

FINAL TRANSCRIPT

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MRK - Q2 2007 Merck & Co., Inc. Earnings Conference Call

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PRESENTATION

Operator

Good day, everyone, and welcome to Merck's second quarter 2007 earnings conference call. Today's call is being recorded.

At this time, I would like to turn the call over to Mr. Graeme Bell, Executive Director of Investor Relations. Please go ahead, sir.

Graeme Bell - *Merck & Co., Inc. - ED, IR*

Thank you, Cynthia, and good morning. Welcome to our call this morning to review the business results for the second quarter of 2007. Joining me on the call today are our Chairman, President and CEO, Dick Clark, and for the last time prior to her formal retirement, Miss Judy Lewent, our Executive Vice President and Chief Financial Officer.

Before we get into the details, let me go over the logistics as usual. On this call, we will review the results contained on the release we issued at 7:30 a.m. this morning. You can access this through the Investor Relations section of Merck.com, and I would remind you that this conference call is being webcast live and recorded. The replay of this event will be available later today via phone, webcast and our usual pod cast.

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As we begin to review the results, let me remind you some of the statements made during this call may discuss certain subjects that may contain forward-looking statements as that term is defined in the Private Securities Litigation Reform Act of 1995. These statements are based on management's current expectations and involve risks and uncertainty which may cause results to differ materially from those set forth in the statements. The forward-looking statements may include statements regarding product development, product potential or financial performance. No forward-looking statement can be guaranteed, and actual results may differ materially from those projected. Merck undertakes no obligation to publicly update any forward-looking statements whether as a result of new information, future events or otherwise.

Forward-looking statements in this call should be evaluated together with the many uncertainties that affects Merck business, particularly those mentioned in the risk factors and cautionary statements set forth in item 1A of the Merck's form 10-K for the year ending December 31, 2006, and its periodic report of form 10-Q and form 8-K which the Company incorporates by reference and that are posted on our website. With that, let me turn the call over to Dick Clark, for prepared remarks.

Dick Clark - Merck & Co., Inc. - CEO, President, Chairman

Thank you, Graeme, and good morning, everyone. The results we are reporting to you today reinforce our confidence that Merck's plan to regain our leadership position in the pharmaceutical industry is the right one and that we are successfully executing our plan. Our overall performance has positioned us well to achieve our business targets, meet the challenges that lie ahead, and continue to invest in drug discovery.

I am pleased to announce that our second quarter 2007 earnings per share were \$0.82, excluding restructuring charges, a 12% increase from the second quarter of 2006. Our reported EPS for the second quarter were \$0.77, both results include the impact, the reserving and additional \$210 million for future Vioxx legal defense costs. In addition, our worldwide sales were \$6.1 billion during the quarter, and \$11.9 billion for the first six months of 2007. This revenue in the first half of 2007 is up 6% from the same period last year, and I would note that our results include Zocor in the base. This better-than-expected performance was driven by a broad range of both our newer and our established products, delivering strong growth again during the second quarter.

Singulair continues to be the number one prescribed product in the United States respiratory market, with worldwide sales last quarter reaching \$1.1 billion, an increase of 15% from the same quarter last year. Vytorin and ZETIA achieved all-time highs in both new and total prescription share in the quarter, posting combined global sales of \$1.3 billion, an increase of 30% compared to the second quarter of 2006. Gardasil, along with our pediatric vaccines, helped drive total worldwide vaccine sales over the \$1 billion mark in the quarter, nearly tripling the total vaccine sales in the second quarter of last year.

Global revenue for JANUVIA and JANUMET reached \$144 million, and \$24 million respectively in the second quarter. Managed care acceptance of these medicines has been strong and we're pleased that all major pharmacy benefit managers in the United States have added both of them to their formularies. Our revenues reflect the high value that physicians, patients and payors are placing on our products and on the healthcare benefits they provide. They also demonstrate that we continue to build on momentum established with our product launches last year.

Regarding the full year 2007, we are raising our EPS guidance range to reflect the impressive sales growth that our products have achieved during the first half of the year. We now anticipate a full year EPS range of \$3.00 to \$3.10, excluding restructuring charges and reported full-year EPS range of \$2.80 to \$2.95. Judy Lewent will provide more details on the financial performance and guidance in a few minutes.

As we look at the third and fourth quarter of 2007 and into 2008, we are working to ensure our expected launches of ISENTIS and of MK-0524A are accomplished with the same level of energy and success that distinguished our product launches in 2006 and 2007. We are pleased that the FDA has granted ISENTIS priority review status, and we anticipate regulatory action by mid-October following the FDA Advisory Committee meeting scheduled for September 5th. If approved, ISENTIS would be the first in a new class of anti-retroviral agents called integrase inhibitors, and in clinical trials, ISENTIS has demonstrated the ability

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to block the ability of the HIV virus to replicate and infect new cells in human patients. ISENTRIS has the potential to represent a significant step forward in meeting one of the world's major unmet medical needs.

We continue to anticipate an NDA will be filed with the FDA in the second half of 2007 for MK-0524A, our investigational atherosclerosis compound. MK-0524A combines Merck's extended release niacin with the Merck compound that reduces flushing, a common side effect of niacin therapy. In addition to the progress we are making in our own pipeline, we are also continuing to seek new licensing opportunities and targeted acquisition in therapeutic areas that are of strategic importance to Merck.

Earlier this month, we announced an important licensing agreement with Ariad pharmaceutical. This agreement expands Merck's investment in the field of oncology and holds the potential of bringing a novel medicine to cancer patients worldwide. Our future success clearly depends on our ability to discover, develop, and market novel medicines that address unmet medical needs, and entering into these types of agreements clearly complement our in-house efforts. To support these efforts, we also remain focused on controlling expenses to further reduce our cost structure and creating a leaner and more nimble business model, so that we can respond quickly and efficiently to customers' expectations and the demands of the market. We remain on track to deliver what we promised eighteen months ago, double-digit compound annual EPS growth excluding one-time items and restructuring charges by 2010 from a 2005 base.

When I reflect on what this quarter means to Merck, I see it as significant for several reasons. New product launches are continuing to gain momentum and strong acceptance in the market place. We are translating lessons learned from our new launches to our established brands and seeing greater market acceptance as a result. The quality of our external partnerships and alliances are reinforcing our considerable research efforts that are commitment to the development of new medicines, and all of these factors, when looked at in context with our 2010 stated goals, give us confidence that we can sustain our strong overall growth.

Before I turn the call over to Judy for what really will be her last earnings call with Merck, I wanted to take this opportunity again to thank her for 27 years of service to Merck, to thank her for her leadership, her commitment, her dedication and her accomplishments as CFO of Merck and Company. So with that, I am pleased to turn the call over to Judy.

Judy Lewent - Merck & Co., Inc. - CFO

Thank you, Dick, very much, and thank you for joining us today and good morning. As Dick said, we are extremely pleased with our reported results. In the second quarter of 2007, the Company reported mid-single digit growth on the top line and double-digit growth on the bottom line, as we continue to work toward our stated long-term performance targets. The second quarter recorded EPS growth, excluding restructuring costs, was driven by revenue that reflects strong performance of our in-line franchises like Singulair and Cozaar, as well as the rapid early up take of JANUVIA and JANUMET, and the continued strong growth of Gardasil. Other notable contributions to this result came from our improving product gross margin and the outstanding performance of our partnership and alliances, which resulted in enhanced equity income. As usual, I will go into more detail about the important underlying drivers of our performance and explain why we remain confident in our abilities to achieve our higher full year EPS guidance for 2007.

Dick mentioned several of the highlights of the quarterly results a moment ago, so I will build on that. In the second quarter we saw revenue of \$6.1 billion. That represents a 6% increase over the same period last year including in the aggregate, an overall 4% growth in volume and a 2% positive impact coming from foreign exchange. Collectively, worldwide revenue was above our initial expectations, and we saw encouraging sales performances from our newer and in-line franchises. A major contributing factor to our top line growth came from our vaccines business. Collectively, vaccine revenue as recorded by Merck, was in excess of \$1 billion for the second quarter, representing a 199% increase as compared to the same period in 2006. Driven by the continued up take of Gardasil, RotaTeq, and ZOSTAVAX in the second quarter, our three new vaccines collectively accounted for greater than \$0.5 billion of revenue.

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As always, to assist in your modeling, we provide a breakdown of the product revenues in our other financial disclosure schedule. We are extremely pleased that the global sales for Gardasil as recorded by Merck reflect the continued strong underlying demand for the vaccine in both the public and private sector. Of the \$358 million recorded in the quarter, \$286 million was in the United States. Sales outside the U.S. continued to show strong growth and increase 34% sequentially as we continued to successfully navigate the processes surrounding regulatory approval, country recommendations, and reimbursement with governments.

Gardasil has been approved in 80 countries, mostly under accelerated reviews, and has been launched in 69 of those countries. When you take the end market sales as recorded by Merck, and include end market sales recorded by the ST-MSD JV, global sales of Gardasil increased 10% sequentially in the second quarter. Total sales of Merck's other promoted medicines were collectively \$1.4 billion for the second quarter, representing a 17% increase compared to same period in 2006.

As you know, late last year we launched JANUVIA. It is currently approved in 61 countries worldwide as the only DPP-4 inhibitor available for use in the treatment of type two diabetes when diet and exercise are not enough. In its second full quarter on the market, global revenue of JANUVIA reached \$144 million, of which \$137 million was in the U.S. In the domestic market, we have shown strong growth in new and total prescriptions since March, indicative of robust underlying demand and the broad utility of JANUVIA and JANUMET in the clinical setting, and as market share data shows, the introduction of JANUMET is not cannibalizing JANUVIA, and it is clearly adding to the overall value of the franchise. In the U.S., JANUVIA has achieved reimbursement coverage for more than 164 million lives on Tier-2, and for more than 210 million lives in Tiers 2 and 3 combined. JANUMET has achieved reimbursement coverage for more than 112 million lives in Tier 2 and more than 200 million lives in Tiers 2 and 3 combined.

Also contributing to our top line, our revenues from our alliances, primarily AstraZeneca LP. In the second quarter, revenue recorded by Merck from the company's relationship with AZLP was \$524 million. As always, keep in mind that there is inherent variability relating to this revenue given that Merck is not actively managing these products. Our revenue recognition takes into account inventory levels at AZLP for PPI and non-PPI products as well as their product shipments. As we have stated many times, we have the opportunity to capitalize on our robust product portfolio and deliver compound annual revenue growth through 2010.

Despite the patent expirations that we all know will occur during this time frame, we continue to expect that our in-line products, our launch products and our potential new products if approved can drive revenue growth of 4 to 6% on a compound annualized basis including 50% of the revenues of the joint ventures from the 2005 base. Taking the second quarter revenue announced today and adding 50% of the revenues from the Merck Schering-Plough, Merial, Sanofi Pasteur MSD, and Johnson and Johnson Merck joint ventures and partnerships, revenue was \$7.2 billion. If you do the same adjustment in the base period, the revenue growth was 8%.

Year-to-date, our reported sales were \$11.9 billion, an increase of 6% over the same period last year. I need not remind you that this stellar top line growth is over a base period that included Zocor and Proscar prior to their loss of marketing exclusivity. If we were to exclude Zocar, Proscar, and the revenue associated with the supply of authorized generics from the first half of 2007, and the first half of 2006, then our year-over-year revenue growth would have been 28%. This again emphasizes the strength of our organic growth, fueled by our established brands and newer products.

Regarding 2007, given the second quarter and year-to-date performance, we are revising upward our full year revenue guidance by more than \$1 billion to support our increased full year EPS guidance provided today. This guidance revision includes five of our product guidance elements. Regarding Singulair, we are increasing by \$100 million the full year range, which makes that 4.0 to \$4.3 billion. Regarding vaccines, we are increasing by \$600 million the full year range, which makes that 3.9 to \$4.3 billion. Regarding Cozaar Hyzaar, we're increasing by \$100 million the full year range, which makes that 3.2 to \$3.5 billion. Regarding Fosamax, we are increasing by \$200 million the full year range, which makes that 2.8 to \$3.1 billion. Regarding other reported products, we're raising the full year range and now anticipate that to be 5.6 to \$5.9 billion.

We are reaffirming full year guidance for Zocor and AstraZeneca. As always, the AZLP guidance is an update based on recent results as well as future expectations and reflects the dynamics of the PPI market, multiple generics, OTC products and the

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uncertainty these create with regard to future volume and pricing. Also keep in mind that our reaffirmed guidance incorporates the expectations of the non-PPI products such as Atacand, Plendil, Lexxel, and Entocort.

Moving down the P&L, materials and production came in at \$1.6 billion for the quarter. The quarter includes \$119 million for costs associated with the global restructuring program primarily related to accelerated depreciation and asset impairment costs. Excluding these costs, materials and production increased 12% in the quarter. Our gross margin in this quarter was 74.6%, reflecting a 1.9 percentage point unfavorable impact relating to the restructuring costs. Excluding restructuring charges, we had a second quarter product gross margin of 76.5%. Just as in previous periods, these results were affected by the final product mix. For the half year, our adjusted gross margin is 76.1%. Given the strength of this result, we are raising our full year 2007 guidance range and now anticipate our product gross margin to be approximately 75 to 76%. This guidance excludes the portion of the restructuring costs that will be included in product costs and will affect reported product gross margins in 2007.

Regarding marketing administrative, second quarter expense came in at \$2.1 billion, an increase of 20% over the same period last year. In the second quarter, after reviewing the actual costs incurred and estimates of future costs, the Company determined that it was appropriate to record a charge of \$210 million to increase the reserves solely for its future legal defense costs related to the Vioxx litigation to \$810 million at June 30, 2007. Regarding the legal defense reserve charge, the Company accrued legal defense costs expected to be incurred in connection with a loss contingency where such costs are probable and reasonably estimable.

In the second quarter, the Company spent \$137 million in the aggregate for legal defense costs worldwide related to the Vioxx litigation. In adjusting the reserve, the Company considered the same factors that can be considered when it previously established reserves for the Vioxx litigation, including the actual costs incurred by the company, the development of the company's legal strategy and structure in light of the scope of the Vioxx litigation, the number of cases being brought against the Company, the costs and outcomes of completed trials, and most current information regarding anticipated timing, progress, and related costs of pretrial activities and trials in the Vioxx product liability losses.

Events such as scheduled trials which are expected to occur throughout 2007 and into 2008 and the inherent inability to predict the ultimate outcomes of such trials limits the Company's ability to reasonably estimate its legal costs beyond the end of 2008. Accordingly, the reserve at June 30, 2007, represents the Company's best estimate of legal costs that will be incurred through 2008. While the Company does not anticipate that it will need to increase the reserves every quarter, it will continue to monitor its legal defense costs and review the adequacy of the associated reserves. It may determine to increase its reserves for legal defense costs at any time in the future, if, based on the factors set forth, it believes it would be appropriate to do so. The Company has not established any reserves for any potential liabilities relating to the Vioxx litigation.

We continue to believe that every case contains a unique set of facts, and the appropriate strategy is to defend these matters on a case by case basis. So excluding the charge, marketing and administrative increased 8% in the quarter. Regarding the underlying level of spend once again, the primary driver of the marketing administrative increase was promotional spend for Gardasil, Zostavax, and continuing efforts to more aggressively support the JANUVIA and JANUMET launches. Where appropriate, these were deliberate choices made in response to the evolving competitive dynamics that we felt could provide additional advantages as we have the first in class products.

As you have seen from our revised product-specific financial guidance, we are adjusting revenue upward to reflect these incremental investments in order to enhance our opportunity to better position our products in 2007 and beyond. Reflecting our commitment to realizing efficiencies throughout the Company and optimizing our cost structure, the component of marketing administrative consisting of selling administrative and general administrative costs which support our core operations remain down through the first half of 2007 over the prior year.

Even as we plan to launch additional new products this year, and continue building on the momentum of our successful 2007 launches, we expect that our cost containment efforts and initiatives will allow us to meet our guidance on marketing and administrative spending in 2007 and our commitment to maintain flat marketing and administrative expenses in 2010 relative

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to the 2006 space excluding charges taken to increase the legal defense reserves. Regarding 2007 guidance, we're continuing to provide it on the change in marketing and administrative expense relative to the base period, excluding one-time items to help in your modeling, and we are reaffirming our full-year 2007 guidance. That is, we anticipate marketing and administrative expense to increase between 0 and 2 percentage points over the full year 2006 level.

Regarding research and development, expenses were \$1 billion for the quarter. This represents a decrease from the comparable period in 2006 of 12%, but we should note that this time last year we acquired GlycoFi. I want to take an extra minute to explain this result and our R&D guidance for the remainder of the year. At Merck we remain committed to fully funding core internal R&D to ensure that continued progress of compounds in all phases of development. Internal R&D growth remained strong as we continue to invest in late stage clinical trials on Isentris, MK-0524A, MK-0524B, MK-0364, MK-0822, MK-0974, sitagliptin and vaccines. In addition to this significant investment in our internal research capabilities, the Company continues to fully fund clinical grant programs, third party scientific collaborations, and licensing transactions.

When we provide R&D guidance, it includes certain assumptions regarding the timing of partnering and licensing transactions. For example, earlier this month, we announced the licensing transaction with Arad that includes significant up front and incremental payments we now anticipate to occur in the third quarter. Originally we anticipated the transaction closing in the second quarter of 2007. At Merck, partnering is an essential component of our strategy to discover and development novel medicines that meet major unmet medical needs. We place a premium on our ability to identify the best external opportunities and these opportunities require ongoing and incremental investment.

However, given the nature of transactions, there is inherent variability. Therefore, we now anticipate that research and development expense excluding restructuring charges to be higher in the third quarter than in this quarter. Regarding the full year, we are raising our 2007 guidance for research and development expense to adequately resource incremental external R&D opportunities, and now I anticipate R&D spend to increase at a mid to high single digit percentage growth rate over the full year 2006 level, and I would refer you to our press release to see how we define the base period.

Moving on to restructuring, total costs associated with the Company's global restructuring program were \$172 million for the second quarter, and as I just mentioned, there were \$119 million within there for asset related charges that are included in materials and production. The restructuring cost line reflects \$55.8 million of costs for employee separation, and other related costs associated with the approximately 625 positions eliminated, bringing the total to 5,700 to date. We remain on track to eliminate 7,000 positions by the end of 2008. During our ongoing restructuring process, we have identified opportunities to accelerate schedule closures, and therefore we are raising our guidance for 2007. As part of the company's restructuring of its operations, additional costs related to site closings, position eliminations and related costs will be incurred in 2007.

The aggregate 2007 pre-tax expense related to these activities is estimated to be 500 to \$700 million. In reviewing equity income from affiliates, you will see \$759 million in income in this quarter related to the contributions from all of our joint ventures. This result reflects the continued success of the Merck Schering-Plough cholesterol franchise in the U.S. and Europe in the seasonality of the Merial animal health business. As always, I would remind you that there are several components components to AZLP equity income which make it inappropriate to draw significant conclusions just based on PPI products. There are complexities that involve at a minimum timing and tax differences. That said, the second quarter equity income contribution from Merck's share of the partnership with AstraZeneca LP was \$215 million.

Regarding the Merck Schering-Plough partnership, the second quarter combined MSP cholesterol franchise global revenue as reported by the Merck Schering-Plough partnership, continued to grow to \$1.3 billion. In the quarter, revenues of Vytorin and ZETIA were \$686 million and \$578 million respectively. In the U.S., Vytorin was \$534 million, up 27%, and ZETIA was \$424 million, up 17%. Within Merck's quarterly equity income results, the Merck Schering-Plough partnership contributed \$465 million, and that reflects a 45% increase over the prior year. The balance of equity income comes from our other joint ventures, namely Merial, Sanofi Pasteur MSD, and Johnson & Johnson Merck. Given this result, we're raising our guidance for full year 2007 equity income by \$100 million, and now expect equity income from affiliates to be approximately 2.7 to \$3.0 billion.

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For the quarter, income before taxes was \$2.2 billion. Taxes on income in the period were \$556 million, and the reported tax rate was 24.9%. This reflects in general the changes in foreign and domestic mix and currency fluctuations and these elements change throughout the quarter. We are reaffirming our full year 2007 tax rate guidance range, and I would direct you to today's press release for the details.

Moving on to net income and earnings per share, net income for the second quarter is \$1.7 billion, compared to \$1.5 billion in the second quarter of 2006, and that represents growth of 12%. During the quarter, we spent \$250 million in treasury stock and now have \$6 billion under the current authorization from the Board with no time limit. In summary, earnings per share for the second quarter were \$0.82 excluding a \$0.05 charge for site closures and position eliminations primarily associated with the global restructuring, and our reported second quarter EPS was \$0.77.

Turning briefly to our guidance, I have mentioned several changes as a part of the results review, and I would direct you to the details of our financial guidance contained in today's release. We are raising or changing many elements of our full year 2007 guidance, and as a result, Merck is raising the full year 2007 EPS range to \$3 to \$3.10 a share, excluding the restructuring charges related to site closures and position eliminations. We now anticipate reported full year 2007 EPS of \$2.80 to \$2.95 a share. In other words, we anticipate that EPS, excluding restructuring, will grow in the range of 33 to 43% in the second half of this year versus the last six months of the base period. As stated, this guidance does not reflect the establishment of any additional reserves or any addition to reserves for any potential liability relating to the Vioxx litigation.

We're committed to providing quality full year guidance and updating it during the year. We believe that there is value in providing quality financial guidance because of it assists investors and promotes strong capital markets. We also recognize that our business is complex, and we serve our investors well by communicating our financial performance expectations. At this point in the year, we are halfway through. You now have six months of actual results, and to assist in your modeling, we have provided you with an upward revision on EPS and refreshed the detailed elements of our full year financial guidance. Our revised product specific financial guidance reflects that we continue to anticipate strong performance from our key franchises in the second half of the year.

Regarding R&D, partnering is an essential component of our strategy to discover and develop novel medicines. We place a premium on our ability to identify the best external opportunities, and these opportunities require ongoing and incremental investment. However, given the inherent variability associated with transactions, we now anticipate research and development expense, excluding restructuring charges, to be higher in the third quarter than the amount reported in the second quarter. We believe it is prudent not to give specific EPS guidance for the third quarter of 2007, as this year progresses and we gain more clarity on many opportunities we have, we will evaluate the best way to provide you with insight into our progress towards our annual financial guidance.

In addition, as Dick noted, the company remains on track in terms of both strategy and performance to deliver long-term double-digit compound annual earnings per share growth from 2005 to 2010, excluding one-time items and restructuring charges. I also want to continue to emphasize that we have the financial strength to support our dividend and we remain fully committed to maintaining it at the current level while at the same time continuing to fully invest in our key priorities for our strategy going forward. With that said, I will turn the call back over to Graeme.

Graeme Bell - Merck & Co., Inc. - ED, IR

Thank you, Judy. We will now open the call and take your questions. We will take the questions in the order they are received and try get through as many as possible in the allocated time. At this point, I will turn the call over to Cynthia, who will communicate instructions for our Q&A format, then introduce the first question.

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QUESTIONS AND ANSWERS

Operator

(OPERATOR INSTRUCTIONS). Your first question comes from David Risinger with Merrill Lynch.

David Risinger - Merrill Lynch - Analyst

Thanks very much, and thank you, Judy, and best of luck to you. With respect to my questions, first, if you could please provide an update on the Zostavax and ProQuad manufacturing issues and the outlook for resolution. Second, with respect to Gardasil, the product was down sequentially in the U.S. If there is any help you can provide to help us understand how much stocking may have inflated the first quarter '07 sales and what the underlying sequential demand was in the second quarter that you have seen, that would be helpful, and finally, if you could comment on the factors that you expect will hold back the second half of '07 adjusted EPS relative to what you booked for first half of '07 adjusted EPS, you have obviously called out the R&D item for the third quarter, but any more color on that would be helpful. Thank you.

Dick Clark - Merck & Co., Inc. - CEO, President, Chairman

With regards to your first question, on the varicella potency issue we're making excellent progress on finalizing the manufacturing and technological changes we have to make for varicella, and I have a great deal of confidence from a planning standpoint we will actually start a varicella in that fashion this month. Obviously it will take us a period of time to know the results, but I think we're there from an ability and confidence level to start up again.

Concerning your question with Gardasil, talking about stocking and inventory, that's a very difficult question to answer. We can tell you that 50 of the vaccine for children projects did make purchase at the end of the first quarter and obviously that that inventory is being utilized in the country as a part of those projects. As Judy said, we still see strong growth in the U.S. and outside the U.S., so I think it will just take us a period of time as we get the stocking and inventory levels, but there is no question as we can see by our relationship with health plans and other formularies, that the utilization of Gardasil in the United States is very, very positive.

Judy Lewent - Merck & Co., Inc. - CFO

I will take the last question. Thank you for your good wishes, Dave. You're absolutely right, first of all. As you think about progression on R&D expense, both the continued growth and supporting the rollout of our pipeline, and making sure we're supporting that as well as a real focus on external opportunities, that's contributing to the different expense level in R&D in the second half versus the first half, but I would also point you to marketing administrative. Even though as I noted, we are reaffirming that for the year marketing administrative will be growing between 0 and 2% on normalized basis excluding the one-time charges.

I do call your attention to the fact that not only are we continuing to roll out launches for products but typically the second half is a heavier half in terms of spending, so in terms of change versus prior year for the year, we expect to be 0 to 2%. In terms of absolute level, I call your attention to what the spending patterns tend to be in the third and in particularly the fourth quarter. You need to factor that into the analysis.

Dick Clark - Merck & Co., Inc. - CEO, President, Chairman

What's exciting about what we're talking about from a launch standpoint, when you look at the numbers that Judy and I presented this morning, if you look at JANUVIA, it is approved in 51 countries, but only launched in 25 so far. With Gardasil approved in 80, launched in 59 and under review in another 40, and with RotaTeq, 61 countries approved and only launched

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in 22 and JANUMET moving forward will have the same numbers, and Isentris is in addition, so we are definitely even though we launched these important products and vaccines, and in several countries, we're still in the launch phase, and we have to make sure we support that launch phase the right way.

Graeme Bell - Merck & Co., Inc. - ED, IR

Next question, please.

Operator

Your next question comes from Jami Rubin with Morgan Stanley.

Jami Rubin - Morgan Stanley - Analyst

Thank you. Ditto to Judy. My best wishes. I have two specific questions. One, I am wondering if you can provide an update on Vioxx litigation, specifically, are there any forthcoming cases that we should be aware of that on the case front has been pretty quiet and just wondering what's coming down, what's in the calendar going forward. Secondly, what is the status of the New Jersey Consumer Protections Act and are there other consumer protection acts forming outside of New Jersey, and lastly we'll continue to argue the 18 month window or has that now been discredited because of the Victor trial, and a question on gross margins, Judy, the guidance for the year now has been adjusted to 75 to 76%, but on an adjusted basis this quarter it was 76.5% and that's with a heavy drag from Zocor, which goes away in the second half, or is this typical Merck conservatism, or is there something that we should be aware of that acts as a natural drag on gross margins and could it be that as Gardasil sales add another whatever in the second half that the actually gross margin contribution becomes a detriment, but because of the royalty payments and lower yields, but if you can address that, I would appreciate it. Thanks.

Graeme Bell - Merck & Co., Inc. - ED, IR

Jami, let me start if you wouldn't mind on the Vioxx related questions. As always, we commit to posting the trial schedule on Merck.com, and as of July the 20th, you will see that there are seven trials scheduled for the balance of 2007 starting on September 17th in California and we are currently posting that there are four starting on January the 7th, 2008, up through April of 2008. With regard to the seven, as posted to Merck.com, you will see that, for instance, some are consolidated. I would direct you back to that for the details, but I would point out, for instance, in New Jersey and Atlantic County on October 15th, the current schedule calls for New Jersey coordinator trials where there will be four trials and up to two or three plaintiffs in each respective trial, and also in California in November the 26th, a trial is scheduled to start with up to 5 plaintiffs, so I would just point you to that and it gives you a cents of the activity and schedule going forward.

With regard to Victor and the science behind that, I think we indicated many times that that is but one study, and you know the history in terms of it being stopped prematurely, and that data such in and of itself has been available to all plaintiff and this has been argued and presented many times in the 15, 16 16 trials that have actually gone through to juries, and we feel that that one data point in and of itself can draw no conclusion whatsoever, so we remain steadfast based on the scientific evidence relating to the long-term trial. With regard to consumer fraud here in New Jersey, that really was just in a holding pattern so to speak, and the judges have yet to render their specific opinion, and we just don't have a sense of when that decision will come down, and right now that is the only consumer case that is currently work in progress awaiting a decision. Once we communicate that decision, clearly we'll take appropriate steps. Just as a reminder, it does cause a decision pertaining to whether a class action will be created as opposed to anything else, so that's the update on Vioxx right now, and I will pass it over to Judy or Dick for the PDM question.

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Judy Lewent - Merck & Co., Inc. - CFO

Thank you, Jami. So first of all, as I believe you noted, we did tighten the product gross margin guidance range, so we were at 74 to 76, and given the performance of the first six months, we are comfortable with 65 to 76, but you do have to bear in mind although the first half looks promising, that product mix is a very key factor here, and so that's what we have taken into account as we think about the full year.

Graeme Bell - Merck & Co., Inc. - ED, IR

Thank you. Next question, please.

Operator

Your next question is from Bert Hazlett with BMO Capital Markets.

Bert Hazlett - BMO Capital Markets - Analyst

Thanks. I will take a follow-onto Jamie's question. As we see the vaccine business continuing to grow, not only with Gardasil with the other vaccines, RotaTeq in particular, how should we think about the pushes and pulls on the margins? Again, gross margins and SG&A, and then secondly, you made a comment on 524 A in terms of filing in the second half. Could you remind us as to 524 B, and are you still supporting the time lines with that particular combination? Thanks.

Judy Lewent - Merck & Co., Inc. - CFO

Relative to the pushing and pull on vaccines, as we don't get into details across the product line, we have noted from time to time that vaccines tend to have a slightly lower product gross margin than some of our other in-line products, and of course as you know Gardasil in particular carries a royalty burden that we discussed in the 24 and 26% range. That said, what we continue to see in our performance year-to-date and what we expect in the future are improvements across the board including vaccines in terms of productivity improvements that will continue to improve the possibility for a product gross margins and as we guided to product gross margins through 2010, we did note that we expect to return to pre-Zocor patent ex levels, and we continue to reaffirm that and that is in full recognition of the product mix we see going forward, so it is really continued improvement on manufacturing productivity improvements and recognition of the product mix we have but still delivering that uptick in product gross margin by 2010.

Dick Clark - Merck & Co., Inc. - CEO, President, Chairman

Your question with 524-B,B, as we stated along the clinical trials.gov, protocol number 63 is an MK524-B lipid study, and we're currently rolling patients for that study, and really there is no change from a timing standpoint, and we're committed to the 2008 filing for 524-B, so we feel that's on track for '08.

Graeme Bell - Merck & Co., Inc. - ED, IR

And with regard to 524-A, we remain committed as indicated in the prepared remarks that an MDA will be filed with the FDA in the second half of 2007. Cynthia, could we have the next question, please.

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Operator

Your next question comes from James Kelly with Goldman Sachs.

James Kelly - *Goldman Sachs - Analyst*

Good morning and let me also echo my best wish to say Judy. I have a question about Gardasil and how we should be thinking about Gardasil in the various patient cohorts and how adoption is going there and any sense of how it might have changed from the first quarter into the second quarter and anything that's coming back from the sales salesforce about people using above the age of 26. Thank you.

Dick Clark - *Merck & Co., Inc. - CEO, President, Chairman*

We certainly don't have information that we can provide you on the specifics, the detailed specifics you're asking at this time. The important thing that we're focusing our attention on from a compliant standpoint and precision standpoint is to make sure when the [indiscernible] receive their first shot of Gardasil, the first vaccination they're able to come back and get the second and third which is critical, so we're making sure that physician offices with healthcare practices, there are reminder mechanisms and capabilities put in place that a second and third vaccine is put in place, but we can't give you specifics on the questions that you asked.

Graeme Bell - *Merck & Co., Inc. - ED, IR*

Thank you. Next question, please.

Operator

Your next question comes from Tony Butler with Lehman Brothers.

Tony Butler - *Lehman Brothers - Analyst*

Thanks very much. My question also is gross margin related, but it is related to the restructuring costs, Judy. The increase in this quarter for future activities of 500 to \$700 million I believe is a change from the previous quarter of 300 to \$500 million, and the question I have is is the change principally related to those site closings which could have some positive impact to gross margin and/or to product eliminations or position elimination s as it relates to SG&A which I guess could help operating margins, and the reason I am asking this is to offset maybe the dynamic growth in vaccines which could possibly put that as Jamie alluded to the drag on the overall gross margins, and this is principally related to the back half of the year but more importantly to 2008. Thanks.

Judy Lewent - *Merck & Co., Inc. - CFO*

Exactly. This is a timing -- this is strictly a timing issue, so this doesn't really change even our overall expectations of the network strategy that we rolled out in November of 2005, but it is a positive in terms of acceleration of some of our plans for site closures, so, yes, we're moving that along more rapidly than we originally anticipated in 2007. It is predominantly accelerated depreciation. It is not really driven by position eliminations per se, but really driven by the timing of site closures.

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Graeme Bell - Merck & Co., Inc. - ED, IR

Next question, please.

Operator

Your next question comes from Chris Schott with Banc of America Securities.

Chris Schott - Banc of America - Analyst

Quick questions. First you've had a very successful JV with one of your major -- when you talk about licensing transactions going forward, how would you characterize the opportunity for additional partnerships with some of major Pharma Co.s out there and not specific questions but compounds that interest you or are you looking at or should we see these deals more along the line of the area deal and the CB1 MK364, how comfortable are you with the Phase III program following the recent panel, and do you intend to or have you altered any of those Phase III program science thanks.

Dick Clark - Merck & Co., Inc. - CEO, President, Chairman

Concerns your first question, we're interested in any relationship with either our pharma colleagues or licensing capability in Biotech that really add long-term shareholder value. If there is a relationship based on the synergies between those two companies, then whatever they are would be important to consider them as we move forward. As we have always stated, target acquisition is sincerely a key part of our strategy as well, and we're looking at those from a Biotech company as well, not only for the relationship and the research but the relationship that we would have that would help the top line, so we're very flexible and open to those kind of relationships, and I think to Judy's credit, and she has built these relationships over the years, that we've been very success successful with our joint venture partnership in the past, and I think Merck is looked upon as a company to be able to have comments and objectives and to be successful for both parent company shareholders. In relation ship to your second question, it is really hard for us to speculate on the class effect, the CB-1s, and obviously we're scoring the clinical profile of our product as an ongoing part of our Phase III clinical programs.

Graeme Bell - Merck & Co., Inc. - ED, IR

Next question, please, Cynthia.

Operator

Your next question is from Steve Scala with Cowen.

Steve Scala - Cowen & Co - Analyst

Thank you. I have two questions. First, does Merck have an understanding of the level of Gardasil stock in physicians offices and if so has that changed quarter over quarter, and in the past I believe Merck has implied that there was not much stock in physicians offices, but that could be one explanation for a flattish quarter over quarter trend, and secondly, if the bioequivalent study is successful, what would that suggest for the timing of MK-0524-B in 2008, as a late 2008 filing more likely than mid or vice versa?

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Dick Clark - Merck & Co., Inc. - CEO, President, Chairman

524-B, we can't speculate, Steve on, what part of 2008. Our comment now is just based on 2008, and in your first question, I think we're gaining more information, but I don't think you will see a tremendous amount of stocking in the physicians offices for Gardasil particularly with the cost of Gardasil and the reimbursement process that we're trying to help as well. Don't nor get there is a difference between public and private, and so in the physicians office it could be more private, and very small. In public can could be building inventory as I said at the end of the first quarter for 50 to 55, and now it is being at this traited out, and we'll see what happens in the third and fourth quarter as that inventory is reduced.

Graeme Bell - Merck & Co., Inc. - ED, IR

Thank you, Dick. Given the time we might have about time for one more two more questions. Cynthia.

Operator

Your final question comes from Seamus Fernandez with Leerink Swann.

Seamus Ferndandez - Cowen & Co - Analyst

Thanks very much. I have a few questions. I was just wondering if you can update us on the timing of AZLP and given they are close involvement in original deal and restructuring if Judy will be available as a consultant to Merck on these issues. Separately, Dick, if you could give us given the strong performance year-to-date, can you give us an update on what you're keenly focused to continue delivering P&L leverage in 2008 particularly given the upcoming U.S. patent expiration of Fosamax? Obviously it will be balanced over the P&L, but if you can give us your biggest focus for execution where you see the best opportunity post 2007 and then as a last question, it took Merck six months to get full reimbursement approval under the vaccines for children program which clearly was very rapid, but is there any reason why the time frame would be shorter or longer for a new competitor and what is Merck planning for relative to new entrants for next year? Thanks very much.

Graeme Bell - Merck & Co., Inc. - ED, IR

Why don't we start with AstraZeneca.

Judy Lewent - Merck & Co., Inc. - CFO

AstraZeneca. I believe what you're referring to is a potential upcoming series of events in 2008 relative to the Merck option, and as many of you know, there will be events that are even independent of the exercise of our options that were triggered back in the 1998/99 period when Astra merged with Zeneca. Namely we will see the equity income priority return reduced from about \$300 million to about \$210 million, and we have recognition of some of the advance payments and other parts of the transaction that were put in place in '98 in the first quarter of 2008. We also will be repaying the \$1.4 billion loan in the first half of 2008, and so really what is left to reflect on is whether we are going to exercise the option for non-CPI products, and that will be evaluated in the coming months and really probably formally decided in the first quarter of 2008, and if Dick wants, he is more than welcome to give me a call as I get closer to that practice.

Dick Clark - Merck & Co., Inc. - CEO, President, Chairman

There is no question that Judy will always be a close adviser to the current Chairman and CEO, and so there is no hesitation that there will be a loss in the leadership she provided in that relationship. Regarding your question, we cannot speculate on the Zerbrex time line and what that means or assistant county attorney mean in the United States, and certainly my focus, Winston

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Churchill once said however beautiful the strategy you should occasionally look at the results, and I think we have looked at the results. I think we have shown you that our results are good, and that our strategy is validated by the results, and so my focus on 2007, 2008, 2009 and 2010 hopefully is to keep executing the strategy to make sure we have strong and talented business leaders in place and our franchise strategies are being executed by listening to our customers, that we continue to invest wisely in basic research and in our clinical development organizations continue accelerate our pipeline, and that we're able to become a lean and flexible organization by taking the right costs out at the right time.

Graeme Bell - Merck & Co., Inc. - ED, IR

So with that last question, it concludes the conference call. The information and all of the Q&A on today's call and the transcript and the replays will be available on our website for the next several months, and as always, Mike Nally and I will be available all day to take your calls and any of your incremental questions. Dick?

Dick Clark - Merck & Co., Inc. - CEO, President, Chairman

Thank you, Graeme, and thanks to all of you who participated and listened in on the call today, including our operator who kept things running smoothly. We look forward to speaking to you in October about our third quarter results. Thank you.

Operator

Ladies and gentlemen, this concludes today's Merck second quarter 2007 earnings conference call. You may now disconnect.

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