatives aimed at reducing our cost structure, enhancing operating efficiencies and expanding our pipeline.

To our stockholders::

As the new President and CEO of Watson, it is both an honor and a pleasure for me to report on the continuing progress and solid results of our company during 2007. When I took on this job in September, my first priority was to travel around the company's various locations to meet with our teams and see first hand who we are as a company and how we are working to execute our business strategy. The experience confirmed for me that Watson is an impressive organization with great people, tremendous assets and unique opportunities.

Over the course of the past 24 years, Dr. Chao and my new colleagues have created a company to be proud of, and I am excited to play a part in helping to build on the vision as we work to lead Watson through the next phase in our continuing evolution.

Our company has a solid base business

With \$2.5 billion in revenue during 2007, Watson today is a leading specialty pharmaceutical company with a broad portfolio of both Generics and Brand products, a highly integrated global supply chain, and a strong research and development program.

We create value through three businesses that are aligned to provide us with distinctive competitive advantages. In addition to providing the healthy cash flow needed to fund future growth, our diversified business model is designed to protect us from market volatility and increase our ability to leverage our assets and create economies of scale across all of our operations.

Through a combination of internal product development and synergistic acquisitions of products and businesses, Watson has grown into a fully integrated pharmaceutical company. The largest of our three operating divisions is a very sound Generics business with a strong portfolio of products, an outstanding pipeline for the future and an industry-leading tradition of excellent customer service.

We also have a growing Brand business, with a strong nephrology presence and a powerful urology franchise that positions us for significant revenue growth. Finally, we have a solid Distribution business that provides us with new opportunities to create value and differentiate Watson from our competitors in the United States pharmaceutical sector.

We are meeting the challenges

This is truly an exciting time for our company and 2007 was a year of achieving milestones while continuing to execute and evolve our strategy for the future. Our Generics business received multiple new product approvals from the FDA and launched 16 new products, a number which enables our company to address large market opportunities.

We also had a productive year in our Brand Division, building on our growing urology franchise and continuing to strengthen our reach into the obstetrics/gynecology community. On the distribution front, our Anda business continues to provide us with a valuable connection to the pharmacists, clinicians, and physicians who comprise our customer universe. This business now services over 50,000 customer locations and gives us a unique presence in almost every pharmacy in America.

Executing on our strategic plan

During 2007, we continued to make progress in our strategic initiatives aimed at reducing our cost structure, enhancing operating efficiencies, and expanding our pipeline.

The sale of our Phoenix facility and the closure of our Puerto Rico site completed the site rationalization work we had planned for this year, helping us to achieve approximately \$30 million in cost savings. Additional improvements in cost of goods are also being realized from enhanced operating efficiencies in both our Corona, California and Carmel, New York facilities. We have set new targets for 2008 and will continue our long-term strategy of maintaining a lean and competitive cost structure both in the United States and abroad.

Growing our offshore presence is critical to the continued success of our company in today's highly competitive environment, and we continue to enhance and expand our operations in India. There was positive progress on this front this year when our Goa, India manufacturing facility received approval to export products to the United States market. We think it is a remarkable achievement to acquire a facility and have it approved for United States manufacture within just 18 months. By early 2008, Goa will be able to produce over a billion units (10 percent of our total production volume) annually for the United States market.

During 2008, we will be expanding Goa's capacity to be capable of handling about a third of our production volume and will look to identify other particularly price-sensitive products that would be appropriate for offshore transfer. As part of this strategic initiative, we will also look to increase our API capabilities, allowing us to work earlier on raw materials that will support future patent challenges, and provide opportunities for backward integration and lower cost of production. Additionally, our recently purchased bioanalytical facility in Mumbai is now in operation and will provide us with the flexibility to manage our own bio-studies at a significantly reduced cost.

This is truly an exciting time for our company, and 2007 was a year of achieving milestones while continuing to execute and evolve our strategy for the future.

In the United States, we continue to maintain and enhance infrastructure and programs that enable us to develop and manufacture high-value products, many of which employ unique delivery technologies. Our heritage in bringing difficult-to-manufacture products to market provides us with yet another significant competitive advantage and we will continue to leverage our expertise in this area as a cornerstone for our strategy moving forward.

Our recently acquired facility in Davie, Florida will play a key role in this strategy. In addition to serving as home base for a major Generics R&D organization, this facility provides us with the potential to significantly enhance our manufacturing capabilities in the United States. We are actively working to resolve pending FDA issues there and look forward to launching important new products from this state-of-the-art facility.

Making progress in our R&D program

Our Generics product pipeline continues to expand significantly, and we are working to balance this important portfolio with both commodity and differentiated drugs. Our internal development program, supplemented by products gained through the acquisition of Andrx, provides us with more than 60 ANDAs on file with the FDA. A number of these opportunities are expected to yield higher margins and longer lifecycles than traditional commodity products. This is consistent with our plan to expand our differentiated product offerings.

We believe that our Brand Division represents a truly valuable asset, and we're working to increase our depth of offerings in this increasingly important part of our business. Accordingly, we remain solidly on track toward building a focused and strategic urology product portfolio that will serve as a cornerstone for our long-term growth.

Our heritage in bringing difficult-to-manufacture products to market provides us with yet another significant competitive advantage and we will continue to leverage our expertise in this area as a cornerstone for our strategy moving forward.

We are quite excited about the opportunities ahead for silodosin, the investigational drug we have been studying as a treatment for BPH, a condition that affects a significant number of aging males and represents the most common reason for men to visit a urology office. We announced promising results from our Phase 3 trials for this drug in 2007, and our NDA was accepted for filing by the FDA in early 2008.

We are also addressing the No. 2 and the No. 3 most common reasons for visiting urologists with our topical gel formulation of oxybutynin for overactive bladder and a six-month formulation of Trelstar® for advanced prostate cancer.

Delivering solid performance and results

To ensure that we have the financial resources needed to execute on our vision for the future, I am pleased to report that we continue to improve operating margins, produce consistent cash flow, reduce our debt and make prudent decisions about managing our capital and increasing value to shareholders.

Our consolidated revenues during 2007 were \$2.5 billion, up 26% from the \$2.0 billion we reported in 2006. Our GAAP earnings per share were \$1.27, and our adjusted earnings per share were \$1.37. Cash flow from operations was \$427 million for the year. Consistent operating and free cash flow allowed us to pay down over \$325 million of debt obligations during 2007. Adjusted EBITDA for the year was \$545 million.

At the division level, net revenue for the Generics segment was \$1.50 billion in 2007, down slightly from \$1.52 billion in 2006. However, the gross margin for this segment increased from 30.2 percent in 2006 to 38.9 percent this year.

Net revenue in the Brand segment increased 16 percent (or \$59.2 million) to \$428.7 million compared to \$369.5 million for 2006, due primarily to our promotion of AndroGel® and to increased sales of our Trelstar® and Androderm® products. Gross margin for this business for 2007 was 76.7 percent up from 75.0 percent in 2006.

In our Distribution segment, this was our first full year of recognizing revenue from the former Andrx business. Net revenue for this segment was \$566.0 million in 2007. Gross margin for this business for the full year was 14.0 percent.

This was a great year in terms of realizing savings on our cost of goods, and Watson's balance sheet is healthy and growing. We have the financial strength and the cash flow to do the things we need to be successful. We can invest in building our business and our R&D programs, and we can be selective and opportunistic in acquiring new products and technology.

We are excited about Watson 2.0

Watson has reached a critical inflection point in its history, and for me personally, this is a wonderful time to have joined the team. Looking ahead, there are many exciting opportunities to grow our company and increase our ability to fulfill our mission of improving the health and quality of people's lives.

To achieve these goals, we are diligently refining our strategic plan and executing, executing, executing. Over the near term, we will balance our Generics portfolio, increase our depth of offerings in differentiated products and maximize profitability across the board. We are determined to unlock the tremendous potential that exists in our emerging Brand business and in our newly acquired Distribution business.

Longer term, we will continue to be opportunistic, finding bold new ways to fuel our growth and increase our profitability. We are determined to grow our Brand Division and believe that the high margins inherent in this part of our business will enable this segment to come into parity with our Generics business in terms of contribution to earnings.

Looking ahead, there are many exciting opportunities to grow our company and increase our ability to fulfill our mission of improving the health and quality of people's lives.

Also in the long-term, we will continue enhancing efficiencies throughout our supply chain. We will form new strategic relationships and look for new acquisition opportunities. We will seek new first-to-file opportunities. And, while proceeding with caution, clearly we are looking to expand our global footprint into new markets in high-growth areas. In all that we do, we seek to be relevant to our customers, providing the high levels of customer service they've come to expect from Watson.

In closing, I would like to thank Dr. Allen Chao, our chairman and founder, for providing me the opportunity to take the reins during this pivotal time. We look forward to his continued support and guidance for many years to come.

Under Dr. Chao's leadership, Watson has been privileged to attract outstanding people at every level of our organization. Continuing to build our executive team this year, I am pleased to welcome Mark Durand as Watson's new CFO and Francois Menard as Senior Vice President in our Generics R&D business. As we come together to align our business and continue to execute on our strategic plan, I would also like to thank all of the wonderful employees at Watson for their excellent teamwork and faith in our future.

Similarly, it is my honor to speak on behalf of the whole team, when I thank our shareholders for continuing to support our aspirations for Watson's future.



Paul M. Bisaro
President and Chief Executive Officer

Guided by a steadfast vision, Watson is on the move.

“I am very proud of what Watson has accomplished since the founding of the company 24 years ago. Over our many years of growth, I’ve worked with an outstanding leadership team and many wonderful people to develop and implement strategic initiatives aimed at expanding our product portfolios in both our Generics and Brand businesses, improving our infrastructure and building a sustainable business. Together, we have achieved something remarkable. Clearly, the cornerstone of our success is the caliber of our people. In retiring from my position as CEO this year, I know that Paul Bisaro is taking the helm of a company that has a solid foundation and tremendous pipeline potential from which to grow. I am excited about the future of Watson and grateful to all who have shared our vision, mission and core values along the way.”

— Allen Chao, Ph.D., Chairman of the Board

“Watson is an industry leader in specialty pharmaceuticals and I am honored to be joining the team at this exciting time in the Company’s development. I am excited about building on the assets in place here at Watson, continuing the tradition of success, and capitalizing on future opportunities to increase value for Watson’s shareholders and employees.”

— Paul M. Bisaro, President and Chief Executive Officer

Solid results in 2007

Years Ended December 31,	2007	2006	2005	2004	2003
(In thousands, except per share amounts)					

Operating Highlights

Net revenues	\$2,496,651	\$1,979,244	\$1,646,203	\$1,640,551	\$1,457,722
Gross profit	991,895	745,761	793,789	819,757	833,071
Operating income (loss)	255,660	(422,096)	218,512	265,940	338,913
Net income (loss) ¹	141,030	(445,005)	138,557	150,018	201,728
Diluted earnings (loss) per share	1.27	(4.37)	1.22	1.26	1.74
Diluted weighted average shares outstanding	117,039	101,761	120,021	124,727	120,727

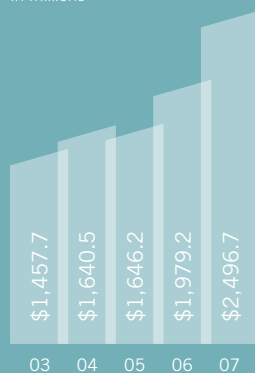
At December 31,	2007	2006	2005	2004	2003
(In thousands, except per share amounts)					

Financial Position

Cash flow from operations	\$ 427,178	\$ 471,365	\$ 325,503	\$ 308,269	\$ 262,517
Working capital	728,849	571,747	1,107,873	1,105,507	971,019
Total assets	3,472,027	3,760,577	3,077,187	3,231,956	3,268,134
Total debt	905,649	1,231,204	587,935	587,653	722,535
Total stockholders' equity	1,849,465	1,680,388	2,100,469	2,230,690	2,042,146

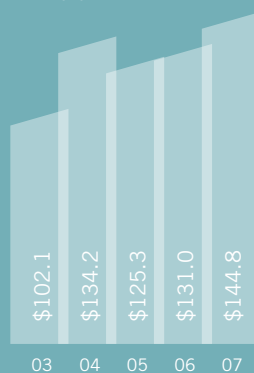
Total Annual Revenue

In millions



R&D Investment²

In millions



Cash Flow from Operations

In millions



¹ Net loss for 2006 includes \$556.0 million in Andrx acquisition-related and other charges, net of tax. See reconciliation table on page 24 for details on the charges.

² 2006 R&D investment excludes \$497.8 million of in-process research and development charges associated with the Andrx acquisition.

Consolidated Statements of Operations

(In thousands, except per share amounts)

Years Ended December 31,

	2007	2006	2005
Net revenues	\$2,496,651	\$1,979,244	\$1,646,203
Cost of sales (excludes amortization, presented below)	1,504,756	1,233,483	852,414
Gross profit	991,895	745,761	793,789
Operating expenses:			
Research and development	144,793	131,023	125,263
Selling and marketing	215,434	173,549	162,342
General and administrative	205,717	131,511	98,657
Amortization	176,409	163,710	163,939
In-process research and development	—	497,800	—
Net (gain) loss on asset sales and impairments	(6,118)	70,264	25,076
Total operating expenses	736,235	1,167,857	575,277
Operating income (loss)	255,660	(422,096)	218,512
Other income (expense):			
Loss on early extinguishment of debt	(5,553)	(525)	—
Interest income	8,886	28,418	19,321
Interest expense	(44,473)	(22,082)	(14,524)
Other income (expense)	9,764	5,336	(3,375)
Total other (expense) income, net	(31,376)	11,147	1,422
Income (loss) before income taxes	224,284	(410,949)	219,934
Provision for income taxes	83,254	34,056	81,377
Net income (loss)	\$ 141,030	\$ (445,005)	\$ 138,557
Earnings (loss) per share:			
Basic	\$ 1.38	\$ (4.37)	\$ 1.32
Diluted	\$ 1.27	\$ (4.37)	\$ 1.22
Weighted average shares outstanding:			
Basic	102,273	101,761	104,949
Diluted	117,039	101,761	120,021

Consolidated Balance Sheets

(In thousands, except per value)

	December 31,	
	2007	2006
Assets		
Current assets:		
Cash and cash equivalents	\$ 204,554	\$ 154,171
Marketable securities	11,799	6,649
Accounts receivable, net of allowances for doubtful accounts of \$3,794 and \$5,914	267,117	384,692
Inventories, net	490,601	517,236
Prepaid expenses and other current assets	86,072	86,115
Deferred tax assets	113,633	112,813
Total current assets	1,173,776	1,261,676
Property and equipment, net	688,185	697,415
Investments and other assets	68,034	76,377
Deferred tax assets	61,886	55,348
Product rights and other intangibles, net	603,697	779,284
Goodwill	876,449	890,477
Total assets	\$3,472,027	\$3,760,577
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable and accrued expenses	\$ 398,154	\$ 516,875
Income taxes payable	—	46,773
Short-term debt and current portion of long-term debt	6,241	107,059
Current deferred tax liabilities	18,778	—
Deferred revenue	21,754	19,222
Total current liabilities	444,927	689,929
Long-term debt	899,408	1,124,145
Deferred revenue	39,535	58,086
Other long-term liabilities	7,333	4,169
Other taxes payable	52,619	—
Deferred tax liabilities	178,740	203,860
Total liabilities	1,622,562	2,080,189
Commitments and contingencies		
Stockholders' equity:		
Preferred stock; no par value per share; 2,500 shares authorized; none issued	—	—
Common stock; \$0.0033 par value per share; 500,000 shares authorized 113,115 and 111,867 shares issued and 103,658 and 102,467 shares outstanding, respectively	373	369
Additional paid-in capital	968,739	937,308
Retained earnings	1,179,737	1,041,638
Accumulated other comprehensive income	2,392	1,073
Treasury stock, at cost; 9,457 and 9,400 shares held, respectively	(301,776)	(300,000)
Total stockholders' equity	1,849,465	1,680,388
Total liabilities and stockholders' equity	\$3,472,027	\$3,760,577

Condensed Consolidated Statements of Cash Flows

(Unaudited; in thousands)

Years Ended December 31,

	2007	2006	2005
Cash Flows from Operating Activities			
Net income (loss)	\$141,030	\$(445,005)	\$138,557
Reconciliation to net cash provided by operating activities:			
Depreciation and amortization	253,559	218,346	206,726
Non-cash impairment charges	4,499	70,264	25,076
Deferred income tax benefit	(6,250)	(24,688)	(5,168)
Provision for inventory reserve	46,853	29,777	42,192
Restricted stock and stock option compensation	14,244	13,336	2,289
In-process research and development	—	497,800	—
Other adjustments to reconcile net income to net cash provided	(9,010)	(4,762)	6,057
Changes in assets and liabilities:			
Accounts receivable, net	120,575	66,172	(82,373)
Inventories	(25,093)	(53,682)	1,045
Accounts payable and accrued expenses	(117,751)	116,709	18,459
Income taxes payable	7,703	(9,094)	(29,062)
Other assets and liabilities	(3,181)	(3,808)	1,705
Total adjustments	286,148	916,370	186,946
Net cash provided by operating activities	427,178	471,365	325,503
Cash Flows from Investing Activities			
Additions to property, equipment and product rights	(75,870)	(45,028)	(81,834)
Acquisition of business, net of cash acquired	—	(1,558,322)	—
Additions to marketable securities and long-term investments	(8,451)	(18,835)	(26,083)
Proceeds from sale of marketable securities and investments	4,113	158,185	221,481
Other investing activities, net	15,916	44,581	2,791
Net cash (used in) provided by investing activities	(64,292)	(1,419,419)	116,355
Cash Flows from Financing Activities			
Proceeds from issuance of long-term debt	—	650,000	—
Payments on term loan, current debt and other long-term liabilities	(329,532)	(23,363)	(1,484)
Proceeds from stock plans	16,160	8,137	28,424
Repurchase of common stock	(1,776)	—	(300,000)
Other	2,645	—	—
Net cash (used in) provided by financing activities	(312,503)	634,774	(273,060)
Net increase (decrease) in cash and cash equivalents	50,383	(313,280)	168,798
Cash and cash equivalents at beginning of period	154,171	467,451	298,653
Cash and cash equivalents at end of period	\$204,554	\$154,171	\$467,451

Reconciliation Tables

(Unaudited; in thousands except per share amounts)

	Years Ended December 31,	
	2007	2006
GAAP to Adjusted Net Income Calculation		
Reported GAAP net income (loss)	\$141,030	\$(445,005)
Adjusted for:		
In-process research and development	—	497,800
Acquisition charges	12,782	12,477
Gain on sale of assets	(13,089)	(3,546)
Non-cash impairment charges	4,631	70,264
Early extinguishment of debt	5,553	525
Legal settlements	7,858	10,250
Income taxes	(6,716)	(31,781)
Adjusted net income	152,049	110,984
Add: Interest expense on CODES, net of tax	7,779	7,361
Adjusted net income, adjusted for interest on CODES	\$159,828	\$ 118,345
Diluted Earnings Per Share – GAAP		
Diluted earnings (loss) per share – GAAP	\$ 1.27	\$ (4.37)
Basic weighted average common shares outstanding	102,273	101,761
Effect of dilutive securities	14,766	—
Diluted weighted average common shares outstanding	117,039	101,761
Diluted Earnings Per Share – Adjusted		
Diluted earnings per share – Adjusted	\$ 1.37	\$ 1.02
Basic weighted average common shares outstanding	102,273	101,761
Effect of dilutive securities	14,766	14,591
Diluted average common shares outstanding	117,039	116,352
GAAP to Adjusted EBITDA Calculation		
GAAP net income (loss)	\$141,030	\$(445,005)
Plus:		
Interest expense	44,473	22,082
Interest income	(8,886)	(28,418)
Provision for income taxes	83,254	34,056
Depreciation	77,150	54,636
Amortization	176,409	163,710
EBITDA	513,430	(198,939)
Adjusted for:		
Non-cash impairment charges	4,631	70,264
Share-based compensation	14,244	13,336
Acquisition related charges	12,782	12,477
Litigation charge	7,858	10,250
Loss on early extinguishment of debt	5,553	525
In-process research and development	—	497,800
Gain on sales of assets	(13,089)	(3,546)
Adjusted EBITDA	\$545,409	\$ 402,167

Leadership

Board of Directors

Paul M. Bisaro

President and
Chief Executive Officer

Allen Chao, Ph.D.

Chairman

Michael J. Fedida

Registered Pharmacist
Consultant and Owner of
Several Retail Pharmacies

Michel J. Feldman

Member, Seyfarth Shaw LLP

Albert F. Hummel

President, Pentech
Pharmaceuticals, Inc.

Catherine M. Klema

President, Nettleton
Advisors LLC

Jack Michelson

Retired Corporate Vice President
and President, Technical
Operations, G.D. Searle

Ronald R. Taylor

President, Tamarack Bay LLC

Andrew L. Turner

Chairman, Enduracare Therapy
Management, Inc.

Fred G. Weiss

Managing Director,
FGW Associates, Inc.

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President and
Chief Executive Officer

David A. Buchen

Senior Vice President,
General Counsel and Secretary

Mark W. Durand

Senior Vice President and
Chief Financial Officer

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Senior Vice President,
Research and Development

Thomas R. Giordano

Senior Vice President and
Chief Information Officer

Edward F. Heimers, Jr.

Executive Vice President
and President, Brand Division

David C. Hsia, Ph.D.

Senior Vice President,
Scientific Affairs

Francois A. Menard, Ph.D.

Senior Vice President,
Generics Research and Development

Gordon Munro, Ph.D.

Senior Vice President,
Quality Assurance

Albert Paonessa III

Executive Vice President and
Chief Operating Officer,
Anda Distribution Division

Thomas R. Russillo

Executive Vice President
and President, Generics Division

Susan K. Skara

Senior Vice President,
Human Resources

Corporate information

Corporate Headquarters

311 Bonnie Circle
Corona, California 92880
951.493.5300

Common Stock

Stock symbol: WPI
Listed: New York Stock Exchange

Independent Registered Public Accounting Firm

PricewaterhouseCoopers LLP
Orange County, California

Stockholder Information

Questions concerning stock
ownership may be directed to
Investor Relations at Corporate
Headquarters.

Stock Transfer Agent

American Stock Transfer
and Trust Company
59 Maiden Lane
New York, NY 10007
800.937.5449
www.amstock.com

Annual Meeting of Stockholders

The Annual Meeting of Stockholders
of Watson Pharmaceuticals, Inc.
will be held at the Westin South
Coast Plaza, 686 Anton Blvd.,
Costa Mesa, CA 92626 on Friday,
May 9, 2008 at 9:00 a.m.

Press Release Information

Press releases and other information
are available on Watson's Web site
at www.watson.com.

Additional Information

Watson files periodic reports with
the Securities and Exchange
Commission that contain additional
information about the company,
including Watson Pharmaceuticals,
Inc.'s Annual Report on Form 10-K
and its Quarterly Reports on Form
10-Q. Copies are available on
Watson's corporate Web site at
www.watson.com, within the
Investors section, or at www.sec.gov,
or upon written request to Investor

Relations at the Corporate
Headquarters address. We have
also filed with the New York Stock
Exchange the most recent Annual
CEO Certification as required by
Section 303A.12(a) of the New
York Stock Exchange Listed
Company Manual.

Trademarks

The following Watson
Pharmaceuticals, Inc. trademarks
appear in this report: ANDRODERM,
INFED, FERRLECIT, OXYTROL,
TRELSTAR, URACYST. All other
trademarks are the property of
their registered owners.

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Any statements contained in this annual report that refer to future events or other non-historical facts are forward-looking statements that reflect Watson's current perspective of existing trends and information as of the date of this publication. Except as expressly required by law, Watson disclaims any intent or obligation to update these forward-looking statements. Actual results may differ materially from Watson's current expectations depending upon a number of factors affecting Watson's business. These factors include, among others, the ability to timely resolve with the FDA the pending Official Action Indicated status of the Davie, Florida manufacturing facility; the difficulty of predicting the timing or outcome of product development efforts and FDA or other regulatory agency approvals or actions; the ability to recognize the anticipated synergies and benefits of strategic transactions, including the Andrx acquisition; the impact of competitive products and pricing; market acceptance of and continued demand for Watson's products; difficulties or delays in manufacturing; and other risks and uncertainties detailed in Watson's periodic public filings with the Securities and Exchange Commission, including but not limited to Watson's Annual Report on Form 10-K for the year ended December 31, 2007.



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