



letter

February 16, 1999

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Arthur D. Levinson, Ph.D.
President and Chief Executive Officer

to stockholders

Since I assumed the leadership of Genentech in 1995, I have reported to you each year on the progress of our business plan. This year I do so with particular pleasure.

1998 was one of the most significant years in Genentech's history. We successfully launched Herceptin, the first monoclonal antibody for the treatment of certain types of metastatic breast cancer, offering enhanced survival time to some of the most seriously ill breast cancer patients. I give tremendous credit to Genentech employees, who discovered Herceptin, developed it, manufacture it, achieved its regulatory approval and launched the new medicine, with some records set for speed and efficiency along the way.

We also in 1998 recorded significant financial growth. In doing so we showed that excellent science can indeed serve as a foundation for solid operating results. Too often our industry has seen these two elements as representing incompatible goals. We, however, are taking a lead in demonstrating a new vision for business success in the industry. Solid business results are absolutely necessary for us to continue our scientific endeavors toward benefiting people's lives. I have gained great satisfaction, as I hope you have, from seeing our approach validated as our scientific efforts continue to drive important product introductions.

Key to our success in making a solid business of excellent science has been our strategy and Long-Range Plan (LRP). From the start, these were designed to be both flexible and disciplined. In 1998, we extended our specific goals into the middle of the first decade of the new millennium.

We reassessed our strengths and challenges and developed a new five-point strategy for achieving our goals — a refinement of our earlier four-point strategy that has served us well. While we have always been an industry leader in terms of science and numbers of products developed, we now strive to have leading financial results as well. For details of our goals and the strategy for achieving them, please see page 10 of this report.

We have shown with our success to date that the discipline of our strategy and LRP has not forced scientific compromise. Rather, it has spurred further innovation, allowing us to make progress in all operating areas within the constraints of our budget.

And our progress has been significant. Besides the approval of Herceptin, we also received a second FDA approval, for a label change to include safety information in the management of cystic fibrosis patients younger than age five with Pulmozyme.

In its first full year on the market, Rituxan was used to treat more than 16,000 patients worldwide — one of the most successful introductions of any cancer therapy. In Europe, Roche received approval to market MabThera (marketed as Rituxan in the United States) for a specific non-Hodgkin's lymphoma indication. Our initial successes with Genentech's BioOncology initiative set the stage well for the launch of Herceptin in the United States. We also reached an agreement with Roche for the international development and marketing of Herceptin. This agreement provides significant revenues to Genentech and helps ensure that this medicine will reach patients worldwide.

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For the remaining products in our portfolio — our growth hormone products and our thrombolytic medicine, Activase — we retained a significant market share even in the face of continued strong competition. These product lines continue to contribute significant revenues. For more information on our efforts related to our seven marketed products, please see page 14 of this report.

As we have since we launched our first product, we continue to support programs to help ensure that patients who need our medicines can receive them, regardless of their ability to pay. I believe that these programs — besides being of tremendous importance to thousands of people — are characteristic of the fundamental ethos of Genentech and its people.

Our product pipeline fuels both our hope for continued business success and patients' hopes for improved or extended lives. 1998 was a year of tremendous progress in our pipeline, and we are poised to learn key results for several of our potential products in coming months. In all, we now have 15 products in our development pipeline, including seven in Phase III or beyond.

Even with the best science, clinical research into new medicines occasionally identifies products that do not work significantly well for certain indications. This was the case with our and others' efforts investigating tissue-plasminogen activator, which we sell as Activase in the United States, for the treatment of acute ischemic stroke in patients arriving for treatment beyond three hours after symptoms began. Activase is currently approved and used successfully for treating acute ischemic stroke in patients within three hours of symptom onset, and we continue our efforts to educate the medical community and the public

about the urgent need for emergency medical treatment of stroke.

Occasional disappointments are to be expected in this business, which is one reason a broad yet focused pipeline of products is necessary for our continued success. As you can see in the section beginning on page 20, the potential medicines in our pipeline represent all four of our areas of therapeutic focus: oncology, cardiovascular medicine, endocrinology and opportunistic (where we pursue exciting opportunities that fall outside of the other three defined areas). With this broad base, even with the inevitable, occasional disappointments, I believe we are well-poised to enhance our portfolio of marketed products in the coming years.

As pipeline products move onto the market, we must ensure that we have the capacity to manufacture them. In 1998, we opened a second manufacturing facility in Vacaville, California, to provide this needed capacity. This new facility defines state-of-the-science for biopharmaceutical manufacturing and is a result of excellent planning by Genentech employees, who are now readying the facility to manufacture future supplies of Herceptin, the first product to be manufactured there.

As projects move through our pipeline, we must continue to build for the future by adding new ones. For this, our discovery research efforts are essential. Two years ago we began implementing a powerful approach to discovering new proteins with pharmaceutical potential. I'm pleased to report that we are beginning to see exciting results. I believe that this approach, called the Secreted Protein Discovery Initiative (SPDI), will serve well to keep our pipeline primed for the years to come. I invite you to read about our discovery efforts on page 18 of this report.

Also important to keeping our pipeline filled are our partnerships with other companies. In fact, such partnerships complement our efforts through all stages of the drug development process. Whether we are working with Abgenix, Inc.'s technology to create new potential antibody medicines, XOMA Ltd. to move a potential psoriasis medicine through the clinical testing process, IDEC Pharmaceuticals Corporation to promote Rituxan, or Schwarz Pharma AG and Sumitomo Pharmaceuticals Co., Ltd. to make our growth hormone available worldwide, our partners' efforts complement our own and strengthen our business. As you can read on page 26, powerful partnerships remain an important component of our business strategy.

While four of the five elements of our new five-point strategy for success are refinements of the elements of our earlier four-point strategy, the fifth one is new. It concerns investing in our people. In fact, it is primarily the articulation of this point in our strategy that is new: we have long recognized the value of our employees and invested in attracting, retaining and training the best people for the job. The fact that *FORTUNE* magazine recently named Genentech to its annual list of the "100 Best Companies to Work for in America" is testimony to our efforts. I'm pleased that we have added this point to our strategy, as it will ensure that we continue to recognize and invest in this valuable asset, and it reaffirms to our employees that they are at the heart of our strategy for success.

On that note, I want to thank our more than 3,300 employees for your tremendous efforts in 1998. You made our success. I also want to thank

all our stockholders for your continued support. You enabled us to pursue our goals. And finally I want to thank the medical community and the patients who use or are waiting for our medicines. In huge measure, you drive us to succeed. And we intend to continue to do so.

We face 1999 with a midyear deadline for Roche's call option followed by a stockholder put option on our stock. These will be important time points in defining our relationship with Roche. Our best approach to this challenge — and one that has moved our stock price beyond the specified put price of \$60 a share — is to continue with our focus on and commitment to implementing our plan for continued growth. We are working hard to ensure that, whatever the outcome of our arrangement with Roche, the spirit, culture and potential of Genentech will continue to flourish. We are also working to achieve financial results that will make exercising the put option unattractive to shareholders.

In 1999 and into the next century, we remain
in business for hope,
in business for results,
in business for life.

Sincerely,

/s/ Arthur D. Levinson

Arthur D. Levinson, Ph.D.
President and Chief Executive Officer