C

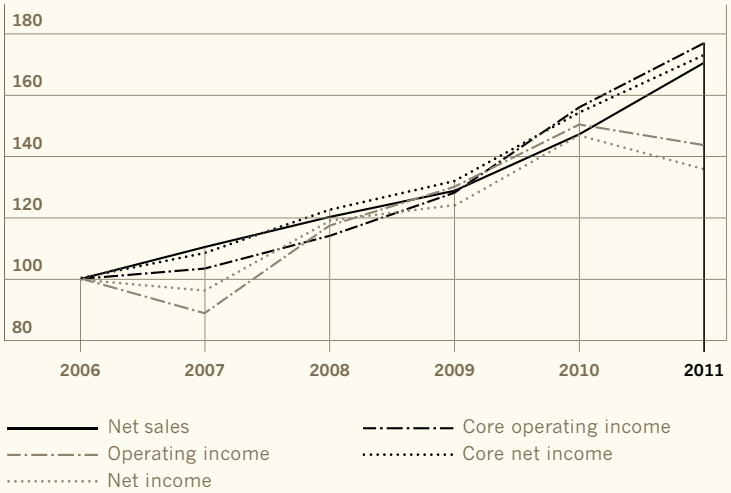
A CA C

FINANCIAL HIGHLIGHTS

KEY FIGURES
(in USD millions, unless indicated otherwise)

	2011	2010
Net sales	**58 566**	50 624
Operating income	**10 998**	11 526
Return on net sales (%)	**18.8**	22.8
Net income	**9 245**	9 969
Basic earnings per share [1] (USD)	**3.83**	4.28
Core [2]		
Operating income	**15 909**	14 006
Core return on net sales (%)	**27.2**	27.7
Net income	**13 490**	12 029
Basic earnings per share [1] (USD)	**5.57**	5.15
Research & Development	**9 239**	8 080
As a % of net sales	**15.8**	16.0
Number of associates (FTE) [3]	**123 686**	119 418
Return on average equity (%)	**13.6**	15.7
Group free cash flow	**12 503**	12 346

NET SALES, OPERATING INCOME, NET INCOME, CORE OPERATING INCOME AND CORE NET INCOME [4]
(Index: 2006 = 100%)



SHARE INFORMATION

	2011	2010
Share price at year-end (CHF)	**53.70**	54.95
ADS price at year-end (USD)	**57.17**	58.95
Dividend [5] (CHF)	**2.25**	2.20
Payout ratio [6]	**63**	55

2011 NET SALES BY REGION
(% and in USD millions)

United States	33	19 225
Europe	37	21 507
Asia/Africa/Australasia	21	12 354
Canada and Latin America	9	5 480
Total		**58 566**

[1] 2011 average number of shares outstanding: 2 382.5 million (2010: 2 285.7 million)
[2] Core results for operating income, net income, earnings per share (EPS) and R&D eliminate the impact of acquisition-related factors and other significant exceptional items. These adjustments are explained in detail starting on page 179.
[3] Full-time equivalent positions at year end
[4] To ease comparability, all figures for 2006 and 2007 exclude the Consumer Health Nutrition operations divested in 2007
[5] Dividend payment for 2011: proposal to 2012 Annual General Meeting
[6] Payout ratio is calculated based on net income attributable to shareholders of Novartis AG. 2011 based on estimated number of shares outstanding on dividend payment date.

NEWS IN 2011

A C 16% (+12%) 58.6 .
5% (+1%) 11.0 , 1.9 .
C 14% (+16%) 15.9
9.2 7% (-2%) . C
12% (+15%) 13.5 .

2007[1] 25% ? , 19% 2010.

C 2007[1] 38% 14.4 . C
15 2011 ,
, . A (*Afinitor/Votubia*)
, *Gilenya* ,
Lucentis , *Arcapta Neohaler*,
, . A , *Dailies Total 1*,
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, *WaveLight* 500 .

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- *Afinitor*,
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Bexsero -
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100%
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85% , C ,
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C A C . A -
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1.7 , 3% .

15 2% 2011 C 2.25
(2010: C 2.20), 4.2%.

[1] A (1) ; A 2010

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Gilenya,
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Votubia
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58.6 -
9.2
2011, - ,
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. *Tasigna* -

The strategy of focusing on the healthcare sector, which we have pursued over the last 15 years, has proven successful.

Glivec,
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. *Lucentis* C .
- , *Lucentis*
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2011 -
. *Diovan*

While there were many successes, there were also setbacks.

In 2011, Novartis continued its support for patients who are unable to afford treatment.

Menveo,

Bexsero

Diovan

Coartem

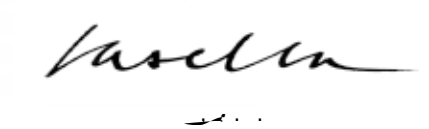
2001

480

1

33 000

In spite of the uncertain economy – particularly government debt and weak growth – we will pursue our strategy.



Chairman of the Board

BUILDING SUSTAINABLE LEADERSHIP IN HEALTHCARE

PHARMACEUTICALS	ALCON	SANDOZ	VACCINES AND DIAGNOSTICS	CONSUMER HEALTH
28% 2011.				

PATIENT-CENTRIC PORTFOLIO

STRATEGIC PRIORITIES

Extend lead in innovation

2007,

Accelerate growth

Drive productivity

WHAT WERE THE HIGHLIGHTS OF 2011 FOR NOVARTIS?

2011. -

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16%,

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38% 2011

25%

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17% 10%

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WHAT IS THE OUTLOOK FOR PERFORMANCE OF THE COMPANY?

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- *Diovan*

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- 2012. *Femara*

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SALES GROWTH ACCELERATED IN THE TOP SIX EMERGING MARKETS LAST YEAR. WHAT WERE THE KEY DRIVERS?

HOW HAS THE INTEGRATION OF THE NEW ALCON DIVISION PROGRESSED SINCE CONSOLIDATION IN APRIL?

NOVARTIS ANNOUNCED STRUCTURAL CHANGES TO REDUCE COSTS. WHY WAS THIS NECESSARY?

Dailies Total 1,

2014.

2012.

350 2013.

RECENTLY LAUNCHED MEDICINES HAVE FUELED GROWTH AT THE PHARMACEUTICALS DIVISION IN RECENT YEARS. DID THAT PORTFOLIO TRANSFORMATION CONTINUE?

Gilenya *Afinitor/Votubia*. *Lucentis* 26% *Tasigna* 19% *Tasigna*, B -2 2011 *Afinitor* 2012.

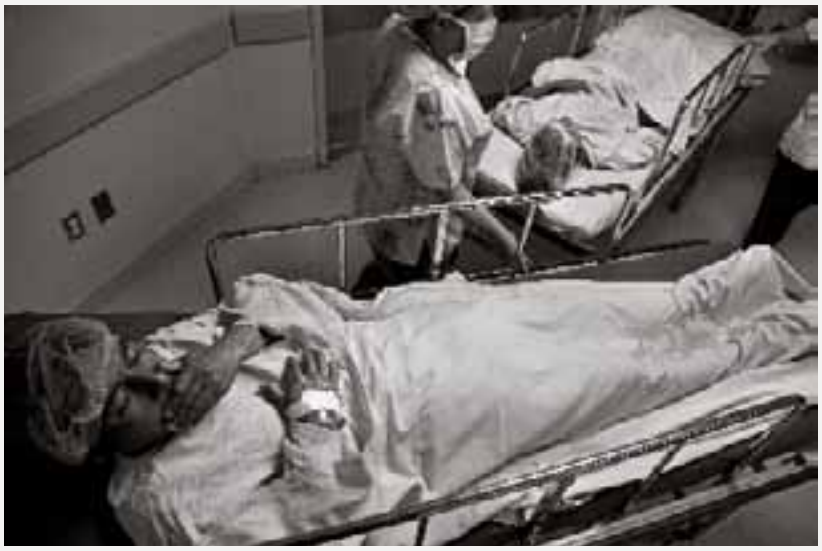
HOW DID OTHER DIVISIONS PERFORM IN 2011?

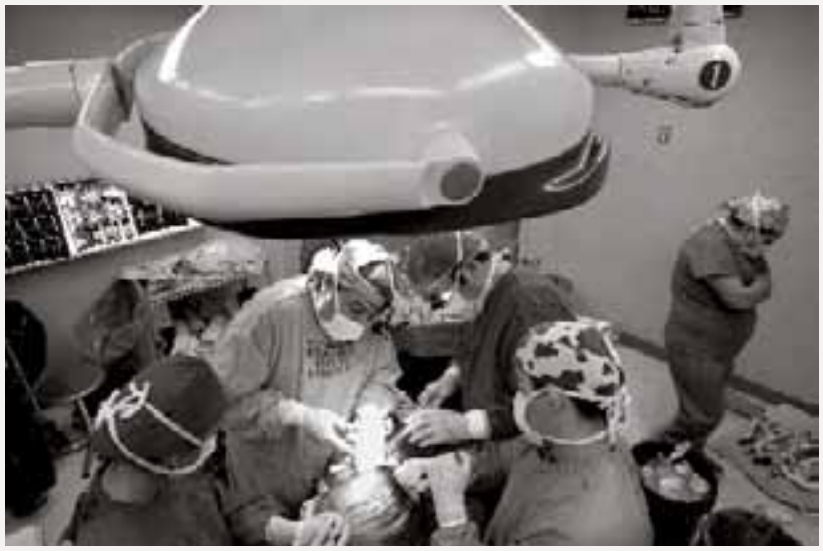
Menveo . *Bexsero,* B 25 000 1 12 .

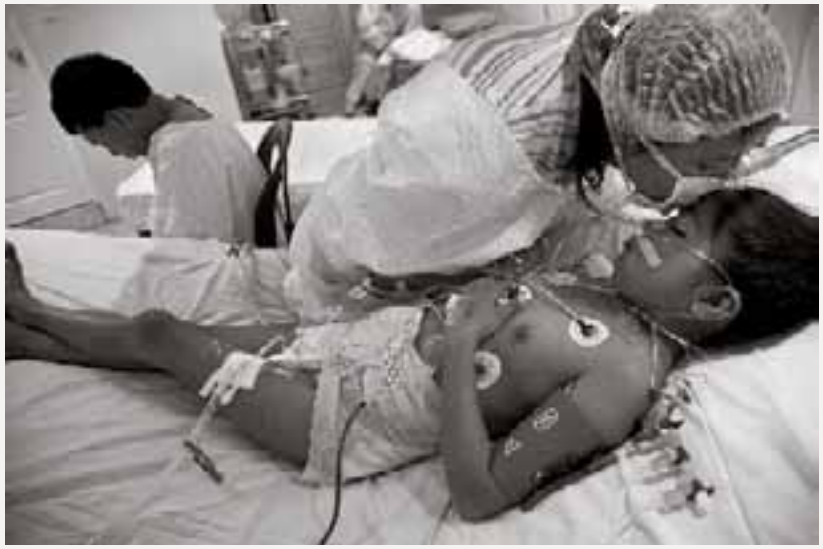
YOU HAVE BEEN A DRIVING FORCE BEHIND THE LAUNCH OF THE INTERNAL INITIATIVE BE HEALTHY. WHAT INSPIRED YOUR INITIATION OF THE PROGRAM DURING 2011?

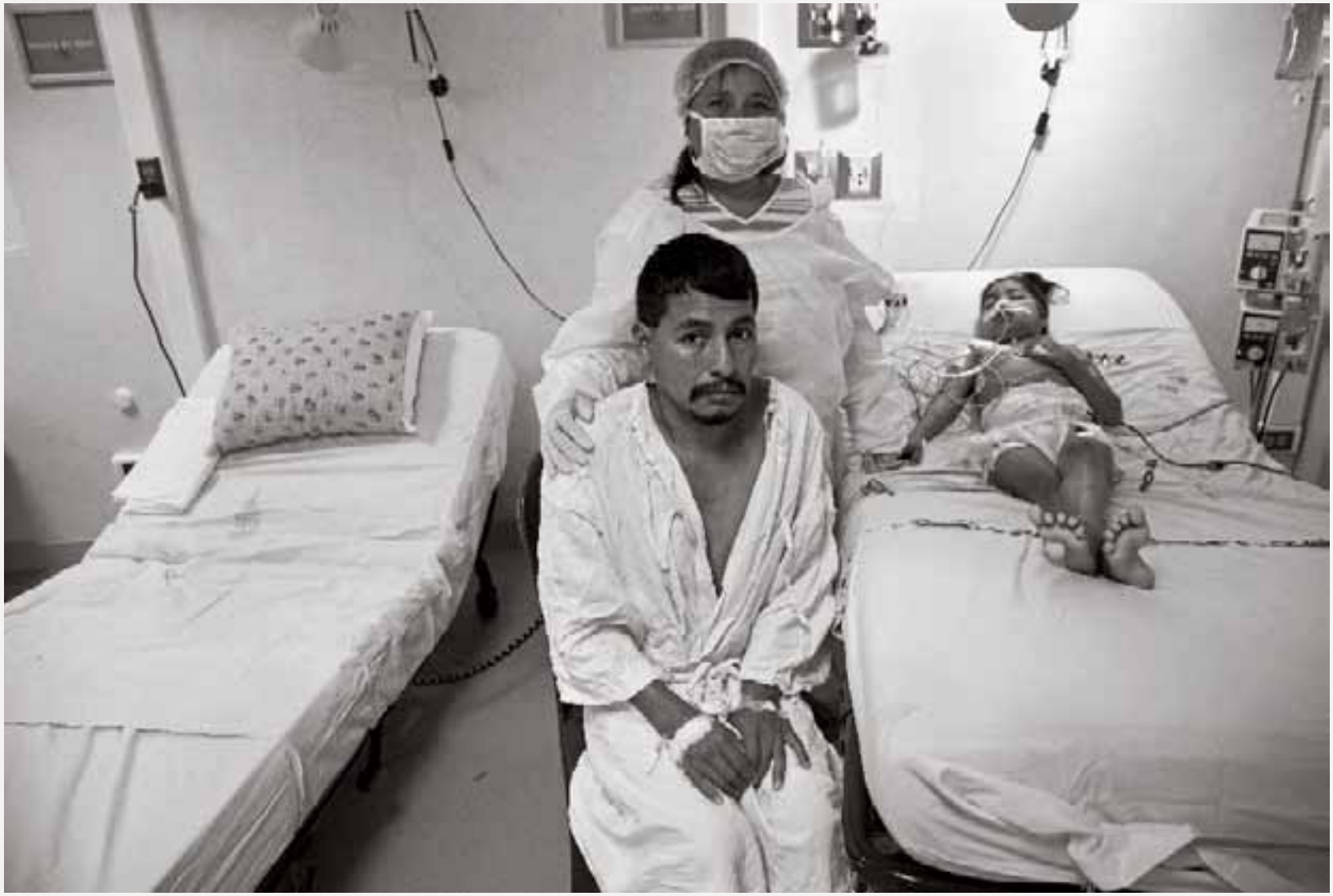
WHAT ADVANCES HAS NOVARTIS MADE IN ENHANCING ACCESS TO MEDICINE AND IN CORPORATE RESPONSIBILITY OVERALL?

JUAN MEJÍA MIRANDA:









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CONTENTS

HEALTHCARE PORTFOLIO OVERVIEW[1]

2011 NET SALES BY SEGMENT
(% and in USD millions)

Pharmaceuticals	56	32 508
Alcon	17	9 958
Sandoz	16	9 473
Vaccines and Diagnostics	3	1 996
Consumer Health	8	4 631
Total		**58 566**

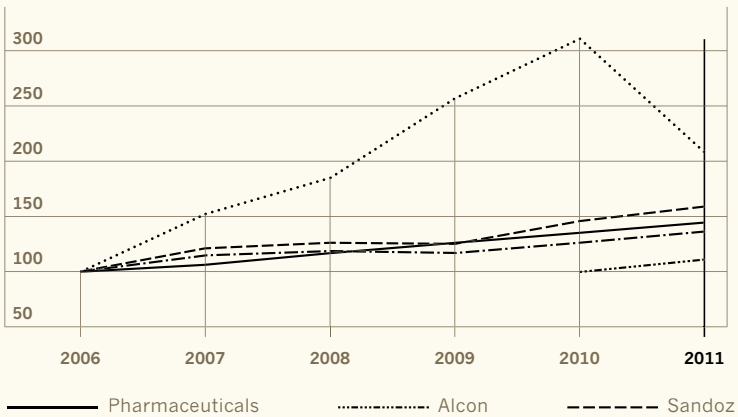
2011 CORE OPERATING INCOME[3] BY SEGMENT
(% and in USD millions)

Pharmaceuticals	61	10 040
Alcon	21	3 492
Sandoz	12	1 921
Vaccines and Diagnostics	1	135
Consumer Health	5	873
Corporate Expenses, net		– 552
Total		**15 909**

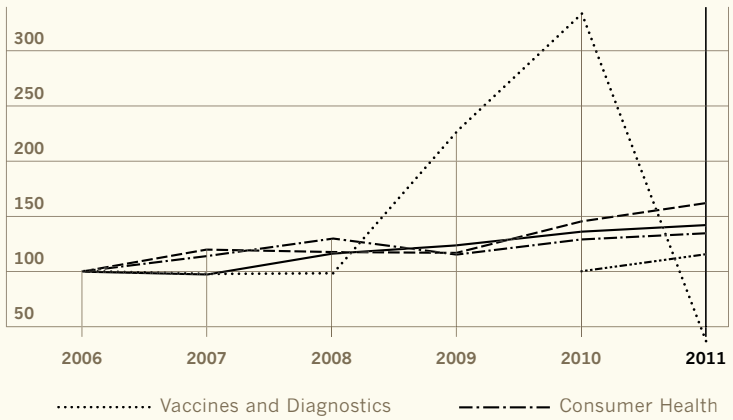
2011 NET SALES BY REGION AND SEGMENT
(% and in USD millions)

	Pharmaceuticals		Alcon		Sandoz		Vaccines and Diagnostics		Consumer Health	
United States	31	9 973	38	3 810	35	3 300	37	737	30	1 405
Europe	36	11 595	29	2 835	47	4 445	33	668	43	1 964
Asia/Africa/Australasia	24	7 928	22	2 207	11	1 064	19	373	17	782
Canada and Latin America	9	3 012	11	1 106	7	664	11	218	10	480
Total		**32 508**		**9 958**		**9 473**		**1 996**		**4 631**

NET SALES BY SEGMENT[2]
(Index: 2006 = 100%; Alcon only consolidated from August 25, 2010.
However, Alcon 2011 growth rate is based on pro forma full year data for 2010)



CORE OPERATING INCOME[3] BY SEGMENT[2]
(Index: 2006 = 100%; Alcon only consolidated from August 25, 2010.
However, Alcon 2011 growth rate is based on pro forma full year data for 2010)



[1] Data since 2009 has been restated to reflect new segment allocation introduced in 2011 as explained in detail on page 159.
[2] 2006-2011 for Consumer Health only includes OTC and Animal Health
[3] Core operating income eliminates the impact of acquisition-related factors and other significant exceptional items. These adjustments are explained in detail starting on page 179.

PHARMACEUTICALS OVERVIEW

KEY FIGURES

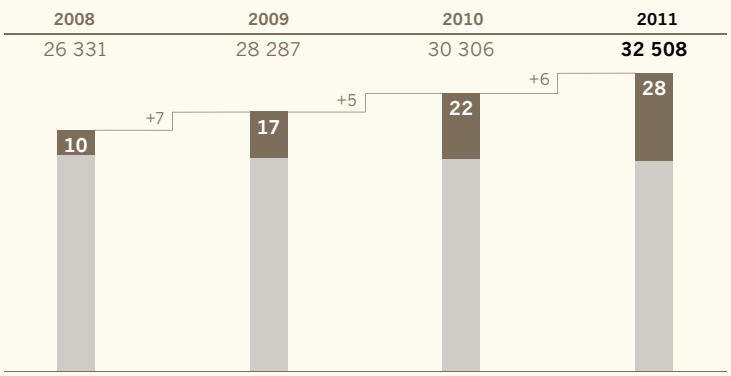
(in USD millions, unless indicated otherwise)

	2011	2010[1]
Net sales	**32 508**	30 306
Operating income	**8 296**	8 471
Return on net sales (%)	**25.5**	28.0
Core operating income[2]	**10 040**	9 586
Core return on net sales (%)	**30.9**	31.6
Core Research & Development[2]	**6 860**	6 344
As % of net sales	**21.1**	20.9
Free cash flow	**10 789**	10 355
Net operating assets	**13 696**	15 212
Additions to property, plant & equipment[3]	**1 041**	777
Number of associates (FTE)[4]	**60 527**	59 409

[1] Restated to reflect new segment allocation introduced during 2011 as explained in detail on page 159.
[2] Core operating income eliminates the impact of acquisition-related factors and other significant exceptional items. These adjustments are explained in detail starting on page 179.
[3] Excluding impact of business combinations
[4] Full-time equivalent positions at year end

PORTFOLIO REJUVENATION

([1] %)



[1] 2007 *Lucentis, Tasigna, Exjade, Sebivo/Tyzeka, Exforge, Galvus, Aclasta/Reclast, Cubicin, Exelon , Afinitor/Votubia, Tekturna/Rasilez, Extavia, Onbrez, Gilenya, Fanapt Ilaris*

NEWS IN 2011

. 7% (+4% ,) 32.5 . (11.6 , +2%), , , - . (3.2 , +7%) - C .? , A C ; , 31% .

2007 (9.2) 28% , 22% 2010. *Lucentis, Tasigna, Afinitor, Gilenya, Exforge, Galvus, Exelon , Exjade, Reclast/Aclasta Onbrez Breezhaler.*

2% (+4%) 8.3 , 1.7 (903 *Tekturna/Rasilez*). C 5% (+8%) 10.0 . C 1.4 . , 2.1 , 0.7 30.9 % .

, 130 , 15 2011. *Gilenya*, , , , . *Afinitor/Votubia* . *Lucentis* . , A *Tekturna/Rasilez*, C .

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TRANSLATIONAL MEDICINE

MASTER SWITCH

DRIVING TUMOR GROWTH

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Journal of Clinical Oncology

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C1 C2.
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B A . ,
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PIPELINE PROGRESS

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C424, , A 922
90 (90), -

PIPELINE

134 .

This table provides an overview of selected pharmaceutical projects in confirmatory development.

28.

Project /product	Common name	Mechanism of action
AC 885		A - -1
A B071		C
A 056		5
A 457		A - -17
A 355		A -A A
A 922		A - [4]90
BC 197		A -
B 235		3 / [5]
B 649		A
B 120		3
CA 106		B - -
B025		C
Exjade		
Gilenya		-1- (1)
C 122		A -C 40
C424		A)
B 589		
C 699		A
C 908		-1
C 696		A - (A)
225		/
571		B ( )
209		

1 ( )
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3
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5

Potential indication/indications	Therapeutic area	Route of administration	Planned submission dates[1]	Current phase[2]
? ( ), , ,	C , C C		,	
- (,),	C		≥2016	
( ), - ,			2013	
( ), , , ,	C ,	,	2013	
			≥2016	
			≥2016	
C	C		≥2016	
			2014	
	C C		≥2016	
			2014	
A ’		,	≥2016	
C C	C		2013	
-			,	
C			2014	
			≥2016	
( ),			,	
- - ( ),			2013	
			≥2016	
	C C		2014	
( ),	C C , C		2014	
B			2014	
C	C		≥2016	
	C C		≥2016	

PIPELINE (CONTINUED)

This table provides an overview of selected pharmaceutical projects in confirmatory development.

, 28.

Project /product	Common name	Mechanism of action
Lucentis		A - [6]
162		[8]
C002		
A237		-
C412		
A 039		A -
149	,	- -2
571		
A149	,	- -2 -
A 001 (*Afinitor*)		[5]
030		
230		
Tasigna		
258		1-3 [11] 1-3 [12], [13] [14]
Xolair		A -
Zortress/Certican		

6
7 C (C) ( ) -
,
8 C (A) -)
9 A
10
11
12
13 -
14

Potential indication/indications	Therapeutic area	Route of administration	Planned submission dates[1]	Current phase[2]
, [7]			2012	
			≥2016	
	C		≥2016	
C	C		, (B)	
A ( ),			2013	
A	C		≥2016	
A ,	C		2015	
	C C		2012	
C	C		2012	
A [9] (-), + 2- , 2- - , 2- - / , - ,			, (2012)	
A	C C		2013	
C ' ( ), ,		,	, (2012)	
- [10]			2014	
,			2013	
C	C C		2013	
	C		,	

PIPELINE GLOSSARY

Confirmatory development

(/ /)
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Project/product

( ),

Common name

Mechanism of action

,

Potential indication/indications

Route of administration

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Phase I

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Phase II

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Phase III

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Submission

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Reclast/Aclasta

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MUSCLE WASTING

(C),

/A

5%

50. B

5% 10%

60,

Annals of the New York Academy of Sciences, ?

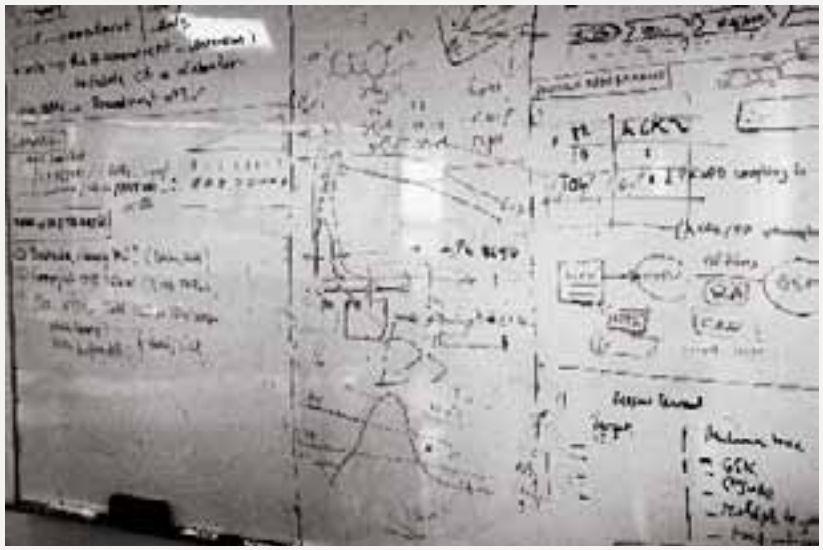
B

ACCELERATING RECOVERY

80 000

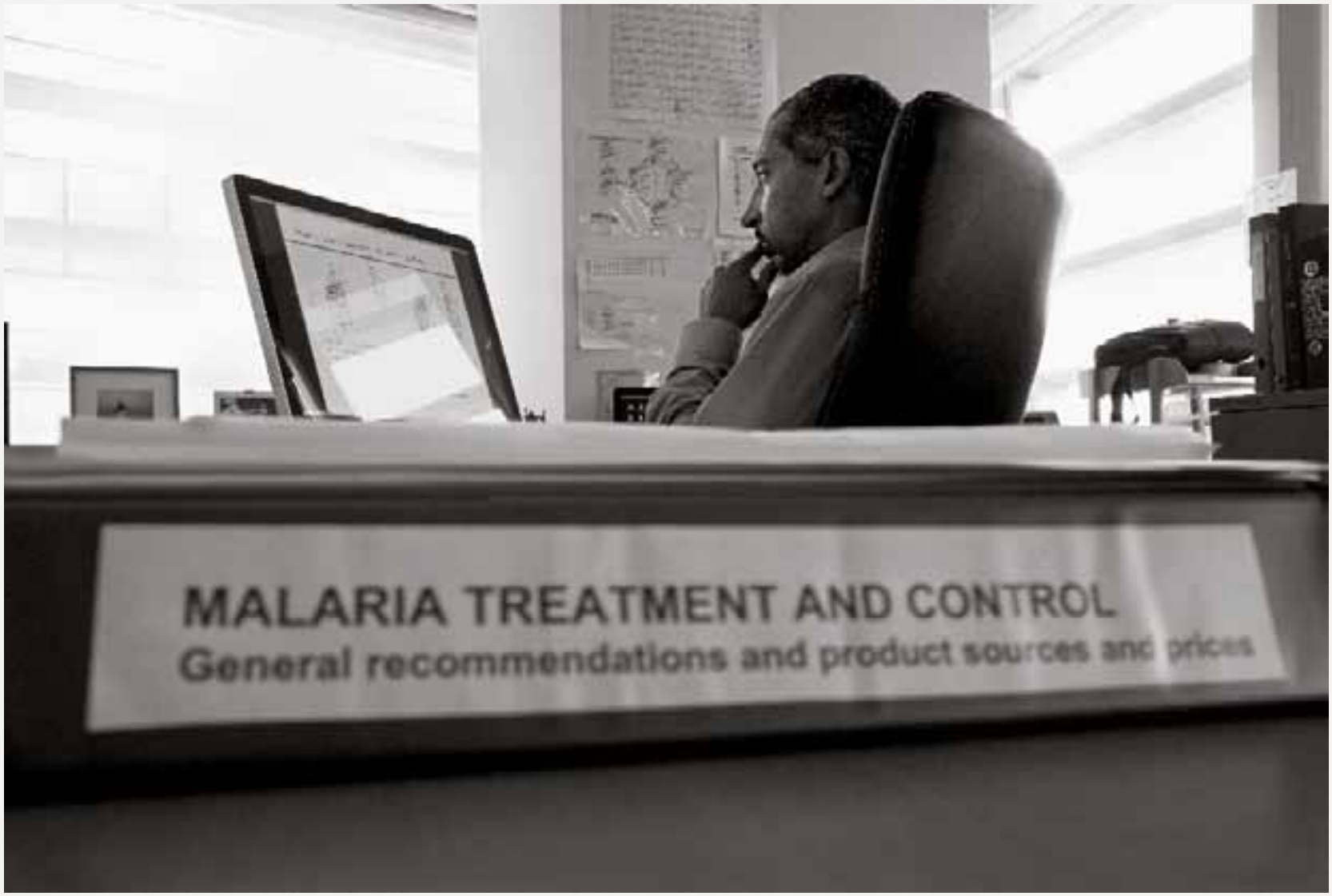
GENETIC SWITCH

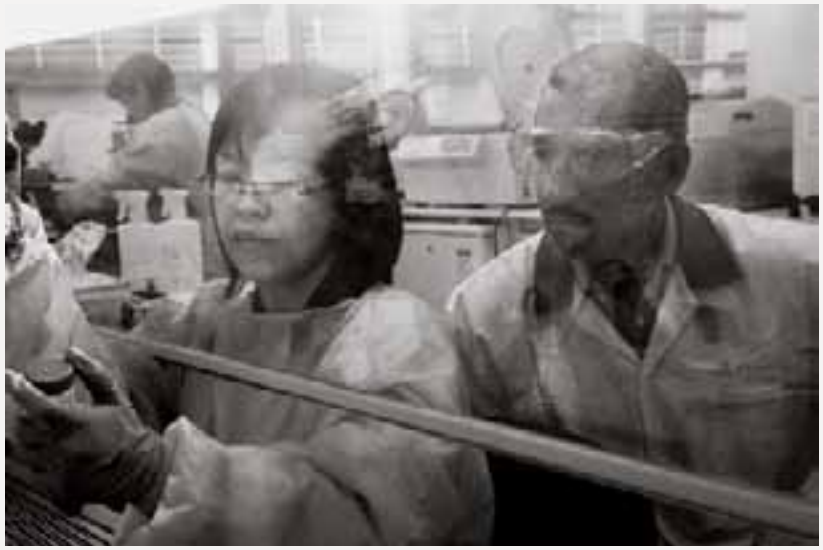
1990 .



DR. THIERRY DIAGANA:

fight against what we call neglected diseases. Here we have programs for


MALARIA TREATMENT AND CONTROL
General recommendations and product sources and prices



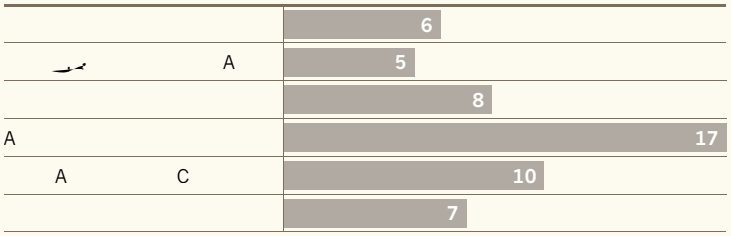
ALCON OVERVIEW

KEY FIGURES
(in USD millions, unless indicated otherwise)

	2011	2010[1]
Net sales	**9 958**	9 031
Operating income	**1 472**	1 181
Return on net sales (%)	**14.8**	13.1
Core operating income[2]	**3 492**	3 095
Core return on net sales (%)	**35.1**	34.3
Core Research & Development[2]	**869**	826
As a % of net sales	**8.7**	9.1
Free cash flow[3]	**3 498**	1 191
Net operating assets[3]	**43 792**	46 253
Additions to property, plant & equipment[3; 4]	**354**	193
Number of associates (FTE)[3; 5]	**22 987**	22 108

[1] 2010 on a full year pro forma basis as explained in detail on page 184, except where otherwise indicated.
[2] Core operating income eliminates the impact of acquisition-related factors and other significant exceptional items. These adjustments are explained in detail starting on page 179.
[3] 2010 on a restated basis as explained in detail on page 159.
[4] Excluding impact of business combinations
[5] Full-time equivalent positions at year end

NET SALES GROWTH BY REGION[1]
(%)



[1] 2011 % - 2010

NEWS IN 2011

A , C BA .
- , A
, .

10.0 10% (+7% ,) ,
(+10%) (+8%).
26% (+22%), C . -
(75).

1.5 24% (+14%) , 3.5
13% (+9%) . C 34.3% 35.1% .

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Azarga, *Travatan* *DuoTrav* . , , - , -
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C BA , A
. *Air Optix* . *Dailies Total 1,*
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26% (22%)

, A 10% .

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"WE FOCUS ON THE EYE..."

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PREVENTING BLINDNESS

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A ’ **NEW ERA IN CONTACT LENSES**

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2011.

Air Optix

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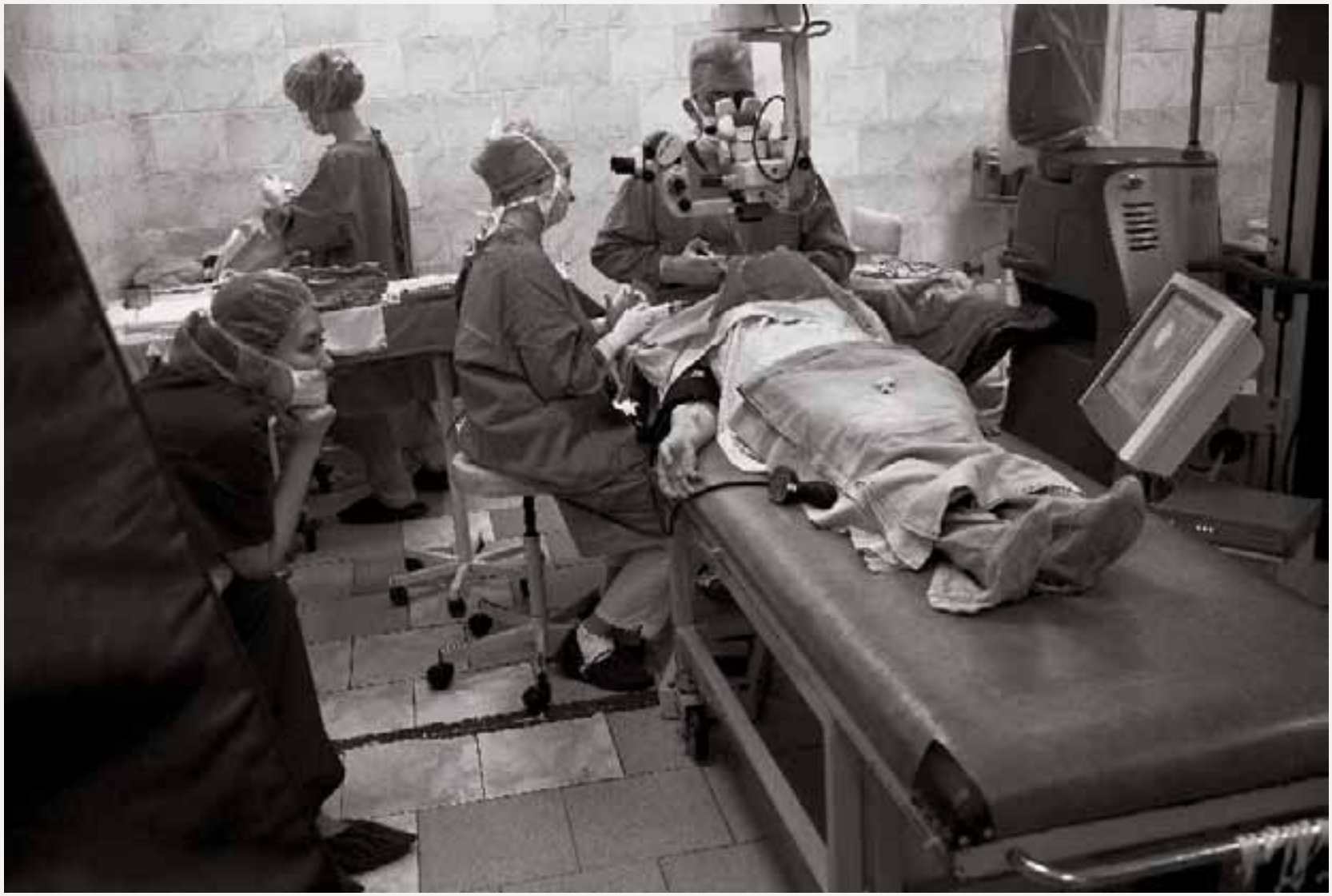
I was operated on first for the right eye. After the bandage was taken off, I looked out the window and saw such a nice green tree. Then I noticed that the doctor was so young. As for my husband, the two of us have been together from 1964, so the way he looks doesn't any longer make any difference to me.

DR. ALEXANDER IGOREVICH SAMOYLENKO:



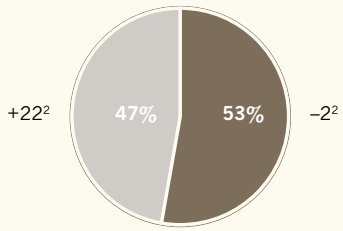
SANDOZ OVERVIEW

KEY FIGURES
(in USD millions, unless indicated otherwise)

	2011	2010[1]
Net sales	**9 473**	8 592
Operating income	**1 422**	1 321
Return on net sales (%)	**15.0**	15.4
Core operating income[2]	**1 921**	1 742
Core return on net sales (%)	**20.3**	20.3
Core Research & Development[2]	**724**	618
As a % of net sales	**7.6**	7.2
Free cash flow	**1 587**	2 141
Net operating assets	**15 223**	15 576
Additions to property, plant & equipment[3]	**335**	307
Number of associates (FTE)[4]	**24 377**	23 536

[1] Restated to reflect new segment allocation introduced during 2011 as explained in detail on page 159.
[2] Core operating income eliminates the impact of acquisition-related factors and other significant exceptional items. These adjustments are explained in detail starting on page 179.
[3] Excluding impact of business combinations
[4] Full-time equivalent positions at year end

2011 NET SALES [1] – DIFFERENTIATED VS. COMMODITIZED GENERICS
(in %)



Differentiated Products[3] Commoditized Products

[1] Net sales percentage based on retail generics and biosimilar sales
[2] 2011 Sandoz third party net sales growth in constant currencies versus 2010
[3] Differentiated products refer to products requiring specialized knowledge and expertise in development, production and/or commercialization, characterized by the active ingredient, formulation/delivery mechanism and/or underlying technology. Examples include complex oral solids, transdermal patches, implants, ophthalmics, inhalables, injectables and biosimilars

NEWS IN 2011

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ABBREVIATED CLINICAL TRIALS

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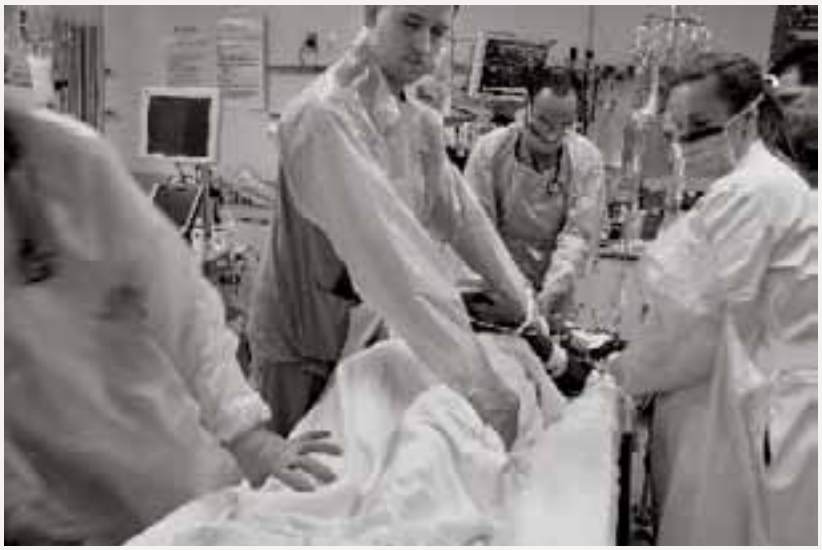

DR. OMAR BHOLAT:


HOSPITAL & EMERGENCY ROOM

VACCINES AND DIAGNOSTICS OVERVIEW

KEY FIGURES

(in USD millions, unless indicated otherwise)

	2011	2010
Net sales	**1 996**	2 918
Operating loss / income	**– 249**	612
Return on net sales (%)	**– 12.5**	21.0
Core operating income [1]	**135**	1 066
Core return on net sales (%)	**6.8**	36.5
Core Research & Development [1]	**494**	506
As a % of net sales	**24.7**	17.3
Free cash flow	**– 292**	1 336
Net operating assets	**5 067**	4 804
Additions to property, plant & equipment [2]	**192**	159
Number of associates (FTE) [3]	**6 122**	5 394

[1] Core operating income eliminates the impact of acquisition-related factors and other significant exceptional items. These adjustments are explained in detail starting on page 179.
[2] Excluding impact of business combinations
[3] Full-time equivalent positions at year end

VACCINES LATE-STAGE DEVELOPMENT PIPELINE

	Phase I	Phase II	Phase III	Registration
Menveo 2-10 [1]				
Menveo infant [1]				
Bexsero [2]				
Fluad pediatric				
Optaflu [3]				
Agriflu pediatric				
MenABCWY [4]				
Pseudomonas aeruginosa [5]				
GBS [6]				
FCC [3] H5N1				

[1] *Neisseria meningitidis* bacteria serogroups A, C, W-135 and Y
[2] *Neisseria meningitidis* bacteria serogroup B
[3] Influenza cell culture
[4] *Neisseria meningitidis* bacteria serogroups A, B, C, W-135 and Y
[5] Collaboration with Intercell
[6] Group B Streptococcus

NEWS IN 2011

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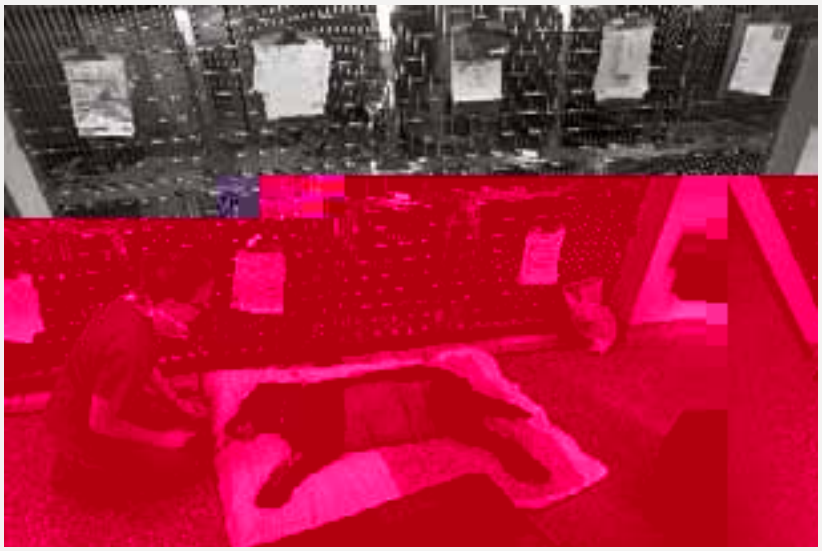
DR. MARK PROCTOR:



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FROM ANTIBIOTICS TO VACCINES

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MONITORING SEA LICE

NEW MARKETS

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CONTENTS

Indicator	2011	2010	2009	2008	2007
Economic[1]					
Net sales in USD billions	**58.6**	50.6	44.3	41.5	38.1
Net income in USD billions; % of net sales	**9.2; 16%**	10; 20%	8.5; 19%	8.2; 20%	6.5; 17%
Core Research & Development in USD billions; % of net sales	**9.2; 16%**	8.1; 16%	7.3; 16%	6.8; 16%	6.2; 16%
Purchased goods and services[2] in USD billions; % of net sales	**26.8; 46%**	22.3; 44%	21.3; 48%	20.3; 49%	19.4; 51%
Personnel costs in USD billions; % of net sales	**14.9; 26%**	12.2; 24%	10.9; 25%	10.6; 26%	9.9; 26%
Taxes in USD billions; % of net income before taxes	**1.5; 14%**	1.7; 15%	1.5; 15%	1.3; 14%	0.9; 13%
Dividends in USD billions; % of net income attributable to Novartis shareholders[3]	**5.8; 63%**	5.4; 55%	4.5; 53%	3.9; 49%	3.3; 51%
Cash returned to shareholders via second-line share repurchases in USD billions; % of Group total net income	**2.4; 26%**	0; 0%	0; 0%	0.3; 0%	4.7; 39%
Share price at year-end (CHF)	**53.70**	54.95	56.50	52.7	62.1
Patients[4]					
Access to medicine: value in USD millions	**1 784**	1 544	1510	1259	937
Access to medicine: number of patients reached in millions	**89.6**	85.5	79.5	73.7	65.7
People and Communities					
Full-time equivalent positions	**123 686**	119 418	99 834	96 717	98 200
Resignations (incl. retirements); separations; hiring (% of associates)	**8; 4; 15**	8; 3; 14	8; 3; 14	10; 5; 14	9; 4; 17
Women in management[5]: % of management; % of Board of Directors	**36%; 18.2%**	36%; 16.7%	35%; 16.7%	37%; 8.3%	35%; 8.3%
Number of associate nationalities	**153**	149	144	143	139
Lost-time injury and illness rate (per 200 000 hours worked)[1,6,7]	**0.15**	0.18	0.22	0.34	0.42
Total recordable case rate (per 200 000 hours worked)[1,6,7,8]	**0.54**	0.73	0.93	1.09	1.42
Transportation-related injuries leading to lost time[1,6,7]	**26**	49	58	77	92
Environment[1,7,9]					
Contact water use, excluding cooling water (million m^3)	**16.0**	15.1	15.0	15.1	15.4
Energy use (million GJ), on site and purchased	**17.4**	17.6	17.0	16.9	16.8
GHG emissions, Scope 1 vehicles (1000 t)	**155**	168	176	183	197
GHG emissions, total Scope 1, including vehicles, and Scope 2 (1000 t)	**1 459**	1 507	1 510	1 526	1 498
Total operational waste not recycled (1000 t), hazardous and non-hazardous	**142**	154	141	138	175
Ethical Business Conduct					
Novartis associates trained on Code of Conduct via e-learning course[10]	**14 419**	18 302	29 493	15 990	16 697
Associates completing certification on Code of Conduct	**33 080**	29 835	26 300	26 750	27 000
Cases of misconduct reported; substantiated[11]	**1 522; 825**	1 236; 743	913; 541	884; 374	906; 421
Dismissals and resignations related to misconduct[11]	**384**	608	564	217	249
Total number of suppliers	**225 500**	241 365	206 155	228 769	228 558
Suppliers informed of Novartis Third-Party Guidelines (annual sales of more than USD 100 000 and not requiring a self-declaration)	**45 203**	39 575	45 858	28 792	61 715
Suppliers to confirm key standards (self-declaration)	**3 926**	3 388	842	1 157	1 377

[1] Data for 2007 have been adjusted to exclude Consumer Health Nutrition operations divested in 2007, unless otherwise stated

[2] As included in the Net Novartis Added Value Statement

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SUPPLY CHAIN MANAGEMENT

UPGRADING INFORMATION

NOVARTIS ACCESS-TO-MEDICINE PROJECTS 2011

Project	Description	Target region	Value (USD millions)	Patients
Malaria [1]	Provide *Coartem* without profit for public sector use	Africa, Asia, Latin America	269	84 470 000
Leprosy/WHO [2,3]	Eliminate leprosy by providing free medications to all patients worldwide with WHO	Global	6	318 000
Tuberculosis [2,3]	Donate fixed-dose combinations	Tanzania	2	121 000
Fascioliasis [4]	Provide *Egaten* free of charge to treat patients infected with fascioliasis	Bolivia, Egypt, Iran, Madagascar, Switzerland, Vietnam, Yemen	0.1	170 000
Novartis Foundation for Sustainable Development (NFSD) [5,6]	Improve health and quality of life of poor people in developing countries through think tank, policy and project work	Developing countries	10	3 713 000
Novartis Institute for Tropical Diseases (NITD) [5]	Discover novel treatments and prevention methods for major tropical diseases; NITD discoveries to be available in poor endemic countries without profit	Developing countries	15	-
Novartis Vaccines Institute for Global Health (NVGH) [5]	Develop effective and affordable vaccines for neglected infectious diseases of developing countries	Developing countries	10	-
US patient assistance program (PAP) [2] (excl. *Gleevec*)	Assist patients experiencing financial hardship, without third-party insurance coverage for their medicines	United States	269	103 000
Gleevec US PAP [2,7]	Within capability of Novartis, continue to ensure access for patients in the US who cannot afford the drug	United States	144	4 000
Glivec Global PAP/ *Tasigna* Global PAP [2,7,8]	Within capability of Novartis, continue to ensure access for patients outside the US who cannot afford the drug	Global (excluding US)	933	47 000
Alcon medical missions [9]	Provide traveling medical teams with Alcon products	Developing countries	49	705 000
Alcon US patient assistance [9] (all programs)	Assist patients experiencing financial hardship by providing Alcon products	United States	17	19 000
Emergency relief and other donations	Support humanitarian organizations	Global	59	-
Total			**1 784**	**89.6 million**

[1] During 2011, 84.5 million *Coartem* treatments reached patients based on a preliminary analysis of local distribution. Of these, 43.9 million treatments came from shipments completed in 2010, and 40.6 million from shipments in 2011. A total of 100.1 million treatments were shipped in 2011. Value was calculated using the number of treatments shipped in 2011 and the ex-factory price of *Coartem* to private-sector purchasers in malaria-endemic developing countries, excluding private-sector buyers using the Affordable Medicines Facility for malaria, minus payments to Novartis to cover costs under terms of the public-private partnership with the WHO, which formally ended in May 2011. These payments were received through the WHO, UNICEF and other procurement agencies, acting on behalf of governments and other public sector institutions in developing countries eligible to receive *Coartem* at the not-for-profit price.

[2] Ex-factory price to private market

[3] Value and patients are based on WHO estimates

[4] Manufacturing costs

[5] Novartis operating costs

[6] Patients number indicates beneficiaries of projects supported by NFSD and partners; beneficiaries include patients, healthcare professionals and members of health insurance schemes.

[7] US donations of *Tasigna* are included in US patient assistance program

[8] Value and patients include donations under shared contribution and co-pay models

[9] Full US retail value

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QUALITY EYE CARE FOR PATIENTS IN NEED

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CORPORATE CITIZENSHIP: KEY TARGETS AND RESULTS FOR 2011 AND KEY TARGETS FOR 2012

ACCESS TO MEDICINE

Targets 2011	Results 2011	Targets 2012
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NOVARTIS INSTITUTE FOR TROPICAL DISEASES

Targets 2011	Results 2011	Targets 2012
- - 609. . B .	609 , C 2012 - A 156. 2012. *P. vivax* .	609 (C) A 156.

NOVARTIS VACCINES INSTITUTE FOR GLOBAL HEALTH

Targets 2011	Results 2011	Targets 2012
-C 197 *Paratyphi* A *Shigella* .	A - *Paratyphi* A	-C 197. - ( )-3( )-21( )-48 2011 6.762 -4( )10( )461.2 (( )1(( )-1

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ROOM FOR IMPROVEMENT

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MONITORING OUTCOMES

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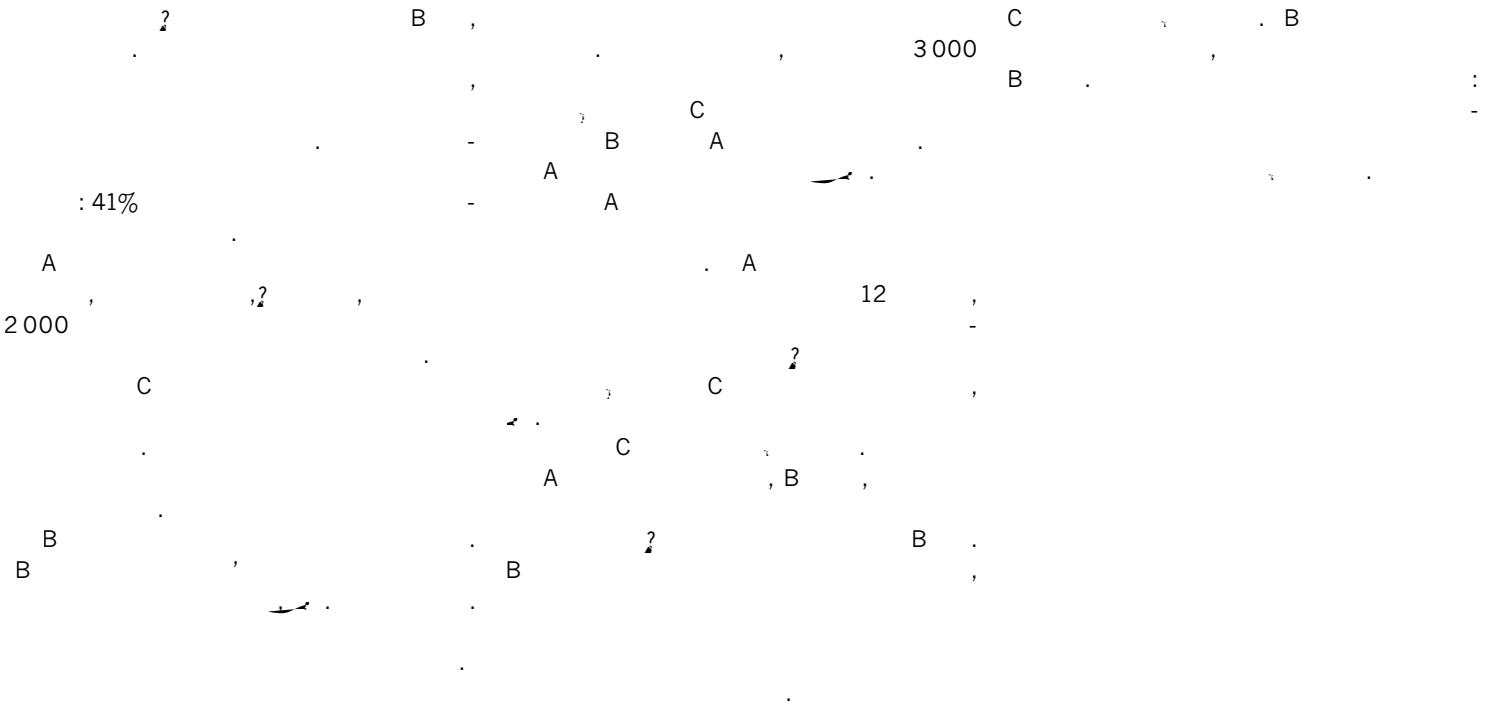
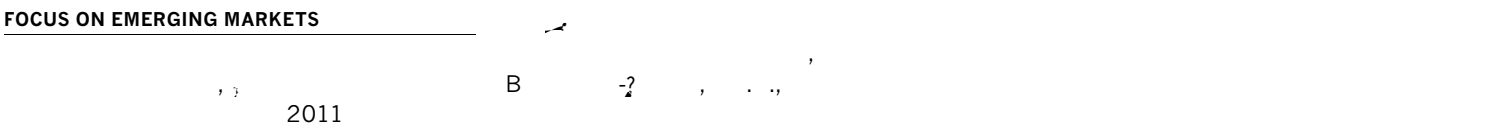


FOCUS ON EMERGING MARKETS



ASSOCIATES BY REGION AND SEGMENT AS OF DECEMBER 31[1]

	United States		Canada and Latin America		Europe		Asia/Africa/ Australasia		Total	
	2011	2010	**2011**	2010	**2011**	2010	**2011**	2010	**2011**	2010
Pharmaceuticals	12 869	13 704	4 557	4 390	26 338	26 275	16 763	15 040	60 527	59 409
Alcon	9 347	9 175	1 794	2 033	7 410	6 704	4 436	4 196	22 987	22 108
Sandoz	1 442	1 349	2 532	2 427	15 595	15 308	4 808	4 452	24 377	23 536
Vaccines and Diagnostics	1 530	1 394	114	83	3 676	3 604	802	313	6 122	5 394
Consumer Health	1 797	1 731	890	737	3 567	3 432	2 036	1 828	8 290	7 728
Shared services	124	117	25	23	281	268	52	50	482	458
Corporate	133	117	25	21	686	599	57	48	901	785
Total	**27 242**	**27 587**	**9 937**	**9 714**	**57 553**	**56 190**	**28 954**	**25 927**	**123 686**	**119 418**

[1] Full-time equivalent positions. 2010 segments restated to reflect the new segment allocation introduced during 2011 as explained in detail on page 159.

SHIWAGA HAGOS:

Plasmodium vivax *Plasmodium falciparum*

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NOVARTIS HEALTH, SAFETY AND ENVIRONMENT (HSE) DATA 2011

	Novartis Group[1]		Pharmaceuticals		NIBR		Sandoz		Vaccines and Diagnostics		Consumer Health[2]		Alcon[3]
	2011	2010	2011	2010	2011	2010	2011	2010	2011	2010	2011	2010	2011
HSE personnel	**442**	435	**208**	195	**26**	22	**124**	129	**26**	28	**47**	50	**39**
Lost-time injury and illness rate (LTIR)	**0.15**	0.18	**0.13**	0.20	**0.09**	0.16	**0.18**	0.19	**0.17**	0.17	**0.17**	0.13	**0.45**
Total recordable case rate	**0.54**	0.73	**0.53**	0.81	**0.57**	0.68	**0.52**	0.64	**0.48**	0.43	**0.44**	0.74	**1.04**
Total production (1000 t)	**174**	168	**25**	25	**0**	0	**86**	87	**0.3**	0.4	**63**	56	**45**
Contact water use (million m^3)	**16.0**	15.1	**4.1**	4.1	**0.6**	0.6	**8.7**	7.8	**1.0**	1.0	**1.6**	1.6	**1.6**
Energy use (million GJ)	**17.4**	17.6	**5.5**	5.6	**1.3**	1.3	**7.6**	7.7	**1.5**	1.4	**1.5**	1.5	**2.0**
Emissions													
Effluent discharge (million m^3)	**16.9**	15.9	**4.1**	4.3	**0.6**	0.6	**8.6**	7.8	**1.1**	1.0	**2.5**	2.2	**1.4**
COD into water (1000 t)	**3.9**	3.6	**0.7**	0.8	**0.0**	0.0	**3.1**	2.8	**0.0**	0.0	**0.1**	0.1	**0.0**
Sulfur dioxide SO_2 (t)	**76**	82	**4.4**	7.3	**0.5**	0.5	**69**	72	**0.1**	0.1	**0.5**	1.5	**0.7**
Nitrogen oxide NO_2 (t)	**288**	313	**103**	113	**10**	12	**140**	141	**11**	24	**23**	22	**38**
Halogenated VOCs (t)	**136**	244	**1.6**	2.1	**6.8**	6.9	**128**	235	**0.0**	0.0	**0.0**	0.0	**0.0**
Non-halogenated VOCs (t)	**1 050**	1 277	**217**	247	**25**	26	**722**	925	**1.2**	1.9	**84**	78	**21**
GHG Scope 1, combustion and process (1000 t)	**414**	418	**139**	143	**17**	18	**189**	190	**37**	38	**32**	28	**49**
GHG Scope 1, vehicles (1000 t)	**155**	168	**103**	120	**0.1**	0.2	**27**	25	**4.5**	4.6	**14**	13	**41**
GHG Scope 2, purchased energy (1000 t)	**890**	922	**224**	235	**81**	84	**354**	381	**91**	81	**139**	140	**165**
Operational waste													
Non-hazardous waste not recycled (1000 t)	**47**	58	**7.4**	7.1	**1.6**	1.8	**9.3**	7.9	**23**	35	**6.5**	6.1	**3.4**
Hazardous waste not recycled (1000 t)	**95**	96	**64**	65	**1.2**	1.4	**25**	26	**1.3**	1.2	**2.4**	2.7	**0.7**
Non-hazardous waste recycled (1000 t)	**39**	36	**11**	11	**1.4**	1.3	**16**	15	**1.9**	2.2	**8.2**	7.0	**6.7**
Hazardous waste recycled (1000 t)	**90**	89	**20**	38	**0.0**	0.0	**67**	51	**0.1**	0.2	**2.5**	0.2	**0.0**

[1] Novartis Group includes Novartis Corporate; Alcon is not included.
[2] Consumer Health data include Animal Health, CIBA Vision and OTC.
[3] Data from newly acquired Alcon sites, excluding CIBA Vision; Alcon data only available for 2011.

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FURTHER INFORMATION

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To the Audit and Compliance Committee of the Board of Directors of Novartis AG, Basel

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CORPORATE GOVERNANCE REPORT

Novartis strives to create sustainable value. Our corporate governance framework is designed to support this. While it complies with all applicable laws and implements best corporate governance standards, it is tailor-made for Novartis.

CONTENTS

INTRODUCTION

The corporate governance framework of Novartis reflects a system of checks and balances between the powers of the shareholders, the Board of Directors and the management with the goal to safeguard the interests of Novartis and its shareholders while creating sustainable value.

Since the creation of Novartis in 1996, the Board of Directors has continuously improved the corporate governance framework of Novartis by proactively implementing emerging best corporate governance standards long before these were embedded in the Swiss Code of Best Practice for Corporate Governance ("the Swiss Code") or in the law.

In 1999, Novartis established the new position of Lead Director as a check and balance following the election of Chief Executive Officer Daniel Vasella, M.D., to the additional post of Chairman. Moreover, three new Board committees – the Compensation Committee, the Audit and Compliance Committee and the Corporate Governance and Nomination Committee – were created, composed exclusively of independent Board members.

In 2002, five years before legislation came into force in 2007, requiring companies to disclose the total compensation of their executive management group as well as the highest compensation attributed to a member of the executive management, Novartis had already implemented even more rigorous disclosure standards by reporting the individual annual compensation of all members of the Executive Committee.

In 2004, two years earlier than required for non-US corporations, Novartis complied with the challenging certification requirements under the US Sarbanes-Oxley Act, in particular Section 404 of this Act.

In 2009, the Board of Directors established a new Risk Committee that oversees the Group's enterprise risk management, strengthening the Board of Directors' supervisory function over management in this critical area. While fostering a culture of risk-adjusted decision making, the Risk Committee ensures that reasonable risk-taking and innovation are not constrained.

In 2010, the Chairman and CEO functions were separated. In addition several emerging best corporate governance standards were proactively implemented, including the introduction of a "say-on-pay" shareholder vote, making changes to our executive compensation system to further strengthen the alignment of incentives with the long-term success of Novartis and a number of new disclosures, including on qualifications of Board members.

In 2011, the first "say-on-pay" vote was held, where the shareholders endorsed the compensation system of Novartis.

Novartis evaluates emerging best governance standards and adopts those that are found to be appropriate for Novartis. These standards are then tailored to Novartis, its business, management, stakeholders and shareholders with a view to create a corporate governance regime that supports the creation of sustainable value. This cannot be achieved by implementing corporate governance standards "as is" ("one size fits all approach") and becomes impossible if corporate governance standards (embedded in corporate governance codes) are converted into binding, "one size fits all" rules as is currently contemplated in Switzerland.

In Switzerland, Parliament considers introducing binding, "one size fits all" rules such as a binding shareholder vote on executive compensation and a ban on sign-on bonuses. Such rules would eliminate the flexibility of issuers to adapt corporate governance recommendations to the specific circumstances and needs of each individual company. Moreover, if such rules were introduced, Switzerland would get a corporate governance regime that would be substantially more restrictive than that of other countries. Such binding corporate governance rules are not needed. The "market" (corporate governance rating agencies, proxy voting agencies, institutional investors, Stock Exchanges) already plays a very effective role in deciding whether a given explanation is sufficient and plausible or not.

We note however an encouraging development in that regulators start to acknowledge and seem to become willing to regulate many corporate governance issues that have been highlighted by issuers for a long time but did not make it "on the corporate governance agenda" yet: In 2010, the US Securities Exchange Commission in its "Concept Release on the U.S. Proxy System" and, in 2011, the European Commission in its green paper entitled "The EU Corporate Governance Framework" have noted a number of such issues, including deficiencies in the proxy system, potential conflicts of interest and a lack of accuracy and transparency of proxy advisory firms, and what the European Commission called "inappropriate short-termism among investors." On that last point, we note that the UK government commissioned a review (*"The Kay Review"*) on whether the time horizons of investors match those of their principals and whether equity markets and government policies promote long-term horizons of institutional shareholders and fund managers and sufficiently encourage boards to have a long-term horizon.

At the heart of good corporate governance lies a strong Board of Directors, which represents the interests of the shareholders and other stakeholders, and the professionalism and integrity of management, creating the foundation for sustainable value. While the size, composition and structure of the Board of Directors are easy to describe and can be easily checked from the outside, it is difficult to demonstrate that the core processes, like information flow and decision making, are state-of-the-art. It is even more difficult, if not impossible, to describe the prevailing board culture, although the latter is essential for its effective function. Novartis aims to foster an atmosphere in which Board members can pose challenging

questions, voice dissenting views and secure access to independent information through extensive contacts with senior Novartis executives – inside and outside the boardroom. Diversity of a Board of Directors is a critical success factor for its work. The Novartis Board of Directors today is diverse in terms of background, interests and skills.

OUR CORPORATE GOVERNANCE FRAMEWORK

LAWS AND REGULATIONS

Novartis is subject to the laws of Switzerland, in particular Swiss company and securities laws, and to the securities laws of the United States as applicable to foreign private issuers of securities.

In addition, Novartis is subject to the rules of the Swiss Stock Exchange (SIX Swiss Exchange), including the Directive on Information relating to Corporate Governance.

Novartis is also subject to the rules of the New York Stock Exchange (NYSE) as applicable to foreign private issuers of securities. The NYSE requires Novartis to describe any material ways in which its corporate governance differs from that of domestic US companies listed on the NYSE. Different from corporate governance rules applicable to domestic US companies listed on NYSE, shareholders of Novartis do not receive written reports from committees of the Board of Directors. Also, the external auditors are appointed by our shareholders at the Annual General Meeting, as opposed to being appointed by the Audit and Compliance Committee. In addition, while our shareholders cannot vote on all equity-compensation plans, they are entitled to hold a consultative vote on the compensation system of Novartis. The vote takes place before every significant change to the compensation system, but at least every third Annual General Meeting. Finally, our Board of Directors has set up a separate Risk Committee that is responsible for risk oversight, as opposed to delegating this responsibility to the Audit and Compliance Committee.

SWISS CODE OF BEST PRACTICE FOR CORPORATE GOVERNANCE

Novartis applies the Swiss Code of Best Practice for Corporate Governance.

NOVARTIS CORPORATE GOVERNANCE STANDARDS

Novartis has incorporated the corporate governance standards described above into the Articles of Incorporation and the Regulations of the Board of Directors, its Committees and the Executive Committee (www.novartis.com/corporate-governance).

The Corporate Governance and Nomination Committee regularly reviews these standards and principles in the light of prevailing best practices and makes recommendations for improvements of the corporate governance framework of Novartis for consideration by the full Board of Directors.

Additional corporate governance information can be found on the Novartis website: http://www.novartis.com/corporate-governance

Printed copies of the Novartis Articles of Incorporation, Regulations of the Board and Charters of Board Committees can be obtained by writing to: Novartis AG, Attn: Corporate Secretary, Lichtstrasse 35, CH-4056 Basel, Switzerland.

OUR SHAREHOLDERS

SHARES

SHARE CAPITAL OF NOVARTIS AG

The share capital of Novartis AG is CHF 1 372 811 500, fully paid-in and divided into CHF 2 745 623 000 registered shares, each with a nominal value of CHF 0.50.

Novartis has neither authorized nor conditional capital. There are no preferential voting shares; all shares have equal voting rights. No participation certificates, non-voting equity securities (Genussscheine) or profit-sharing certificates have been issued.

Novartis shares are listed and traded on the SIX Swiss Exchange (Valor No. 001200526, ISIN CH0012005267, symbol: NOVN) as well as on the NYSE in the form of American Depositary Receipts (ADRs) representing Novartis American Depositary Shares (ADSs) (Valor No. 567514, ISIN US66987V1098, symbol: NVS).

The holder of an ADS has the rights enumerated in the Deposit Agreement (such as the right to vote and to receive a dividend). The ADS depositary of Novartis, JPMorgan Chase Bank, New York, holding the Novartis shares underlying the ADSs, is registered as shareholder in the share register of Novartis. An ADS is not a Novartis share and an ADS holder is not a Novartis shareholder. ADS holders exercise their voting rights by instructing the depositary to exercise their voting rights. Each ADS represents one Novartis share.

SHARE REPURCHASE PROGRAMS

Novartis began repurchasing its shares in 1999. Since then, five share repurchase programs have been completed with the repurchase of shares worth CHF 19 billion. Shares repurchased under the first program were not cancelled. However, shares repurchased under the other four programs were cancelled. At the Annual General Meeting in February 2008, shareholders authorized the Board of Directors to launch a sixth program to repurchase shares up to a maximum amount of CHF 10 billion via a second trading line on the SIX Swiss Exchange. In 2008, a total of six million shares were repurchased at an average price of CHF 49.42 per share and cancelled. The share repurchase program was suspended in April 2008 in favor of debt repayment. In December 2010, the Board of Direc-

tors announced the reactivation of the share repurchase program to minimize dilution to existing Novartis shareholders in connection with the proposed merger of Alcon, Inc. into Novartis. In 2010, no shares were repurchased under the share repurchase program. In 2011, 39 430 000 shares were repurchased under the share repurchase program.

CHANGES IN SHARE CAPITAL

During the last three years there were the following changes to the share capital of Novartis:

Novartis increased its share capital once: On 8 April 2011 for the purpose of completing the merger of Alcon, Inc. into Novartis AG, the share capital was increased by CHF 54 million, from CHF 1 318 811 500 to CHF 1 372 811 500, through the issuance of 108 000 000 fully paid-in registered shares with a nominal value of CHF 0.50 each.

As part of a share repurchase program, Novartis reduced its share capital once: In 2009 the share capital was reduced by CHF 3 million, from CHF 1 321 811 500 to CHF 1 318 811 500.

CAPITAL CHANGES

	Number of shares			
Year	As of Jan 1	Shares	As of Dec 31	Amount of capital changed in CHF
2009	2 643 623 000	– 6 000 000	2 637 623 000	– 3 000 000
2010	2 637 623 000	0	2 637 623 000	0
2011	2 637 623 000	108 000 000	2 745 623 000[1]	54 000 000

[1] Capital increase as set-out above

A table with additional information on changes in the Novartis share capital can be found in Note 6 to the Financial Statements of Novartis AG.

CONVERTIBLE OR EXCHANGEABLE SECURITIES

Novartis has not issued convertible or exchangeable bonds, warrants, options or other securities granting rights to Novartis shares, other than options granted to associates as an element of compensation.

SHAREHOLDINGS

SIGNIFICANT SHAREHOLDERS

According to the share register, as of December 31, 2011, the following registered shareholders (including nominees and the ADS depositary) held more than 2% of the total share capital of Novartis with the right to vote these shares:[1]

- Shareholders: Novartis Foundation for Employee Participation, with its registered office in Basel, Switzerland, holding 4.1%, and Emasan AG, with its registered office in Basel, Switzerland, holding 3.2%;
- Nominees: JPMorgan Chase Bank, New York, holding 10.9%, Nortrust Nominees, London, holding 3.2%, and Mellon Bank, Everett, Massachusetts, holding 3%; and
- ADS depositary: JPMorgan Chase Bank, New York, holding 11%.

[1] Excluding 5.76% of the share capital held by Novartis AG, together with Novartis affiliates, as treasury shares.

According to a disclosure notification filed with Novartis AG and the SIX Swiss Exchange, Capital Group Companies, Inc., Los Angeles, USA, held between 3% and 5% of the share capital of Novartis AG as of December 31, 2011.

Disclosure notifications pertaining to shareholdings in Novartis AG that were filed with Novartis AG and the SIX Swiss Exchange are published on the latter's electronic publication platform, and can be accessed via the database search page:
http://www.six-exchange-regulation.com/obligations/disclosure/major_shareholders_en.html

Novartis has not entered into any agreement with any shareholder regarding the voting or holding of Novartis shares.

CROSS SHAREHOLDINGS

Novartis has no cross shareholdings in excess of 5% of capital or voting rights with any other company.

DISTRIBUTION OF NOVARTIS SHARES

The information in the following tables relates only to registered shareholders and does not include holders of unregistered shares. Also, the information provided in the tables below cannot be assumed to be representative of the entire Novartis investor base since nominees and JPMorgan Chase Bank, as ADS depositary, are registered as shareholders for a large number of beneficial owners.

As of December 31, 2011, Novartis had more than 164 000 registered shareholders.

The following table provides information about the distribution of registered shareholders by number of shares held:

NUMBER OF SHARES HELD

As of December 31, 2011	Number of registered shareholders	% of registered share capital
1–100	20 836	0.05
101–1 000	97 906	1.59
1 001–10 000	41 655	4.25
10 001–100 000	3 837	3.60
100 001–1 000 000	495	5.26
1 000 001–5 000 000	79	6.60
5 000 001 or more[1]	35	53.58
Total registered shareholders/shares	164 843	74.93
Unregistered shares		25.07
Total		**100.00**

[1] Including significant registered shareholders as listed above

The following table provides information about distribution of registered shareholders by type:

REGISTERED SHAREHOLDERS BY TYPE

As of December 31, 2011	Shareholders in %	Shares in %
Individual shareholders	96.05	12.37
Legal entities	3.85	39.00
Nominees, fiduciaries	0.10	48.63
Total	**100.00**	**100.00**

The following table provides information about registered shareholders by country:

REGISTERED SHAREHOLDERS BY COUNTRY

As of December 31, 2011	Shareholders in %	Shares in %
France	2.86	1.32
Germany	4.34	3.47
Switzerland[1]	89.37	43.03
United Kingdom	0.51	3.07
United States	0.36	44.57
Other countries	2.56	4.54
Total	**100.00**	**100.00**

[1] Excluding 5.76% of the share capital held by Novartis AG, together with Novartis affiliates, as treasury shares

SHAREHOLDER RIGHTS

RIGHT TO VOTE ("ONE SHARE, ONE VOTE")

Each share registered with the right to vote entitles the holder to one vote at General Meetings.

ADS holders may vote by instructing JPMorgan Chase Bank, the ADS depositary, to exercise the voting rights attached to the registered shares underlying the ADSs. JPMorgan Chase Bank exercises the voting rights for registered shares underlying ADSs for which no voting instructions have been given by providing a discretionary proxy to the independent proxy (unabhängiger Stimmrechtsvertreter) appointed by Novartis pursuant to Swiss law.

RESOLUTIONS AND ELECTIONS AT GENERAL MEETINGS

The General Meeting passes resolutions and elections with the absolute majority of the votes represented at the meeting. However, under the Articles of Incorporation (www.novartis.com/corporate-governance) the approval of two-thirds of the votes represented at the meeting is required for:

– An alteration of the purpose of Novartis AG;
– The creation of shares with increased voting powers;
– An implementation of restrictions on the transfer of registered shares and the removal of such restrictions;
– An authorized or conditional increase of the share capital;
– An increase of the share capital out of equity, by contribution in kind, for the purpose of an acquisition of property, or the grant of special rights;
– A restriction or suspension of rights or options to subscribe;
– A change of location of the registered office of Novartis AG; or
– The dissolution of Novartis AG.

In addition, the law provides for a special quorum also for other resolutions, such as, for example, for a merger or spin-off.

OTHER SHAREHOLDER RIGHTS

Shareholders representing at least 10% of the share capital may request that an extraordinary General Meeting of shareholders be convened. Shareholders representing shares with an aggregate nominal value of at least CHF 1 million may request that an item be included in the agenda of a General Meeting of shareholders. Such requests must be made in writing at least 45 days before the date of the General Meeting, specify the item to be included in the agenda and contain the proposal on which the shareholder requests a vote.

Shareholders have the right to receive dividends, appoint another shareholder, the corporate proxy, the independent proxy or a custody proxy as proxy and hold such other rights as are granted under Swiss Law.

SHAREHOLDER REGISTRATION

No restrictions apply on the transferability of Novartis shares. However, only shareholders registered in the Novartis share register may exercise their voting rights. In order to be registered, a shareholder must declare that he or she acquired the shares in his or her own name and for his or her own account. The Articles of Incorporation provide that the Board of Directors may register nominees with the right to vote. For restrictions on registration of nominees, please see below.

The Articles of Incorporation provide that no shareholder shall be registered with the right to vote for more than 2% of the registered share capital. The Board of Directors may, upon request, grant an exemption from this restriction. Exemptions are in force for the registered Significant Shareholders listed under – Our Shareholders – Shareholdings – Significant Shareholders. In 2011, no exemptions were requested.

The same restrictions apply to holders of ADSs as those holding Novartis shares.

Given that shareholder representation at General Meetings has traditionally been low in Switzerland, Novartis considers the restriction on registration necessary to prevent a minority shareholder from dominating a General Meeting.

The Articles of Incorporation provide that no nominee shall be registered with the right to vote for more than 0.5% of the registered share capital. The Board of Directors may, upon request, grant an exemption from this restriction if the nominee discloses the names, addresses and the number of shares of the persons for whose account it holds 0.5% or more of the registered share capital. Exemptions are in force for the nominees listed under – Our Shareholders – Shareholdings – Significant Shareholders.

The same restrictions apply to holders of ADSs as those holding Novartis shares.

The restrictions on registration contained in the Articles of Incorporation may only be removed by a resolution of the General Meeting of shareholders, with approval of at least two-thirds of the votes represented at the meeting.

Shareholders, ADS holders or nominees that are linked to each other or act in concert to circumvent the restrictions on registration are treated as one person or nominee for the purposes of the restrictions on registration.

NO RESTRICTION ON TRADING OF SHARES

The registration of shareholders in the Novartis share register or in the ADS register kept by JPMorgan Chase Bank does not affect the tradability of Novartis shares or ADSs. No restrictions are imposed by Novartis or JPMorgan Chase Bank on the trading of registered Novartis shares or ADSs. Registered Novartis shareholders or ADS holders may, therefore, purchase or sell their Novartis shares or ADSs at any time, including prior to a General Meeting regardless of the record date. The record date serves only to determine the right to vote at a General Meeting of Novartis.

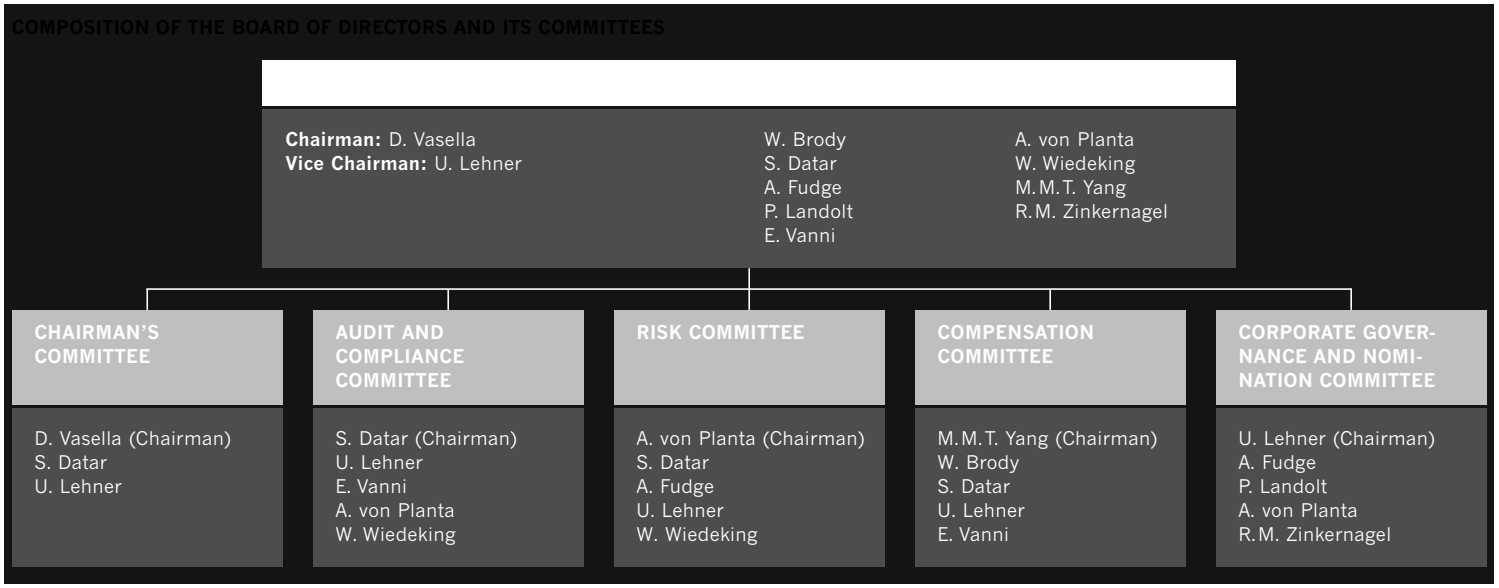
CHANGE-OF-CONTROL PROVISIONS

NO OPTING UP, NO OPTING OUT

The Swiss Stock Exchange Act provides that anyone who, directly, indirectly or acting in concert with third parties, acquires equity securities exceeding 33 1/3% of the voting rights of a company – whether or not such rights are exercisable – is required to make an offer to acquire all listed equity securities of that company. A company may raise this threshold to 49% of the voting rights ("opting up") or may, under certain circumstances, waive the threshold ("opting out"). Novartis has not adopted any such measures.

CLAUSES ON CHANGES-OF-CONTROL

There are no change-of-control clauses benefiting Board members. With respect to members of the Executive Committee, see below under – Our Management – Contracts with Members of the Executive Committee.



ELECTION AND TERM OF OFFICE

All Board members are elected individually.

Board members are elected to terms of office of three years or less by shareholders at General Meetings. The terms of office among Board members are to be coordinated so that approximately one-third of all Board members are subject each year to re-election or election. Under Swiss law, a General Meeting of shareholders is entitled to remove any Board member at any time, regardless of his or her remaining term of office.

The average tenure of Board members is eight years and the average age is 61. A Board member must retire after reaching age 70. Under special circumstances, shareholders may grant an exemption from this rule and re-elect a Board member for additional terms of office of no more than three years at a time.

Name	Nationality	Year of birth	First election at AGM	Last election at AGM	End of current Term
Daniel Vasella, M.D.	CH	1953	1996	2010	2013
Ulrich Lehner, Ph.D.	D	1946	2002	2011	2014
William Brody, M.D., Ph.D.	US	1944	2009	2009	2012
Srikant Datar, Ph.D.	US	1953	2003	2009	2012
Ann Fudge	US	1951	2008	2011	2014
Pierre Landolt, Ph.D.	CH	1947	1996	2011	2014
Enrico Vanni, Ph.D.	CH	1951	2011	2011	2014
Andreas von Planta, Ph.D.	CH	1955	2006	2009	2012
Dr. Ing. Wendelin Wiedeking	D	1952	2003	2009	2012
Marjorie M.T. Yang	CHN	1952	2007	2010	2013
Rolf M. Zinkernagel, M.D.	CH	1944	1999	2009	2012

BOARD MEMBER QUALIFICATIONS

The Corporate Governance and Nomination Committee determines the criteria for the selection of the Board members and Board committee members. Factors considered include skills and knowledge, diversity of viewpoints, professional backgrounds and expertise, business and other experience relevant to the business of Novartis, the ability and willingness to commit adequate time and effort to Board and committee responsibilities, the extent to which person-

ality, background, expertise, knowledge and experience will interact with other Board members to build an effective and complementary Board, and whether existing board memberships or other positions held by a candidate could lead to a conflict of interest.

The biographies of the Board members (pages 98–101) set out the particular qualifications that led the Board of Directors to conclude that a Board member is qualified to serve on the Board of Directors, creating a Board that today is diverse in terms of background, qualifications, interests and skills.

ROLE OF THE BOARD OF DIRECTORS AND THE BOARD COMMITTEES

The Board of Directors is responsible for the overall direction and supervision of the management and holds the ultimate decision-making authority for Novartis AG, except for those decisions reserved to the shareholders.

The Board of Directors has delegated certain responsibilities to five committees: Chairman's Committee, Compensation Committee, Audit and Compliance Committee, Corporate Governance and Nomination Committee and Risk Committee as set out below (responsibilities described with the terms "overseeing" or "reviewing" are subject to final approval by the Board of Directors).

Responsibilities	Membership comprises	Number of meetings held in 2011/approximate average duration of each meeting Attendance	Link
THE BOARD OF DIRECTORS		**9/7**	
The primary responsibilities of the Board of Directors include: – Setting the strategic direction of the Group; – Determining the organizational structure and governance of the Group; – Appointing, overseeing and dismissing key executives and planning their succession; – Determining and overseeing the financial planning, accounting, reporting and controlling; – Approving the annual financial statements and the corresponding financial results releases; and – Approving major transactions and investments.	**Daniel Vasella**[1] Ulrich Lehner William Brody Srikant Datar Ann Fudge Pierre Landolt Enrico Vanni[2] Andreas von Planta Wendelin Wiedeking Marjorie M.T. Yang Rolf M. Zinkernagel	9 9 9 9 9 7 7 9 9 9 8	Articles of Incorporation of Novartis AG Regulations of the Board of Directors, its Committees and the Executive Committee of Novartis AG (Board Regulations) http://www.novartis.com/corporate-governance
THE CHAIRMAN'S COMMITTEE		**6/2**	
The primary responsibilities of this committee include: – Commenting on significant matters before the Board of Directors makes a decision; – Recommending key executive appointments to the Board of Directors; – Dealing with Board matters arising in between Board meetings, including the taking of required preliminary actions; and – Approving transactions and investments as delegated by the Board of Directors.	**Daniel Vasella**[1] Srikant Datar[2] Ulrich Lehner	6 5 6	Charter of the Chairman's Committee http://www.novartis.com/corporate-governance
THE AUDIT AND COMPLIANCE COMMITTEE		**6/3**	
The primary responsibilities of this committee include: – Overseeing the internal auditors; – Supervising the external auditors and selecting and nominating the external auditors for election by the meeting of the shareholders; – Overseeing the accounting policies, financial controls and compliance with accounting and internal control standards; – Approving quarterly financial statements and financial results releases; – Overseeing internal control and compliance processes and procedures; and – Overseeing compliance with laws and external and internal regulations. The Audit and Compliance Committee has the authority to retain external consultants and other advisors.	**Srikant Datar**[1,3] Ulrich Lehner[3] Enrico Vanni[4] Andreas von Planta Wendelin Wiedeking	6 6 3 6 6	Charter of the Audit and Compliance Committee http://www.novartis.com/corporate-governance

[1] Chair
[2] Since February 2011
[3] Audit Committee Financial Expert as defined by the US Securities and Exchange Commission (SEC)
[4] Since April 2011

Responsibilities	Membership comprises	Number of meetings held in 2011/approximate average duration of each meeting Attendance	Link
THE RISK COMMITTEE		**4/2**	
The primary responsibilities of this committee include: – Ensuring that Novartis has implemented an appropriate and effective risk management system and process; – Ensuring that all necessary steps are taken to foster a culture of risk-adjusted decision making without constraining reasonable risk-taking and innovation; – Approving guidelines and reviewing policies and processes; and – Reviewing with management, internal auditors and external auditors the identification, prioritization and management of the risks, the accountabilities and roles of the functions involved with risk management, the risk portfolio and the related actions implemented by management. The Risk Committee has the authority to retain external consultants and other advisors.	**Andreas von Planta**[1] Srikant Datar Ann Fudge[2] Ulrich Lehner Wendelin Wiedeking	4 4 3 4 4	Charter of the Risk Committee http://www.novartis.com/corporate-governance
THE COMPENSATION COMMITTEE		**5/1.5**	
The primary responsibilities of this committee include: – Designing, reviewing and recommending to the Board compensation policies and programs; – Advising the Board on the compensation of the Board members; – Approving the employment terms of key executives; – Deciding on the variable compensation of the Chief Executive Officer, the members of the Executive Committee and other key executives for the past year; and – Deciding on the base salary and the total target compensation of the Chief Executive Officer, the members of the Executive Committee and other key executives for the coming year. The Compensation Committee has the authority to retain external consultants and other advisors.	**Marjorie M.T. Yang**[1] William Brody Srikant Datar Ulrich Lehner Enrico Vanni[3]	5 4 5 4 4	Charter of the Compensation Committee http://www.novartis.com/corporate-governance
THE CORPORATE GOVERNANCE AND NOMINATION COMMITTEE		**3/2**	
The primary responsibilities of this committee include: – Designing, reviewing and recommending to the Board corporate governance principles; – Reviewing on a regular basis the Articles of Incorporation with a view to reinforcing shareholder rights; – Reviewing on a regular basis the composition and size of the Board and its committees; – Reviewing annually the independence status of each Board member; – Reviewing directorships and agreements of board members for conflicts of interest and dealing with conflicts of interest; – Identifying candidates for election as Board member; – Assessing existing Board members and recommending to the Board whether they should stand for re-election; – Preparing and reviewing the succession plan for the CEO; and – Developing and reviewing an orientation program for new Board members and an ongoing education plan for existing Board members. The Corporate Governance and Nomination Committee has the authority to retain external consultants and other advisors.	**Ulrich Lehner**[1] Ann Fudge Pierre Landolt Andreas von Planta Rolf M. Zinkernagel	3 3 2 3 3	Charter of the Corporate Governance and Nomination Committee http://www.novartis.com/corporate-governance

[1] Chair
[2] Since February 2011
[3] Since April 2011

THE FUNCTIONING OF THE BOARD OF DIRECTORS

The Novartis Board of Directors takes decisions as a whole, supported by its five Board committees (Chairman's Committee, Compensation Committee, Audit and Compliance Committee, Corporate Governance and Nomination Committee and Risk Committee). Each Board committee has a written charter outlining its duties and responsibilities and is led by a Chair elected by the Board of Directors.

The Board of Directors and its Board committees meet regularly throughout the year. The Chairs set the agendas of their meetings. Any Board member may request a Board meeting, a meeting of a Board committee, a meeting of the independent Board members or the inclusion of an item on the agenda of such meetings. Board members are provided, in advance of meetings, with materials intended to prepare them to discuss the items on the agenda.

THE CHAIRMAN

The Chairman provides leadership to the Board of Directors in its governance role, oversees that the strategy agreed by the Board of Directors is implemented by the Chief Executive Officer and his reports, provides support and advice to the Chief Executive Officer, reviews the yearly objectives and prepares the performance evaluation of the Chief Executive Officer before approval by and feedback session with the Board of Directors, works closely with the Chief Executive Officer in nominating and evaluating members and permanent attendees of the Executive Committee and in establishing succession plans for key management positions, represents Novartis with stakeholders and oversees Internal Audit.

MEETINGS OF THE BOARD OF DIRECTORS

The Board of Directors has meetings with the members of the Executive Committee, private meetings without members of the Executive Committee and meetings of only the independent Board members.

Topics addressed in the meetings with the Executive Committee include strategy, business reviews and major projects, investments and transactions. Topics addressed in private meetings include performance evaluation of top management, succession planning and Board self-evaluation.

As long as the Chairman is not independent, Dr. Ulrich Lehner, Vice-Chairman, chairs sessions of the independent Board members and leads the independent Board members in case of a crisis or matters requiring their separate consideration or decision. Moreover, every independent Board member may request separate meetings of the independent Board members if the need arises. Dr. Ulrich Lehner also leads the Board if the Chairman is incapacitated.

In 2011, there were nine meetings of the Board of Directors and six meetings of the independent Board members.

INDEPENDENCE OF BOARD MEMBERS

The independence of Board members is a key corporate governance issue. Accordingly, Novartis established independence criteria that are intended to reflect international best-practice standards. These independence criteria (last revised on October 16, 2008) can be found on the Novartis website:
www.novartis.com/investors/governance-documents.shtml

The Corporate Governance and Nomination Committee annually submits to the Board of Directors a proposal concerning the determination of the independence of each Board member. For this assessment, the Committee considers all relevant facts and circumstances of which it is aware.

In its meeting on December 14, 2011, the Board of Directors determined that all of its members, except for Dr. Vasella, were independent.

Dr. Vasella, the Chairman, was until January 31, 2010 also the Chief Executive Officer. The Board of Directors has delegated Rolf M. Zinkernagel, M.D., to the Scientific Advisory Board of the Novartis Institute for Tropical Diseases (NITD), and both Dr. Zinkernagel, M.D. and William Brody, M.D. to the Board of Directors of the Genomics Institute of the Novartis Research Foundation (GNF). The Board of Directors concluded that these activities are supervisory and not consultatory in nature and do not affect Dr. Zinkernagel's or Dr. Brody's independence as a Board member.

RELATIONSHIP OF NON-EXECUTIVE BOARD MEMBERS WITH NOVARTIS

With the exception of Dr. Vasella none of the Board members is or was a member of the management of Novartis AG or of any other Novartis Group company in the three financial years preceding 2011.

There are no significant business relationships of any Board member with Novartis AG or with any other Novartis Group company.

INFORMATION AND CONTROL SYSTEMS OF THE BOARD OF DIRECTORS VIS-À-VIS MANAGEMENT

INFORMATION ON THE MANAGEMENT

The Board of Directors ensures that it receives sufficient information from the Executive Committee to perform its supervisory duty and to make decisions that are reserved for the Board of Directors. The authority of the Board of Directors to determine the compensation of the members of the Executive Committee is an important element to ensure the alignment of Executive Committee members with the interests of Novartis and its shareholders.

The Board of Directors obtains the information required to perform its duties through several means:
- the Chief Executive Officer informs the Board regularly about current developments;
- the minutes of Executive Committee meetings are made available to the Board members;
- meetings or teleconferences are held as required between Board members and the Chief Executive Officer;
- the Board of Directors regularly meets with all members of the Executive Committee;

– the Board of Directors is updated in detail by each Division Head on a quarterly basis;
– by invitation, other members of management are invited to attend Board meetings to report on areas of the business within their responsibility; and
– Board members are entitled to request information from members of the Executive Committee or any other Novartis associate, and may also visit any Novartis site.

BOARD COMMITTEES

Board committees regularly meet with management and, at times, outside consultants to review the business, better understand applicable laws and policies affecting the Group and support the Board of Directors and the management in meeting the requirements and expectations of stakeholders and shareholders.

In particular, the Chief Financial Officer, the Group General Counsel and representatives of the external auditors are invited to meetings of the Audit and Compliance Committee. Furthermore, the Heads of Internal Audit, Financial Reporting and Accounting, Compliance, as well as the Business Practices Officers, report on a regular basis to the Audit and Compliance Committee.

The Audit and Compliance Committee reviews financial reporting processes on behalf of the Board of Directors. For each quarterly and annual release of financial information, the Disclosure Review Committee reviews the release for accuracy and completeness of disclosures. The Disclosure Review Committee is chaired by the Chief Financial Officer and is attended by the Group General Counsel, the Heads of the Divisions, the Heads of Finance of the Divisions and the Heads of the following Corporate Functions: Treasury, Financial Reporting and Accounting, Internal Audit and Investor Relations. Decisions made by the Disclosure Review Committee are reviewed by the Audit and Compliance Committee before publication of the quarterly and annual release.

The Risk Committee oversees the risk management system and processes, as well as reviews the risk portfolio of the Group to ensure appropriate and professional management of the risks. For this purpose the Corporate Risk Management function and the risk owners of the Divisions report on a regular basis to the Risk Committee. The Group General Counsel and the Head of Internal Audit are also invited to the meetings.

NOVARTIS MANAGEMENT INFORMATION SYSTEM

Novartis produces comprehensive consolidated financial statements on a monthly basis. These are typically available within ten days of the end of the month and include the following:
– consolidated income statement of the month, quarter-to-date and year-to-date in accordance with International Financial Reporting Standards (IFRS), as well as on a year-to-date and quarterly basis adjustments to arrive at Core results as defined by Novartis. The IFRS figures are compared to the prior year period and targets in both USD and on a constant currency basis;
– consolidated balance sheet as of the month end in accordance with IFRS in USD;
– consolidated cash flow on a year-to-date basis in accordance with IFRS in USD; and
– supplementary data on a monthly, quarterly and year-to-date basis such as free cash flow and gross and net liquidity, headcount, personnel costs, and working capital as defined by Novartis and on a USD basis where applicable.

The above information is made available to the members of the Board on a monthly basis. An analysis of the key deviations from prior year or target is also provided.

The Board also receives on a quarterly basis an outlook of the full year results in accordance with IFRS and Core, together with related commentary prior to the release of the quarterly results.

On an annual basis, in the fourth quarter of the year, the Board receives and approves the operating and financial targets for the following year.

In the middle of the year, the Board also reviews and approves the Strategic Plan for the next five years and the consolidated income statement in USD in accordance with IFRS and Core contained in the Plan.

The Board does not have direct access to Novartis' financial and management reporting systems but can at any time request more detailed financial information on any aspect that is presented to it.

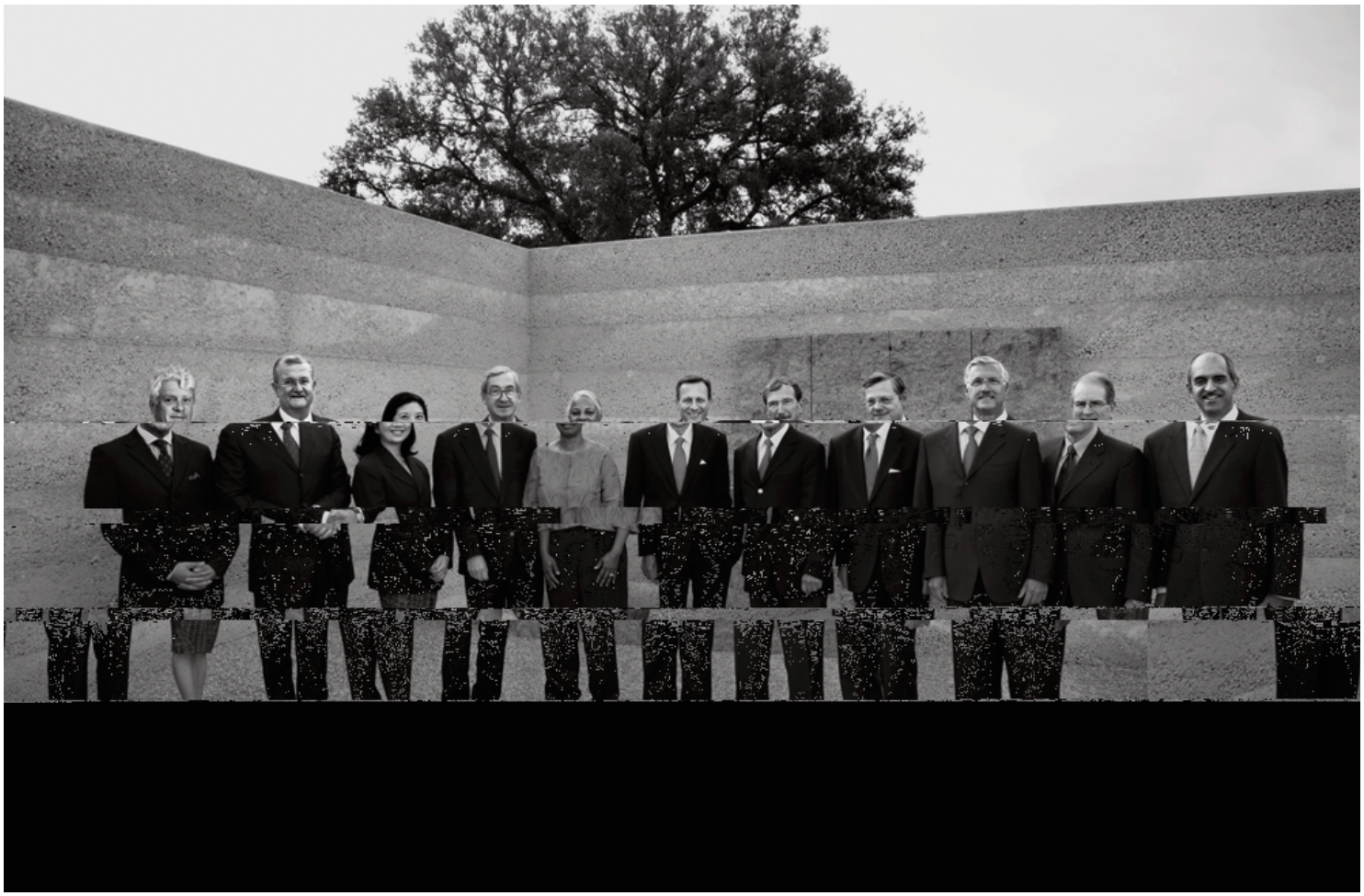
INTERNAL AUDIT

The Internal Audit function carries out operational and system audits in accordance with an audit plan approved by the Audit and Compliance Committee; assists organizational units in the accomplishment of objectives by providing an independent approach to the evaluation, improvement and effectiveness of their internal control framework; prepares reports regarding the audits it has performed; and reports actual or suspected irregularities to the Audit and Compliance Committee and the Chairman. The Audit and Compliance Committee regularly reviews the scope of Internal Audit, the audit plans and the results of the internal audits.

RISK MANAGEMENT

The Corporate Risk Management function reports to the independent Risk Committee of the Board of Directors. The Compensation Committee works closely with the Risk Committee to ensure that the compensation system does not lead to excessive risk-taking by management (for details see our Compensation Report).

Organizational and process measures have been designed to identify and mitigate risks at an early stage. Organizationally, the individual divisions are responsible for risk and risk mitigation, with specialized corporate functions, such as Group Finance, Group Quality Operations, Corporate Health, Safety, Environment and Business Continuity, providing support and controlling the effectiveness of risk management by the Divisions in these respective areas.



From left to right: Pierre Landolt, Wendelin Wiedeking, Marjorie Mun Tak Yang, Ulrich Lehner, Ann Fudge, Daniel Vasella, Rolf M. Zinkernagel, Andreas von Planta, Enrico Vanni, William Brody, Srikant Datar

BOARD OF DIRECTORS

MEMBERS

Chairman
Swiss, age 58

Vice Chairman
German, age 65

American, age 67

American, age 58

American, age 60

Swiss, age 64

Swiss, age 60

Swiss, age 56

German, age 59

Chinese, age 59

Swiss, age 67

HONORARY CHAIRMAN

CORPORATE SECRETARY

Swiss, age 58

Function at Novartis AG Daniel Vasella, M.D., is Chairman of the Board of Directors for Novartis AG. He served as Chief Executive Officer (CEO) and executive member of the Board of Directors for 14 years following the merger that created Novartis in 1996. Dr. Vasella was appointed Chairman in April 1999.

Other activities Dr. Vasella is a member of the board of directors of PepsiCo, Inc. He is also a member of the International Board of Governors of the Peres Center for Peace in Israel, the International Business Leaders Advisory Council for the Mayor of Shanghai, the Global Health Program Advisory Panel of the Bill & Melinda Gates Foundation, and is a foreign honorary member of the American Academy of Arts and Sciences. He is also a member of the Board of Trustees of the Carnegie Endowment for International Peace. In addition, Dr. Vasella serves as a member of several industry associations and educational institutions.

Professional background Before the Novartis merger, Dr. Vasella was CEO of Sandoz Pharma Ltd. and a member of the Sandoz Group Executive Committee. From 1988 to 1992, he was with Sandoz Pharmaceuticals Corporation in the United States, prior to which he held a number of medical positions in Switzerland. He graduated with an M.D. from the University of Bern in Switzerland and completed executive training at the Harvard Business School in the United States. He was also awarded an honorary doctorate by the University of Basel.

Key knowledge/experience *Leadership, Biomedical Science and Global Marketing experience* – former CEO of Novartis; advisory panel member for international health and development foundation. *Industry experience* – board member for global consumer goods company.

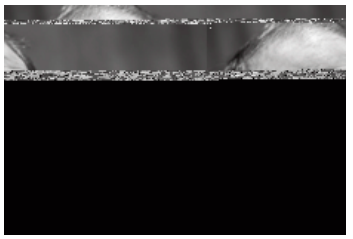
German, age 65

Function at Novartis AG Ulrich Lehner, Ph.D., has been a member of the Board of Directors since 2002. He qualifies as an independent Non-Executive Director. He serves as Vice Chairman and Chairman of the Corporate Governance and Nomination Committee. He is also a member of the Audit and Compliance Committee, the Risk Committee, the Chairman's Committee, and the Compensation Committee. The Board of Directors has appointed him as Audit Committee Financial Expert.

Other activities Mr. Lehner is member of the shareholders' committee of Henkel AG & Co. KGaA, Chairman of the Supervisory Board of Deutsche Telekom AG, and serves as a member of the supervisory boards of E.ON AG, ThyssenKrupp AG, Porsche Automobil Holding SE and Henkel Management AG, all in Germany. He is also a member of the shareholders' committee of Dr. August Oetker KG and Krombacher Brauerei, both in Germany.

Professional background Mr. Lehner graduated in business administration and mechanical engineering from the Darmstadt University of Technology, Germany, in 1975. From 1975 to 1981, he was an auditor with KPMG Deutsche Treuhand-Gesellschaft AG in Duesseldorf. In 1981, he joined Henkel KGaA. After heading the Controlling Department of Fried. Krupp GmbH in Germany from 1983 to 1986, Mr. Lehner returned to Henkel as Finance Director. From 1991 to 1994, he headed Henkel Asia-Pacific Ltd. in Hong Kong, and from 1995 to 2000, he served as Executive Vice President, Finance/Logistics, of Henkel KGaA. From 2000 to 2008, Mr. Lehner served as Chairman of the Management Board of Henkel KGaA.

Key knowledge/experience *Leadership and Global experience* – chairman of supervisory board of global telecommunication company; former chairman of the management board of global consumer goods company. *Industry experience* – member of supervisory boards of global energy, automotive and manufacturing technology companies.



American, age 67

Function at Novartis AG William Brody, M.D., Ph.D., has been a member of the Board of Directors since 2009. He qualifies as an independent Non-Executive Director. He is a member of the Compensation Committee.

Other activities Dr. Brody is President of the Salk Institute for Biological Studies, La Jolla, Calif., United States. He is also a member of the boards of directors of the US-based International Business Machines Corp. and Kool Smiles Inc., and the mutual funds boards of T. Rowe Price. He is a member of numerous professional associations, and also serves on the advisory boards of various government and nonprofit organizations.

Professional background Dr. Brody earned his bachelor's and master's degrees in electrical engineering from the Massachusetts Institute of Technology before completing his M.D. and Ph.D. at Stanford University. Following training in cardiovascular surgery and radiology he held various academic positions, including Professor for Radiology and Electrical Engineering at Stanford University and Director of the Department of Radiology at The Johns Hopkins University. From 1996 to 2009, he was president of The Johns Hopkins University, and since 2009, president of the Salk Institute for Biological Studies in the United States. He is a member of the US National Academy of Engineering and the Institute of Medicine.

Key knowledge/experience *Leadership, Biomedical Science, Healthcare and Education experience* – president of leading US scientific research institution; former president of leading US university. *Global, Engineering and Technology experience* – former board member of global technology company.

American, age 58

Function at Novartis AG Srikant Datar, Ph.D., has been a member of the Board of Directors since 2003. He qualifies as an independent Non-Executive Director. He is Chairman of the Audit and Compliance Committee, and a member of the Chairman's Committee, the Risk Committee and the Compensation Committee. The Board of Directors has appointed him as Audit Committee Financial Expert.

Other activities Mr. Datar is Arthur Lowes Dickinson Professor at the Graduate School of Business Administration at Harvard University. He is also a member of the board of directors of ICF International Inc. and of Stryker Corp., both in the United States, and of KPIT Cummins Infosystems Ltd., India.

Professional background Mr. Datar graduated with distinction in mathematics and economics from the University of Bombay, India, in 1973. He is a Chartered Accountant, and holds two master's degrees and a Ph.D. from Stanford University. Mr. Datar has worked as an accountant and planner in industry, and as a professor at Carnegie Mellon University, Stanford University and Harvard University all in the United States. His research interests are in the areas of cost management, measurement of productivity, new product development, time-based competition, incentives and performance evaluation. He is the author of many scientific publications, and has received several academic awards and honors. Mr. Datar has advised and worked with numerous companies in research, development and training.

Key knowledge/experience *Leadership and Education experience* – former senior associate dean and current professor of leading US university. *Global and Industry experience* – board member of global professional services firm; board member of global leading medical technology company; board member of Indian high-technology company.

American, age 60

Function at Novartis AG Ann Fudge has been a member of the Board of Directors since 2008. She qualifies as an independent Non-Executive Director. She is a member of the Corporate Governance and Nomination Committee, and the Risk Committee.

Other activities Ms. Fudge serves on the board of directors of General Electric Co., on the board of directors of Unilever, UK/Netherlands and on the board of directors of Infosys, India. She is a trustee of the New York-based Rockefeller Foundation and the Atlanta-based Morehouse College, and is chairman of the US Programs Advisory Panel of the Bill & Melinda Gates Foundation. Ms. Fudge is further a member of the Harvard University Corporation Committee on Finance. She also is on the board of the Council on Foreign Relations.

Professional background Ms. Fudge received her bachelor's degree from Simmons College and her MBA from Harvard University Graduate School of Business in the United States. She is former chairman and CEO of Young & Rubicam Brands. Before that, she served as president of the Beverages, Desserts and Post Division of Kraft Foods Inc.

Key knowledge/experience *Leadership and Marketing experience* – former chairman and CEO of global marketing communications company; former president of leading consumer products business unit. *Global and Industry experience* – board member of global technology company and global consumer goods company.

Swiss, age 64

Function at Novartis AG Pierre Landolt has been a member of the Board of Directors since 1996. He qualifies as an independent Non-Executive Director. He is a member of the Corporate Governance and Nomination Committee.

Other activities Mr. Landolt is currently chairman of the Sandoz Family Foundation and oversees the development of the foundation in several investment fields. He is a member of the board of directors of Syngenta AG. He is a partner with unlimited liabilities of the Swiss private bank Landolt & Cie. In Brazil, Mr. Landolt serves as president of the Instituto Fazenda Tamanduá, the Instituto Estrela de Fomento ao Microcrédito, AxialPar Ltda. and Moco Agropecuaria Ltda. In Switzerland, he is chairman of Emasan AG and Vaucher Manufacture Fleurier SA, vice chairman of Parmigiani Fleurier SA, and is on the board of the Syngenta Foundation for Sustainable Agriculture. He is a member of the board of EcoCarbone SA, France, and Swiss Amazentis SA. He is also vice chairman of the Montreux Jazz Festival Foundation.

Professional background Mr. Landolt graduated with a bachelor's degree in law from the University of Paris-Assas. From 1974 to 1976, he worked for Sandoz Brazil SA. In 1977, he acquired an agricultural estate in the semi-arid Northeast Region of Brazil and, over several years, converted it into a model farm in organic and biodynamic production. Since 1997, Mr. Landolt has been associate and chairman of AxialPar Ltda., Brazil, an investment company focused on sustainable development. In 2000, he co-founded EcoCarbone SA, France, a company active in the design and development of carbon-sequestration processes. In 2007, he co-founded Amazentis SA, Switzerland, a startup company active in the convergence space of medication and nutrition.

Key knowledge/experience *Banking and Industry experience; International and Emerging Market experience* – partner of private bank; chairman and vice chairman of luxury goods companies. *Leadership and Global experience* – President of large family investment holding; board member of global agribusiness company; board member of sustainable agriculture foundation.

Swiss, age 60

Function at Novartis AG Enrico Vanni, Ph.D., has been a member of the Board of Directors since 2011. He qualifies as an independent Non-Executive Director. He is a member of the Audit and Compliance Committee, and the Compensation Committee.

Other activities Since his retirement as director of McKinsey & Company in 2007, Mr. Vanni has been an independent consultant. He is currently a member of several boards of directors in industries from healthcare to private banking, for nonlisted companies including Eclosion2, Denzler & Partners SA and Banque Privée BCP (Suisse) SA.

Professional background Mr. Vanni holds an engineering degree in chemistry from the Federal Polytechnic School of Lausanne, Switzerland, a Ph.D. in chemistry from the University of Lausanne, as well as a Master of Business Administration from INSEAD in Fontainebleau, France. He began his career as a research engineer at International Business Machines Corp. in California, and joined McKinsey & Company in Zurich, Switzerland, in 1980. He managed the Geneva office for McKinsey from 1988 to 2004, and consulted for companies in the pharmaceutical, consumer and finance sectors. He led the company's European pharmaceutical practice and served as member of the Partner review committee of the firm prior to his retirement in 2007. As an independent consultant, Mr. Vanni has continued to support leaders of pharmaceutical and biotechnology companies on core strategic challenges facing the healthcare industry.

Key knowledge/experience *Global industry experience* – senior consultant of global pharmaceutical/biotech companies, consumer goods and financial institutions. *Science experience* – research engineer in technology company and management of projects in global pharmaceutical R&D. *Leadership experience* – office management of global consultant company and leadership of its European pharmaceutical practice.

Swiss, age 56

Function at Novartis AG Andreas von Planta, Ph.D., has been a member of the Board of Directors since 2006. He qualifies as an independent Non-Executive Director. He is Chairman of the Risk Committee, and a member of the Audit and Compliance Committee, as well as the Corporate Governance and Nomination Committee.

Other activities Mr. von Planta is chairman of the Schweizerische National-Versicherungs-Gesellschaft AG and a board member of Holcim Ltd., both in Switzerland. He is also a board member of various Swiss subsidiaries of foreign companies and other nonlisted Swiss companies. He is a member of the Board of Editors of the *Swiss Review of Business Law* and is a former chairman of the Geneva Association of Business Law. Mr. von Planta is chairman of the regulatory board of the SIX Swiss Exchange AG.

Professional background Mr. von Planta holds lic. iur. and Ph.D. degrees from the University of Basel, Switzerland, and an LL.M. from Columbia University School of Law, New York, United States. He passed his bar examinations in Basel in 1982. Since 1983 he has lived in Geneva and worked for the law firm Lenz & Staehelin, where he became a partner in 1988. His areas of specialization include corporate law, corporate governance, corporate finance, company reorganizations, and mergers and acquisitions.

Key knowledge/experience *Leadership and Global experience* – chairman of insurance company; board member of global construction materials manufacturer. *Industry experience* – partner of leading Swiss law firm.

German, age 59

Function at Novartis AG Dr. Ing. Wendelin Wiedeking has been a member of the Board of Directors since 2003. He qualifies as an independent Non-Executive Director. He is a member of the Audit and Compliance Committee, and the Risk Committee.

Other activities Mr. Wiedeking was chairman of the executive board of Porsche Automobil Holding SE and of Dr. Ing. h.c. F. Porsche AG, both in Germany, until July 2009. Since then he has been an entrepreneur.

Professional background Mr. Wiedeking graduated in mechanical engineering in 1978 and worked as a scientific assistant in the machine tool laboratory of the Rhine-Westphalian College of Advanced Technology in Germany. His professional career began in 1983 in Germany as director's assistant in the production and materials management area of Dr. Ing. h.c. F. Porsche AG in Stuttgart-Zuffenhausen. In 1988, he moved to Glyco Metall-Werke KG in Wiesbaden as Division Manager, where he advanced by 1990 to the position of Chief Executive Officer and Chairman of the Board of Management of Glyco AG. In 1991, he returned to Dr. Ing. h.c. F. Porsche AG as production director. A year later, the supervisory board appointed him spokesman of the executive board (CEO), then chairman in 1993.

Key knowledge/experience *Leadership, Global and Industry experience* – former chairman and CEO of global automotive company. *Engineering and Technology experience* – former chairman and CEO of manufacturing supply company.

Chinese, age 59

Function at Novartis AG Marjorie Mun Tak Yang has been a member of the Board of Directors since 2008. She qualifies as an independent Non-Executive Director. She is Chairman of the Compensation Committee.

Other activities Ms. Yang is Chairman of the Esquel Group, Hong Kong, China. She is a member of the Executive Council of the Hong Kong Special Administrative Region. In China, she is a member of the National Committee of the Chinese People's Political Consultative Conference. She currently serves on the boards of Swire Pacific Ltd., and The Hong Kong and Shanghai Banking Corp. Ltd. in Hong Kong, and on the boards of a number of nonlisted companies. In January 2010 she was appointed as Chairman of the Council of the Hong Kong Polytechnic University. She also serves on the advisory boards of Harvard Business School, and Tsinghua School of Economics and Management. From 2001 to 2011, Ms. Yang was a member of the MIT Corp.

Professional background Ms. Yang graduated with a bachelor's degree in mathematics from Massachusetts Institute of Technology and holds a master's degree from Harvard Business School, both in the United States. From 1976 to 1978, she was an associate in Corporate Finance, Mergers and Acquisitions, with the First Boston Corporation in New York, United States. In 1979, she returned to Hong Kong and became a founding member of Esquel Group. She was appointed chairman of the Group in 1995.

Key knowledge/experience *Leadership, Global and Industry experience* – chairman of global textile manufacturing company. *Education and Science experience* – trustee of leading US research university; leadership roles at multiple universities.

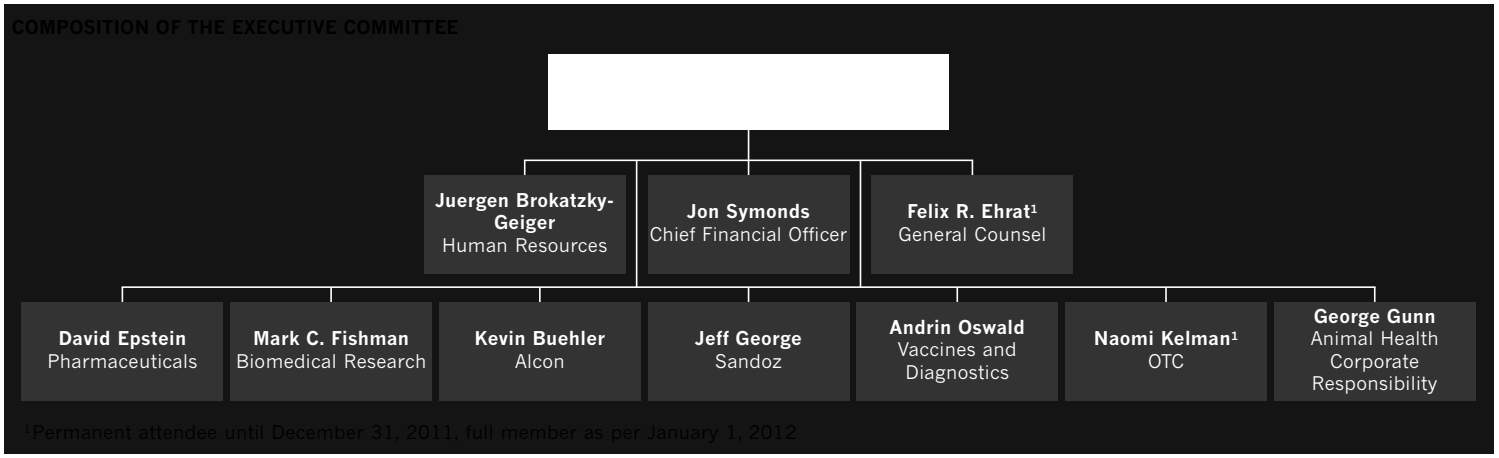
Swiss, age 67

Function at Novartis AG Rolf M. Zinkernagel, M.D., has been a member of the Board of Directors since 1999. He qualifies as an independent Non-Executive Director. He is a member of the Corporate Governance and Nomination Committee.

Other activities Dr. Zinkernagel was Vice President of the International Union of Immunological Societies until 2010. He is a member of the scientific advisory boards of Bio-Alliance AG, Germany; Aravis General Partner Ltd., Cayman Islands and Switzerland; Telormedix, Switzerland; X-Biotech, Canada; Novimmune, Switzerland; Cancevir, Switzerland; Nuvo Research Inc., Canada; ImVision, Germany; MannKind, United States; and Biomedical Sciences International Advisory Council, Singapore. Dr. Zinkernagel is also a science consultant to Chilka Ltd., Cayman Islands; Ganymed, Germany; and Zhen-Ao Group, China. He is a member of the scientific advisory panel of Swiss Re, Switzerland.

Professional background Dr. Zinkernagel graduated from the University of Basel, Switzerland, with an M.D. in 1970. From 1992 to 2008, he was a professor and director of the Institute of Experimental Immunology at the University of Zurich, and after retirement in 2008 continues to be active at the University of Zurich. Dr. Zinkernagel has received many awards and prizes for his work and contribution to science, notably the Nobel Prize in medicine, which he was awarded in 1996.

Key knowledge/experience *Biomedical Science and Education experience* – former professor and director at leading Swiss university. *Leadership and Global experience* – member of scientific advisory boards of numerous global biotech companies; member of major international research councils.



COMPOSITION OF THE EXECUTIVE COMMITTEE

The Executive Committee is headed by the Chief Executive Officer. The members of the Executive Committee are appointed by the Board of Directors. The Chairman may appoint or remove non-voting Permanent Attendees to attend the meetings of the Executive Committee. As of December 31, 2011, there were 2 Permanent Attendees attending meetings of the Executive Committee.

The organizational structure and the details of the responsibility of the Executive Committee are set forth in the Board Regulations (www.novartis.com/corporate-governance).

The Board of Directors has not concluded any contracts with third parties to manage the business.

ROLE AND FUNCTIONING OF THE EXECUTIVE COMMITTEE

The Board of Directors has delegated to the Executive Committee the coordination of the Group's day-to-day business operations. This includes:

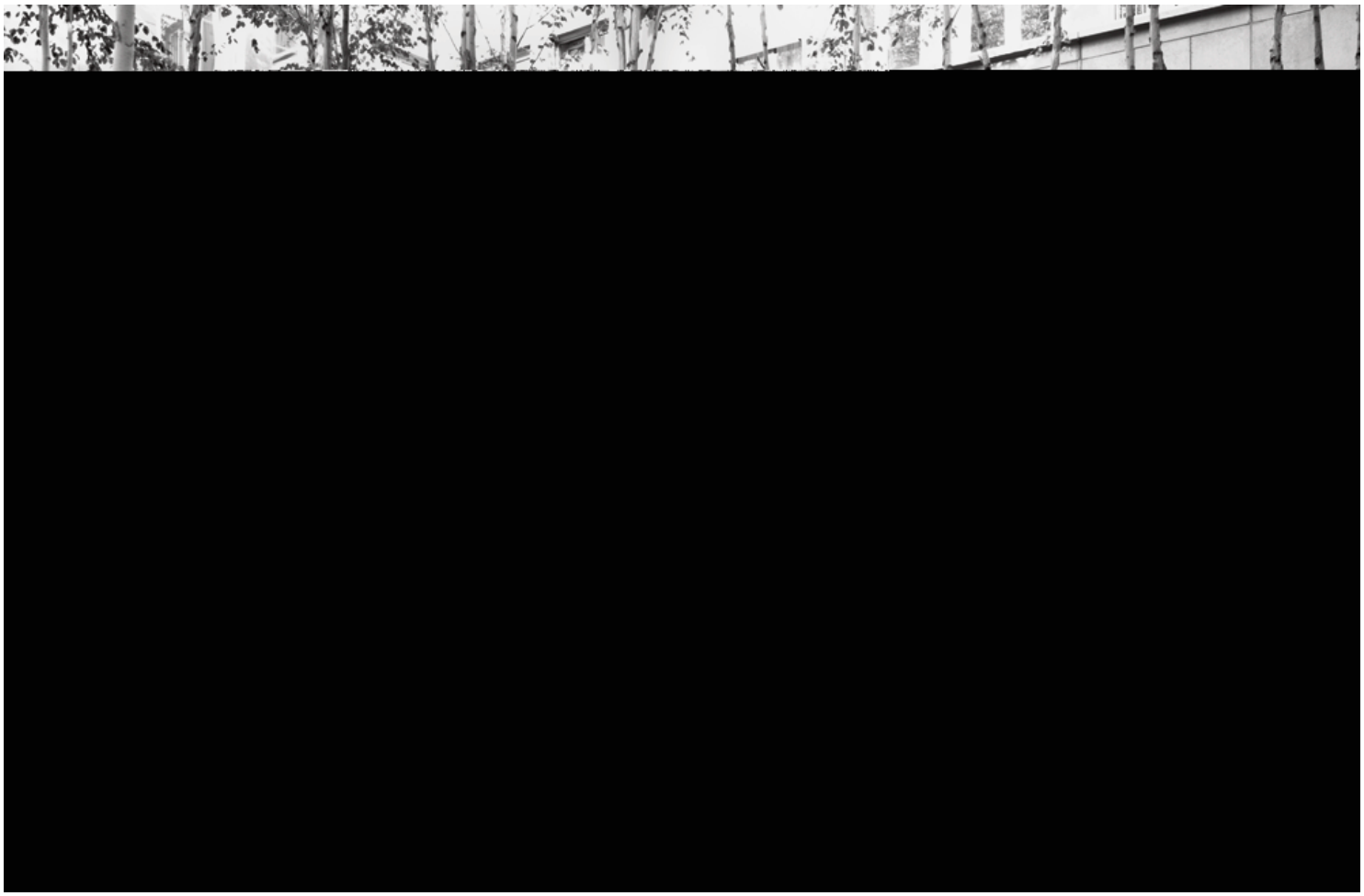
- Developing policies, strategies and strategic plans for approval by the Board of Directors and implementing those approved by the Board of Directors;
- Submitting to the Board of Directors and its committees proposed changes in management positions of material significance, investments, financial measures, acquisitions or divestitures, contracts of material significance and budgets;
- Preparing and submitting quarterly and annual reports to the Board of Directors or its committees;
- Informing the Board of Directors of all matters of fundamental significance to the businesses;
- Recruiting, appointing and promoting senior management;
- Ensuring the efficient operation of the Group and achievement of optimized results;
- Promoting an active internal and external communications policy; and
- Dealing with any other matters as are delegated by the Board of Directors to the Executive Committee.

THE CHIEF EXECUTIVE OFFICER

In addition to other duties that may be assigned by the Board of Directors, the Chief Executive Officer, supported by the Executive Committee, is responsible overall for the management and performance of the business, leads the Executive Committee, builds and maintains an effective executive team and represents Novartis with major customers, financial analysts, investors and with the media.

CONTRACTS WITH MEMBERS OF THE EXECUTIVE COMMITTEE

In accordance with good corporate governance, employment contracts with members of the Executive Committee do not contain unusually long notice periods, change-of-control clauses or severance payments.



From left to right: Juergen Brokatzky-Geiger, Naomi Kelman, Joseph Jimenez, Andrin Oswald, Mark C. Fishman, Felix R. Ehrat, George Gunn, Jonathan Symonds, Kevin Buehler, Jeff George, David Epstein

EXECUTIVE COMMITTEE

MEMBERS

American, age 52

German, age 59

American, age 54

Swiss, age 54

American, age 50

American, age 60

American, age 38

British, age 61

American, age 52

Swiss, age 40

British, age 52

SECRETARY

American, age 52

Joseph Jimenez has been Chief Executive Officer (CEO) of Novartis since 2010. Mr. Jimenez is responsible for leading the company's diversified healthcare portfolio of leading businesses in innovative pharmaceuticals, eye care, generics, vaccines and diagnostics, OTC and animal health. Previously Mr. Jimenez served as Division Head, Novartis Pharmaceuticals. He led the transformation of the pharmaceutical portfolio to balance mass market and specialty products, and significantly increased the percentage of sales from newly launched products. Mr. Jimenez also worked to realign the division's commercial approach to focus on the individual needs of customers, and incorporated more technological tools to better connect with patients and customers. Mr. Jimenez joined Novartis in April 2007 as Division Head, Novartis Consumer Health. Previously, he served as president and CEO of the North America business for the H.J. Heinz Co., and as president and CEO of Heinz in Europe from 2002 to 2006. Prior to joining Novartis, he was a nonexecutive director of AstraZeneca PLC, United Kingdom, from 2002 to 2007. He was also an advisor for the private equity organization Blackstone Group in the United States. Mr. Jimenez is a member of the board of directors of Colgate-Palmolive Co. He graduated in 1982 with a bachelor's degree from Stanford University and in 1984 with a Master of Business Administration from the University of California, Berkeley.

German, age 59

Juergen Brokatzky-Geiger, Ph.D., has been Head of Human Resources of Novartis since 2003. He is a member of the Executive Committee of Novartis. Mr. Brokatzky-Geiger joined Ciba-Geigy Ltd. in 1983 as a laboratory head in the Pharmaceuticals Division in Switzerland. After a job rotation in the United States, he held positions of increasing responsibility in Research and Development (R&D), including Group Leader of Process R&D, Head of Process R&D, and Head of Process Development and Pilot Plant Operations. During the merger of Ciba-Geigy and Sandoz in 1996, Mr. Brokatzky-Geiger was appointed Integration Officer of Technical Operations. He later became the Head of Chemical and Analytical Development, and served as the Global Head of Technical R&D from 1999 to 2003. Mr. Brokatzky-Geiger is a member of the board of Bachem AG. Mr. Brokatzky-Geiger graduated with a Ph.D. in chemistry from the University of Freiburg, Germany, in 1982.

American, age 54

Kevin Buehler has been Division Head, Alcon, since April 2011. He is a member of the Executive Committee of Novartis. Mr. Buehler was president and chief executive officer of Alcon Inc. from 2009 to 2011. He began his career with Alcon in 1984 as a regional sales manager in the Consumer Products Division, and held positions of increasing responsibility before being named director of sales and marketing. In 1996, he became director of Alcon's US Managed Care and Falcon Generic Pharmaceutical groups, and became vice president in 1998. The following year he returned to the US Consumer Products Division as vice president and general manager. Mr. Buehler moved to the International Division in 2002 as vice president and regional manager, Latin America and Caribbean. He was later named area vice president, Latin America, Canada, Australia and Far East. Mr. Buehler also served as senior vice president, global markets, and chief marketing officer. Prior to joining Alcon, he worked for The Gillette Co. and Snyder Drug Stores. Mr. Buehler holds a Bachelor of Science degree from Carroll University in Waukesha, Wis., in the United States, with concentrations in business administration and political science. He completed the Harvard Program for Management Development in 1993.

Swiss, age 54

Felix R. Ehrat, Ph.D., has been Group General Counsel and a permanent attendee of the Executive Committee of Novartis since October 2011. As of January 1, 2012, he is a full member of the Executive Committee. Mr. Ehrat is a leading practitioner of corporate, banking, and mergers and acquisitions law, as well as an expert in corporate governance and arbitration. He started his career as an associate with Baer & Karrer Ltd. in Zurich in 1987, became partner in 1992, and advanced to senior partner (2003 to 2011) and executive chairman of the board (2007 to 2011) of the firm. Mr. Ehrat is chairman of Globalance Bank AG in Switzerland, and a member of the board of Liechtensteinische Landesbank AG in Liechtenstein. Previously, Mr. Ehrat was chairman of Banca del Gottardo, and a board member of Julius Baer Holding AG, Austriamicrosystems AG, Charles Voegele Holding AG, and Carlo Gavazzi Holding AG. Mr. Ehrat was admitted to the Zurich bar in 1985 and received his doctorate of law from the University of Zurich in 1990. In 1986, he completed an LL.M. at McGeorge School of Law in the United States. His past memberships and positions include: the International Bar Association, where he was co-chair of the Committee on Corporate and M&A Law from 2007 to 2008; Association Internationale des Jeunes Avocats, where he was president from 1998 to 1999; and the Swiss Arbitration Association, the Zurich Bar Association, and the Swiss Bar Association.

American, age 50

David Epstein has been Division Head, Novartis Pharmaceuticals, since 2010. He also is responsible for Group Emerging Markets, a group of selected countries with integrated divisional businesses. He is a member of the Executive Committee of Novartis. Prior to his current appointment, Mr. Epstein served as Head of Novartis Oncology for nearly 10 years. In addition, Mr. Epstein led the Molecular Diagnostics Unit since its creation in 2008. Before joining Novartis, Mr. Epstein was an associate in the strategy practice of the consulting firm Booz Allen Hamilton Inc. in the United States. Mr. Epstein joined Sandoz, a predecessor company of Novartis, in 1989, and held various leadership positions of increasing responsibility for the company, including Chief Operating Officer of Novartis Pharmaceuticals Corporation in the United States and Head of Novartis Specialty Medicines. Mr. Epstein graduated with a bachelor's degree in pharmacy from Rutgers University College of Pharmacy in 1984, and with a Master of Business Administration in finance and marketing from New York's Columbia University Graduate School of Business in 1987.

American, age 60

Mark C. Fishman, M.D., has been President of the Novartis Institutes for BioMedical Research (NIBR) since 2002. He is a member of the Executive Committee of Novartis. Before joining Novartis in 2002, Dr. Fishman was chief of cardiology and director of the Cardiovascular Research Center at Massachusetts General Hospital, and was professor of medicine at Harvard Medical School, both in the United States. Dr. Fishman completed his internal medicine residency, chief residency and cardiology training at Massachusetts General Hospital. Dr. Fishman graduated with a bachelor's degree from Yale College in 1972 and an M.D. from Harvard Medical School in 1976. He has been honored with many awards and distinguished lectureships, and is a member of the Institute of Medicine of the National Academies and a Fellow of the American Academy of Arts and Sciences, both in the United States.

American, age 38

Jeff George has been Division Head, Sandoz, since 2008. He is a member of the Executive Committee of Novartis. Mr. George joined the Vaccines and Diagnostics Division of Novartis in 2007 as Head of Commercial Operations for Western and Eastern Europe. He then advanced to Head of Emerging Markets for the Middle East, Africa, Southeast Asia and CIS at Novartis Pharmaceuticals. Before joining Novartis, Mr. George was a Senior Director of Strategy and Business Development at Gap Inc., San Francisco, United States. From 2001 to 2004, he was an Engagement Manager with McKinsey & Company, also in San Francisco. Mr. George received a Master of Business Administration from Harvard University in 2001. He graduated in 1999 with a master's degree from The Johns Hopkins University's School of Advanced International Studies, where he studied international economics and emerging markets political economy. In 1996, he received his bachelor's degree in international relations from Carleton College in Northfield, Minn., in the United States.

British, age 61

George Gunn has been Division Head, Novartis Animal Health, and Head, Corporate Responsibility, since March 2011. He is a member of the Executive Committee of Novartis. Before joining Novartis, Mr. Gunn was president of Pharmacia Animal Health, based in the United States. Previously, he spent more than 15 years in positions of increasing responsibility in healthcare companies. He worked as a veterinary surgeon for nine years before joining the industry. Mr. Gunn joined Novartis in 2003 as Head of Novartis Animal Health, North America. In January 2004, he assumed his position as Head of the Animal Health Business Unit. In addition to this role, he was Division Head, Novartis Consumer Health, from 2008 to 2011. Mr. Gunn graduated with a bachelor of veterinary medicine and surgery degree from the Royal (Dick) School of Veterinary Studies in the United Kingdom in 1973. He graduated with a diploma in veterinary state medicine from the same school in 1978. In 2008, he received an honorary doctorate in veterinary medicine and surgery from the University of Edinburgh.

American, age 52

Naomi Kelman has been Division Head, Novartis OTC and a permanent attendee of the Executive Committee of Novartis since March 2011. As of January 1, 2012, she is a full member of the Executive Committee. Before joining Novartis, Ms. Kelman was president of LifeScan North America, part of the Johnson & Johnson Diabetes Care Franchise. Ms. Kelman joined Johnson & Johnson in 2000, and held several leadership roles within the Consumer as well as the Medical Device and Diagnostic sectors. She also was president of Johnson & Johnson Vision Care for the Americas. Prior to joining Johnson & Johnson, Ms. Kelman held positions of increasing responsibility at Bristol-Myers Squibb Co. in the Clairol Division, and oversaw expansion of some of the company's biggest consumer brands into the Europe, Middle East and Africa regions. Ms. Kelman also was managing director of the Matrix Essentials business for Europe and then vice president of marketing for the worldwide Matrix Essentials business. Prior to her time at Bristol-Myers Squibb, she worked in Finance at American Express Co. Ms. Kelman received both her bachelor's and Master of Business Administration degrees from Cornell University in the United States.

Swiss, age 40

Andrin Oswald, M.D., has been Division Head, Novartis Vaccines and Diagnostics, since 2008. He is a member of the Executive Committee of Novartis. Previously, Dr. Oswald was Chief Executive Officer (CEO) of Speedel Holding AG and Global Head of Pharmaceutical Development Franchises in the Novartis Pharmaceuticals Division, both in Switzerland. Dr. Oswald joined Novartis in 2005 as Assistant to the Chairman and CEO. Before his appointment as Head of Development Franchises, he served as Head of the Country Pharmaceuticals Organization (CPO) and Country President for Novartis in South Korea. Dr. Oswald joined Novartis from McKinsey & Company, Switzerland, where he was an associate principal. Between 2002 and 2003, he was a delegate of the International Committee of the Red Cross (ICRC) to Nepal. He holds a doctorate in medicine from the University of Geneva.

British, age 52

Jonathan Symonds has been Chief Financial Officer (CFO) of Novartis since 2010. He is a member of the Executive Committee of Novartis. Before joining Novartis in 2009, Mr. Symonds was partner and managing director of Goldman Sachs Group Inc. in the United Kingdom. He also has eight years of experience as CFO of AstraZeneca PLC, and previously held positions as Group Finance Director at Zeneca and partner at KPMG. From 2004 to 2007, Mr. Symonds was a director of Diageo PLC and chairman of the audit committee. Other previous roles include director and audit committee chairman of Qinetiq PLC, chairman of the 100 Group of Finance Directors, joint chairman of the Business Tax Forum, board member of the Accounting Standards Board, and founder of the Oxford University Centre for Business Taxation Research, all in the United Kingdom. Mr. Symonds graduated with a first class degree in business finance from the University of Hertfordshire, United Kingdom, in 1980, and became a Fellow of Chartered Accountants in 1982. He is a Commander of the British Empire (CBE).

THE INDEPENDENT EXTERNAL AUDITORS

DURATION OF THE MANDATE AND TERMS OF OFFICE

Based on a recommendation by the Audit and Compliance Committee, the Board of Directors nominates an independent auditor for election at the Annual General Meeting. PricewaterhouseCoopers (PwC) assumed its existing auditing mandate for Novartis in 1996. Peter Kartscher, auditor in charge, and Michael P. Nelligan, global relationship partner, began serving in their respective roles in 2009. The Audit and Compliance Committee ensures that the auditor in charge is rotated at least every five years.

INFORMATION TO THE BOARD OF DIRECTORS AND THE AUDIT AND COMPLIANCE COMMITTEE

The independent auditor, PwC, is responsible for opining on whether the audited consolidated financial statements comply with International Financial Reporting Standards (IFRS) and Swiss law and whether the separate parent company financial statements of Novartis AG comply with Swiss law. Additionally, PwC is responsible for opining on the effectiveness of internal control over financial reporting.

The Audit and Compliance Committee, acting on behalf of the Board of Directors, is responsible for overseeing the activities of PwC. During 2011, the Audit and Compliance Committee held 6 meetings. At each of these meetings, PwC was invited to attend during the discussion of agenda items that dealt with accounting, financial reporting or auditing matters and any other matters relevant for their audit.

On an annual basis, PwC provides to the Audit and Compliance Committee the written disclosures required by Rule 3526, "Communications with Audit Committees Concerning Independence," of the Public Company Accounting Oversight Board (PCAOB), and the Audit and Compliance Committee and PwC discuss PwC's independence from Novartis and Novartis' management.

The Audit and Compliance Committee recommended to the Board of Directors, and the Board of Directors approved, inclusion of the audited financial statements in the Annual Report for the year ended December 31, 2011.

The Audit and Compliance Committee, on a regular basis, evaluates the performance of PwC and, once yearly, based on a performance evaluation, recommends to the Board of Directors whether PwC should be proposed to the Annual General Meeting for election. Also, once yearly, the auditor in charge and the global relationship partner report to the Board of Directors on the activities of PwC during the current year and on the audit plan for the coming year and answer any questions or concerns Board members might have on the performance of PwC, or on the work PwC has conducted or is planning to conduct.

In order to assess the performance of PwC, the Audit and Compliance Committee requires a self-evaluation report from PwC, holds private meetings with the Chief Executive Officer, the Chief Financial Officer and with the Head of Internal Audit and, if necessary, obtains an independent external assessment. The Board of Directors also meets with the auditor in charge and the global relationship partner. Criteria applied for the performance assessment of PwC include technical and operational competence, independent and objective view, sufficient resources employed, focus on areas of significant risk to Novartis, willingness to probe and challenge, ability to provide effective, practical recommendations and open and effective communication and coordination with the Audit and Compliance Committee, the Internal Audit function and management.

PRE-APPROVAL OF AUDIT AND NON-AUDIT SERVICES

The Audit and Compliance Committee's pre-approval is required for all services provided by PwC. These services may include audit services, audit-related services, tax services and other services.

Pre-approval is detailed as to the particular services or categories of services, and is subject to a specific budget. PwC and management report, on a quarterly basis, to the Audit and Compliance Committee regarding the extent of services provided in accordance with this pre-approval and the fees for the services performed to date. The Audit and Compliance Committee may also pre-approve additional services on a case-by-case basis.

AUDITING AND ADDITIONAL FEES

PwC charged the following fees for professional services rendered for the 12-month periods ended December 31, 2011 and December 31, 2010:

	2011 USD thousands	2010 USD thousands
Audit Services	30 060	23 675
Audit-Related Services	2 480	2 140
Tax Services	1 550	1 485
Other Services	190	110
Total	**34 280**	**27 410**

Audit Services are defined as the standard audit work performed each year in order to issue opinions on the parent company and consolidated financial statements of the Group, to issue opinions relating to the effectiveness of the Group's internal controls over financial reporting, and to issue reports on local statutory financial statements. Also included are audit services that can only be provided by the Group auditor, such as auditing of non-recurring transactions and implementation of new accounting policies, audits of accounting infrastructure system controls, pre-issuance reviews of

quarterly financial results, consents and comfort letters and any other audit services required for SEC or other regulatory filings.

Audit-Related Services include those other assurance services provided by the independent auditor but not restricted to those that can only be provided by the auditor signing the audit report. They comprise amounts for services such as acquisition due diligence and related audits, audits of pension and benefit plans, IT infrastructure control assessments, contractual audits of third-party arrangements, assurance services on corporate citizenship reporting and compliance with corporate integrity agreements, and consultation regarding new accounting pronouncements.

Tax Services represent tax compliance, tax returns, assistance with historical tax matters and other tax-related services.

Other Services include training in the finance area, advice for process improvements, benchmarking studies, assessment of certain non-financial processes and license fees for use of accounting and other reporting guidance databases.

FURTHER INFORMATION

THE GROUP STRUCTURE OF NOVARTIS

NOVARTIS AG AND GROUP COMPANIES

Under Swiss company law, Novartis AG is organized as a corporation which has issued shares of common stock to investors. The registered office of Novartis AG is Lichtstrasse 35, CH-4056 Basel, Switzerland.

Business operations are conducted through Novartis Group companies. Novartis AG, a holding company, owns directly or indirectly all companies worldwide belonging to the Novartis Group. Except as described below, the shares of these companies are not publicly traded. The most important Novartis subsidiaries and associated companies are listed in Note 31 to the Group's consolidated financial statements.

DIVISIONS

The wholly-owned businesses of Novartis are divided on a worldwide basis into six operating divisions, Pharmaceuticals, Alcon (eye care), Vaccines and Diagnostics, Sandoz (generics), Over-the-Counter and Animal Health, and Corporate activities.

MAJORITY HOLDINGS IN PUBLICLY TRADED GROUP COMPANIES

76% of Novartis India Limited, with its registered office in Mumbai, India, and listed on the Bombay Stock Exchange (ISIN INE234A01025, symbol: HCBA). The total market value of the 24% free float of Novartis India Limited was USD 92.3 million at December 31, 2011, using the quoted market share price at the year end. Applying this share price to all the shares of the company the market capitalization of the whole company is USD 391.5 million.

SIGNIFICANT MINORITY HOLDINGS IN PUBLICLY TRADED COMPANIES

Novartis AG holds

- 33.3% of the bearer shares of Roche Holding AG, with its registered office in Basel, Switzerland, and listed on the SIX Swiss Exchange (Valor No. 1203211, ISIN CH0012032113, symbol: RO). The market value of the Group's interest in Roche Holding AG, as of December 31, 2011, was USD 9.45 billion. The total market value of Roche Holding AG was USD 147.4 billion. Novartis does not exercise control over Roche Holding AG, which is independently governed, managed and operated.
- 31.1% of Idenix Pharmaceuticals, Inc., with its registered office in Delaware, USA, and listed on NASDAQ (Valor No. 1630029, ISIN US45166R2040, symbol: IDIX). The total market value of the 66.48% free float of Idenix Pharmaceuticals, Inc. was USD 529.3 million at December 31, 2011, using the quoted market share price at the year end. Applying this share price to all the shares of the company the market capitalization of the whole company is USD 793.3 million. Novartis does not exercise control over Idenix Pharmaceuticals, Inc., which is independently governed, managed and operated.

INFORMATION OF OUR STAKEHOLDERS

INTRODUCTION

Novartis is committed to open and transparent communication with shareholders, financial analysts, customers, suppliers and other stakeholders. Novartis aims to disseminate material developments in its businesses in a broad and timely manner that complies with the rules of the SIX Swiss Exchange and the NYSE.

COMMUNICATIONS

Novartis publishes an Annual Report each year that provides information on the Group's results and operations. In addition to the Annual Report, Novartis prepares an annual report on Form 20-F that is filed with the SEC. Novartis discloses quarterly financial results in accordance with IFRS and issues press releases from time to time regarding developments in its businesses.

Novartis furnishes press releases relating to financial results and material events to the SEC via Form 6-K. An archive containing Annual Reports, annual reports on Form 20-F, and quarterly results releases, as well as related materials such as slide presentations and conference call webcasts, is on the Novartis Investor Relations website (www.novartis.com/investors). The archive is available on the Novartis website:
http://www.novartis.com/newsroom/media-releases/index.shtml

Information contained in reports and releases issued by Novartis is only correct and accurate at the time of release. Novartis does not update past releases to reflect subsequent events and advises against relying on them for current information.

INVESTOR RELATIONS PROGRAM

An Investor Relations team manages the Group's interaction with the international financial community. Several events are held each year to provide institutional investors and analysts various opportunities to learn more about Novartis.

Investor Relations is based at the Group's headquarters in Basel, Switzerland. A part of the team is located in New York to coordinate interaction with US investors. Information is available on the Novartis website: www.novartis.com/investors. Investors are also welcome to subscribe to a free e-mail service on this site.

WEBSITE INFORMATION

Topic	Information
Share Capital	Articles of Incorporation of Novartis AG http://www.novartis.com/corporate-governance Novartis key share data http://www.novartis.com/key-share-data
Shareholder Rights	Articles of Incorporation of Novartis AG http://www.novartis.com/corporate-governance Investor Relations information http://www.novartis.com/investors
Board Regulations	Board Regulations http://www.novartis.com/corporate-governance
Executive Committee	Executive Committee http://www.novartis.com/executive-committee
Novartis Code for Senior Financial Officers	Novartis Code of Ethical Conduct for CEO and Senior Financial Officers http://www.novartis.com/corporate-governance
Additional Information	Novartis Investor Relations http://www.novartis.com/investors

ANDRINA WATTS:

COMPENSATION REPORT

Novartis aspires to be an employer of choice and to attract and retain best-in-class talents around the world.

Our compensation plans are designed to support our goal as a preeminent global healthcare company. They provide competitive compensation and benefits for world-class talents in a competitive market. They are aligned with our business performance objectives that are key to our sustained success while being transparent, coherent and aligned with our pay-for-performance philosophy. Our compensation system aims to encourage entrepreneurship and, at the same time, deter excessive risk-taking to enhance short-term financial gain at the expense of the long-term health of the Group.

The Compensation Report describes our compensation system, including our compensation philosophy, details on the compensation plans and the compensation paid for 2011 performance.

CONTENTS

2011 ACTIONS OF NOVARTIS AND OF THE COMPENSATION COMMITTEE

We seek to constantly innovate, to discover and develop important new medicines and vaccines, and to market them successfully to our customers. We abide by regulatory and legal requirements and operate in an ethical and transparent manner. The health benefits we offer to our consumers are our primary concern, and we put their health and safety ahead of any financial considerations. These values are embedded in the way we hire, train and compensate our employees throughout Novartis. Our compensation programs reinforce employee performance that is consistent with our purpose and aspirations and discourage behavior that is inconsistent with our values and expectations.

We consider excellent performance central to the way we do business. Best-in-class innovation helps patients and creates sustainable returns and long-term value, which in turn allow us to adequately reward our employees and shareholders, and pay taxes. Our compensation system incentivizes our organization to thrive and perform in the short and long-term without taking imprudent or unreasonable risks. Yet, the business environment ahead of us will become even more challenging. The healthcare industry is currently facing a number of critical challenges, such as the uncertainties surrounding the global debt crisis, recent substantial regulatory changes and price cuts. Simultaneously, global competition in the healthcare industry and the pressure for realizing efficiencies are increasing even further.

We are convinced that the best answer to these challenges is to focus on our primary purpose and core values and to invest to continuously deliver innovative or best price solutions for patients and customers. This also requires an increasing attention to our business efficiency and cost effectiveness. A compensation system that allows Novartis to attract the best-in-class talent and motivates associates to perform to their full potential is critical for sustainable value creation, ethical business behavior and appropriate risk taking. It also aligns the interests of our employees with those of our shareholders and stakeholders.

We intend to keep our compensation system at a state-of-the-art level and to maintain a dialogue with our stakeholders. As a result, we regularly review our compensation system, taking into account the interests and feedback of our stakeholders. This entails trade-offs, as frequent changes of the compensation system create confusion internally and externally. In our experience it takes 3 to 5 years until a large organization as ours fully understands and aligns behind a new approach.

At the 2011 Annual General Meeting, Novartis shareholders were invited to express their views on our compensation system through a consultative vote (a so-called "say on pay" vote). A majority of Novartis shareholders supported our current compensation system. We also had an opportunity to collect valuable remarks and comments in relation to our compensation system. In addition, management met with our stakeholders to engage in a fruitful dialogue after the 2011 Annual General Meeting.

On the basis of the preparatory work done by the Compensation Committee and the Corporate Governance and Nomination Committee, the Board of Directors noted and thoroughly analyzed the comments made by our shareholders in relation to the 2010 Compensation Report, with a view to identifying potential enhancements to the design, operation and disclosure of our compensation system. As a result, we have decided to further promote the long-term orientation, transparency and governance of our compensation system by taking the following steps:

- We decided to further increase comparability by providing the value of the shares and other equity instruments used for compensation purposes at the undiscounted market value used in preparing the Group's consolidated financial statements, despite the fact that they are subject to multi-year vesting periods;
- For members of the Executive Committee, the Compensation Committee shifted the weighting of awards under its Equity Plan "Select" toward performance vesting through its Long-Term Performance Plan. For 2011, this shift between these two plans represented a reduction of the awards under the Equity Plan "Select" by 33% on average;
- We harmonized the vesting period for participants of the equity plan "Select" by increasing it to three years globally;
- We decided to disclose the actual duration of the CEO's notice period, which is 12 months; and
- The Compensation Committee Charter was amended to reinforce the importance of risk management in our compensation system.

The Board of Directors believes that the compensation system is appropriate for Novartis given the Company's objectives. Moreover, the Compensation Committee confirms that Novartis compensation plans for all associates (including for the Chief Executive Officer and Executive Committee members) are aligned with the healthcare industry practice.

The Members of the Compensation Committee
Marjorie M.T. Yang (chair)
William Brody
Srikant Datar
Ulrich Lehner
Enrico Vanni

For further information on the Compensation Committee organization and responsibilities, see Corporate Governance Report – Our Board of Directors – Role of the Board of Directors and the Board Committees – The Compensation Committee.

COMPENSATION OF THE BOARD OF DIRECTORS

PHILOSOPHY FOR THE BOARD OF DIRECTORS COMPENSATION

Today, the members of boards of directors of global companies face increasing responsibilities and have to deal with issues that require ever higher levels of expertise and engagement. As a global healthcare company, Novartis has appointed members of the Board of Directors who bring these required skills. Novartis has set the compensation for the members of the Board of Directors at a level that allows for the attraction and retention of high-caliber members. The members of its Board of Directors do not receive variable compensation, underscoring their focus on long-term corporate strategy, supervision and governance.

COMPENSATION STRUCTURE

	Board compensation
Fixed compensation	Yes
Variable compensation	No

COMPENSATION OF THE MEMBERS OF THE BOARD OF DIRECTORS

The Board of Directors determines the compensation of its members each year, based on a proposal by the Compensation Committee.

The compensation of the Chairman is based on a contract, which provides for Dr. Daniel Vasella a fixed remuneration of CHF 12.2 million, indexed to the average compensation increase for associates based in Switzerland. One third of his total compensation is paid out in monthly cash installments; the remaining two-thirds are in the form of unrestricted Novartis shares that are granted to him each year at the closing market price of the underlying share at the end of the day at grant date, in 2011 on January 19, 2011. Following his term as Chairman, Dr. Vasella agreed to continue to make available his know-how to Novartis and to refrain from activities that compete with any business of Novartis for a multi-year period. Dr. Vasella will receive fair market compensation in return for his services and for complying with the restriction not to compete. Dr. Vasella carries forward tradable options, shares and benefits (including pension) as a result of his 14-year tenure as our CEO. In his current capacity he receives no variable compensation, tradable options or equity other than the shares that are part of his retainer as Chairman.

The other members of the Board of Directors receive an annual fixed Board membership fee and additional fees for committee chairmanships, committee memberships, and other functions to compensate for their increased responsibilities and engagements. They do not receive additional fees for attending meetings. With the exception of the Chairman, the members of the Board of Directors can choose to receive their fees in cash, shares, or a combination of both and they receive neither share options nor pension benefits.

The fee rates for Board membership and functional roles of other members of the Board of Directors are as follows:

BOARD MEMBER ANNUAL FEE RATES (EXCL. CHAIRMAN)

	Annual fee (CHF)
Board membership	350 000
Vice Chairman	350 000
Board Committee chairmanship	10 000
Chairman's Committee membership	150 000
Audit and Compliance Committee membership	100 000
Risk Committee membership	50 000
Compensation Committee membership	50 000
Corporate Governance and Nomination Committee membership	50 000
Delegated board membership[1]	125 000

[1] The Board of Directors has delegated Rolf M. Zinkernagel to the Scientific Advisory Board of the Novartis Institute for Tropical Diseases (NITD). The Board of Directors has delegated both Rolf M. Zinkernagel and William Brody to the Board of Directors of the Genomics Institute of the Novartis Research Foundation (GNF).

BENCHMARK

The level of pay for the members of the Board of Directors is set based on benchmarks that include the remuneration of members of board of directors of comparable healthcare companies (see also the list of benchmark companies under "Compensation of Executives and other associates – Competitive Positioning", p.126) and selected leading Swiss companies (i.e. UBS, Nestlé and Credit Suisse).

BOARD MEMBER COMPENSATION IN 2011[1]

	Board membership	Vice Chairman	Chairman's Committee	Audit and Compliance Committee	Risk Committee	Compensation Committee	Corporate Governance and Nomination Committee	Delegated board membership	Annual cash compensation (CHF) (A)	Shares (Market value) (CHF) (B)[2]	Shares (Number)	Shares (Tax value)[3]	Other (CHF) (C)	Total (CHF) (A)+(B)+(C)
Daniel Vasella	Chair		Chair	•[4]	•[4]	•[4]	•[4]		4 060 004	8 786 735[5]	160 635[5]	4 906 425[5]	654 207[6]	13 500 946[8]
Ulrich Lehner	•	•	•	•	•	•	Chair		1 110 000	–	–	–	62 650[7]	1 172 650
William Brody[9]	•					•		•	229 688	295 325	5 399	295 325	–	525 013
Srikant Datar	•		•	Chair	•	•			550 250	159 779	2 921	159 779	–	710 029
Ann Fudge	•				•		•		450 000	–	–	–	–	450 000
Pierre Landolt[10]	•						•		106 000	294 013	5 375	294 013	24 177[7]	424 190
Enrico Vanni	•			•		•			425 000	75 048	1 372	75 048	29 404[7]	529 452[8]
Andreas von Planta	•			•	Chair		•		448 000	112 026	2 048	83 712	32 685[7]	592 711
Wendelin Wiedeking	•			•	•				132 500	367 529	6 719	367 529	30 965[7]	530 994
Marjorie M.T. Yang	•					Chair			410 000	–	–	–	24 719[7]	434 719
Rolf M. Zinkernagel[11]	•						•	•	–	650 000	11 883	650 000	34 381[7]	684 381
Total[12]									**7 921 442**	**10 740 454**	**196 352**	**6 831 831**	**893 188**	**19 555 084**

See note 12 to the Financial Statements of Novartis AG for 2010 data.

[1] Does not include reimbursement for travel and other necessary business expenses incurred in the performance of their services as these are not compensation.

[2] The value of the shares reflected in this column has been calculated based on market value of the shares at grant date. All shares were granted as per January 19, 2011 against the prevailing share price of CHF 54.70.

[3] A Board member who is tax resident in Switzerland can voluntarily choose to block the shares. In 2011 Daniel Vasella blocked his shares for ten years and Andreas von Planta for five years. The value of the shares reflected in this column has been calculated using the tax value methodology described under - 2011 Compensation of the Executive Committee Members - Compensation in 2011 - Valuation Principles.

[4] Daniel Vasella attended the meetings of these Committees as a guest without voting rights.

[5] Includes 12 188 shares paid in 2011 related to the grant of 2010.

[6] Includes social security costs due by the individual and paid by the company, pension and life insurance.

[7] Includes social security costs due by the individual and paid by the company.

[8] Does not include Board member compensation granted by Alcon, Inc. until April 8, 2011.

[9] The Board of Directors has delegated William Brody to the Board of Directors of the Genomics Institute of the Novartis Research Foundation (GNF).

[10] According to Pierre Landolt, the Sandoz Family Foundation is the economic beneficiary of the compensation.

[11] The Board of Directors has delegated Rolf M. Zinkernagel to the Scientific Advisory Board of the Novartis Institute for Tropical Diseases (NITD) and to the Board of Directors of the Genomics Institute of the Novartis Research Foundation (GNF).

[12] Alexandre F. Jetzer-Chung and Hans-Jörg Rudloff were members of the Board of Directors until February 22, 2011. Their compensation was reported in the 2010 Annual Report.

SHARES AND SHARE OPTIONS OWNED BY MEMBERS OF THE BOARD OF DIRECTORS

Shareholders want Board members to align their interests with the rest of the shareholders. Among other requirements, the members of the Board of Directors are thus required to own at least 5 000 Novartis shares within three years after joining the Board of Directors. As of December 31, 2011, all members of the Board of Directors who have served at least three years on the Board of Directors have complied with the share ownership guidelines.

The last year in which Novartis granted share options to non-executive members of the Board of Directors was 2002. The total number of vested and unvested Novartis shares and share options owned by members of the Board of Directors and "persons closely linked"[1] to them as of January 19, 2012, is shown in the following tables.

As of January 19, 2012, none of the members of the Board of Directors together with "persons closely linked"[1] to them owned 1% or more of the outstanding shares of Novartis, either directly or through share options.

[1] "Persons closely linked" are (i) their spouse, (ii) their children below age 18, (iii) any legal entities that they own or otherwise control, and (iv) any legal or natural person who is acting as their fiduciary.

SHARES OWNED BY BOARD MEMBERS

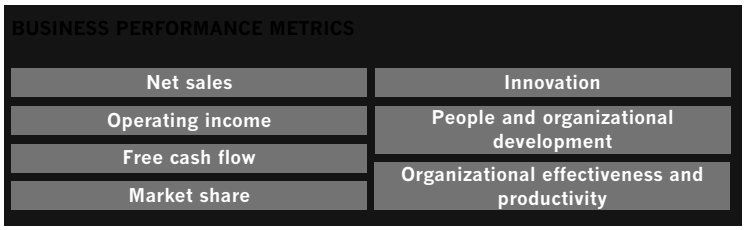
	Number of shares[1,2]
Daniel Vasella	

ers and debt holders) (see also Note 26 to the Group's audited consolidated financial statements for information regarding the NVA).

Objective setting for members of the Executive Committee and associates

At the beginning of each performance year, the CEO and each of the executives directly reporting to him determine together the business objectives and respective metrics applicable to each of the divisional and global functional leaders. In the same manner, each line manager and each associate directly reporting to her or him set the objective and metrics applicable to the next-level associate. As a principle, all written objectives are reviewed by two hierarchical levels, including the direct and the indirect supervisors.

The business objectives are measured against key performance metrics, while the individual performance is derived from the business objectives established at the Group, division, function, country or business area levels.



These financial and operational metrics have been selected because they define in a balanced way how successful we are in meeting our strategic objectives and creating sustainable value to our shareholders.

Depending on functional responsibility, non-financial objectives typically include research and development performance; product launches; successful implementation of growth and productivity initiatives; process improvements; leadership and people management and successful acquisitions, disposals and licensing transactions.

Objectives are set each year at ambitious levels to motivate a high degree of business performance appropriately balancing the short- and long-term objectives.

Decisions and actions leading to results must be consistent with Novartis Values and Behaviors, which describe the desired conduct of associates and set boundaries and guidelines as an important building block for the culture of our Group. The Novartis Values and Behaviors provide a focus on quality, commitment, candor, compassion, loyalty and integrity.

Novartis does not disclose specific business objectives for the upcoming year because they often constitute business secrets, the disclosure of which would signal areas of strategic focus and impair the Group's ability to leverage these areas for competitive advantage. For example, disclosure of our cash-flow objectives would provide insight into timing of large capital investments or acquisitions. In addition, knowledge of the objectives could be used by competitors to recruit key executives from Novartis. Disclosing specific objectives and metrics would also give our competitors insight into key market dynamics and areas that could be used against Novartis competitively by industry consultants or competitors targeting existing customers.

PERFORMANCE EVALUATION

Our performance management system and "pay for performance" principle have spurred a culture of meritocracy at Novartis. We believe that pay for performance is only sustainable when fair performance evaluation procedures ensuring integrity and fairness are in place. Performance evaluation is conducted at all levels of the organization.

The people performance management evaluation process consists of two reviews per year – a mid-year and a year-end review. During such formal meetings, associates and managers evaluate performance against the objectives set at the beginning of the year. In assessing performance, managers focus on results-oriented measures, as well as on how results were achieved. The "four eyes" rule ensures that associates' annual objectives and performance evaluations are reviewed separately by two levels of supervisors.

Process for performance evaluation of the CEO

At the end of a business year, the CEO prepares and presents to the Chairman and the Board of Directors a self-appraisal assessing actual results against the previously agreed-upon objectives, taking into account the audited financial results as well as Novartis Values and Behaviors. Subsequently, the Board of Directors discusses the self-appraisal without the CEO being present. It evaluates the extent to which targeted objectives have been achieved and, to the extent possible, compares these results with peer industry companies, taking into account general economic and financial criteria and industry developments. The Board of Directors later shares its appraisal with the CEO.

Process for performance evaluation of members of the Executive Committee

In January, the Board of Directors meets with the CEO to review and discuss the performance and objectives of the Executive Committee members for the previous year, taking into account the financial results, the level of achievement of financial and non-financial objectives, as well as Novartis Values and Behaviors and the general economic and business environment. In addition to the year-end review, the mid-year performance of the CEO is reviewed by the Chairman while the results of the other Executive Committee members are evaluated by the CEO and then discussed with the Chairman.

Talent Review

Our People Performance Management evaluation process is complemented with an annual Organization and Talent Review in which organizational needs and career aspirations of associates are discussed. The review includes the assessment of strengths, weaknesses and potential for growth. The Organization and Talent Review has become an integral tool for top management in succession planning, and the scope of the program has steadily expanded from a few dozen executives a decade ago to almost 25 000 prospective leaders today.

Because performance appraisals impact significant elements of reward, we ensure each year that there is consistency of performance ratings across the entire Group.

COMPENSATION DETERMINATION

Compensation determination for the CEO

Based on the performance evaluation appraisal made by the Board of Directors, the Compensation Committee decides at its January meeting on the CEO's total compensation and the target compensation for the coming year without the presence of the CEO. In reaching its decision, the Compensation Committee takes into account other relevant factors, including available benchmark information and the advice of the Compensation Committee advisor.

Compensation determination for the Executive Committee members

In the presence of the CEO and based on his recommendations, the Compensation Committee decides on the variable compensation for the other Executive Committee members and other selected key executives for the previous year. At the same meeting, the Compensation Committee decides on the target compensation for these executives for the coming year.

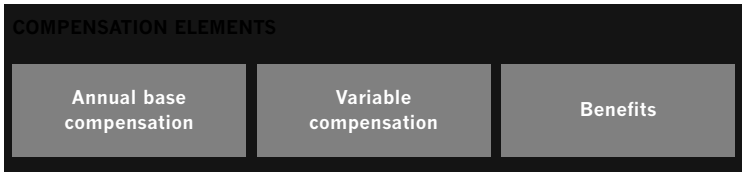
Compensation determination for other associates

Based on the year-end performance rating, line managers and next-level line managers determine the incentive awards for each associate under review, as well as the target compensation for the coming year. The Compensation Committee determines the grants for all equity compensation plans in aggregate.

ELEMENTS OF OUR COMPENSATION PROGRAMS

The primary elements of our compensation system are:

– Annual base compensation – A fixed annual salary
– Variable compensation – Rewards for individual and business performance
– Benefits – Including pension and healthcare benefits



ANNUAL BASE COMPENSATION (SALARY)

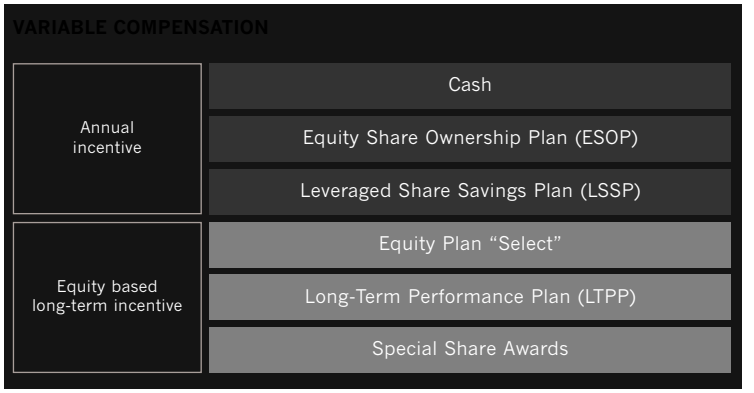
The level of base compensation reflects each associate's key areas of responsibilities, job characteristics, seniority, experience and skill sets. It is paid in cash, typically monthly, and is set according to local practice, designed to provide our associates with fixed compensation to ensure a reasonable standard of living relative to that offered by our peer companies.

In general, base compensation is reviewed annually to ensure that competitive pay is maintained.

VARIABLE COMPENSATION

The goal of variable compensation is to reward Novartis associates according to their performance and in a manner consistent with the "pay for performance" principle.

At lower levels, variable compensation is paid in cash, while at managerial levels, variable compensation is generally composed of annual cash incentive and an equity based long-term incentive. Novartis believes that variable compensation should specifically emphasize long-term incentives to align the interests of our associates with those of long-term shareholders. This also reflects the crucial importance of innovation and the long product development and commercialization cycles that characterize our industry. The amount of variable compensation is based on results and calculated as a percentage (0-200%) of target variable compensation.



ANNUAL INCENTIVE

The annual incentive ensures that the associates focus on individual objectives and objectives defined by the business over a single financial year. These objectives include objectives as market share, innovation, and people management, which also positively influence the long-term performance. It rewards performance in the last 12 months in relation to these objectives and reinforces the "pay for performance" principle.

In principle, the annual incentive is paid in cash and is capped at 200% of target. However, a number of associates in certain countries and certain key executives worldwide are encouraged to invest their annual incentive in a share savings plan. Under the share savings plan, they will receive their annual incentive awards fully or partially in Novartis shares in lieu of cash. As a reward for their participation in the share savings plan, Novartis matches their investments in shares after a holding period of three or five years. As a rule, no shares are matched under these plans if an associate leaves Novartis prior to the expiration of the holding period for reasons other than retirement, disability or death. Thus, through the participation in the share savings plan our associates are incentivized to remain with Novartis in the long-term, while sharing in the future financial success of Novartis and further aligning with the long-term interests of our shareholders.

Novartis currently has three share savings plans:

– *Employee Share Ownership Plan (ESOP):* In Switzerland, the ESOP is available to about 12 688 associates. Participants within this plan may choose to receive the incentive (i) 100% in shares, (ii) 50% in shares and 50% in cash or (iii) 100% in cash. After expiration of a three-year holding period of Novartis shares invested under the ESOP, each participant will receive one free matching share for every two Novartis shares invested. A total of 5 050 associates chose to receive shares under the ESOP for their performance in 2011.
– *United Kingdom Plan*: In the United Kingdom, 2 790 associates can invest up to 5% of their monthly salary in shares (up to a maximum of GBP 125) and also may be invited to invest all or part of their net annual incentive in shares. Two invested shares are matched with one share with a holding period of three years. During 2011, about 1 870 associates elected to participate in this plan.
– *Leveraged Share Savings Plan (LSSP)*: Worldwide 30 key executives were invited to participate in a leveraged share savings plan based on their performance in 2011. Instead of cash, their annual incentive was awarded in shares and subject to a holding period of five years. At the end of the holding period, Novartis will match the invested shares at a ratio of 1-to-1 (i.e. one share awarded for each invested share).

Associates may only participate in only one of these plans in any given year.

EQUITY BASED INCENTIVES

The long-term incentive is designed to focus on our objective of long-term sustainable shareholder value creation and to support our "pay for performance" principle by using equity based compensation with a three year vesting period.

These long-term incentives awarded by Novartis aim at retaining our key talents, encouraging the realization of multi-year business objectives and aligning our associates with our shareholders' interests by tying the value realized to the change in the share price at vesting.

The equity based long-term incentive is subject to the achievement of predetermined performance objectives either at grant or at vesting.

Novartis offers two long-term incentive plans, the Equity Plan "Select" based on yearly results with a vesting period of three years and the Long-Term Performance Plan based on the average results of a three-year period.

In exceptional cases, Novartis may also grant special share awards.

Equity Plan "Select"

The Equity Plan "Select" is a global equity incentive plan under which all associates, including Executive Committee members, may annually be eligible for a grant, which is capped at 200% of target. The Equity Plan "Select" allows its participants to choose the form of their equity compensation in restricted shares (or, in some jurisdictions, RSUs[1]), tradable share options, or a combination of both, with a vesting period of three years.

Tradable share options expire on their 10th anniversary from grant date. Each tradable share option granted to associates entitles the holder to purchase after vesting (and before the 10th anniversary from grant date) one Novartis share at a stated exercise price that equals the closing market price of the underlying share at the grant date January 19, 2012.

[1] In some jurisdictions, RSUs are granted rather than shares. Each RSU is equivalent in value to one Novartis share and is converted into one share at the vesting date. RSUs do not carry any dividend or voting rights, except for USA where employees receive a dividend equivalent during the vesting period for 2009 and 2010 grants. Each restricted share is entitled to voting rights and payment of dividends during the vesting period.

The terms of the tradable share options granted since 2008 are shown in the table below.

TERMS OF SHARE OPTIONS

Grant year	Exercise price (CHF/USD)	Vesting (years) (CH/other countries)	Term (years)
2012	54.20/58.33	3/3	10
2011	54.70/57.07	2/3	10
2010	55.85/53.70	2/3	10
2009	53.65/46.42	2/3	10
2008	64.05/57.96	2/3	10

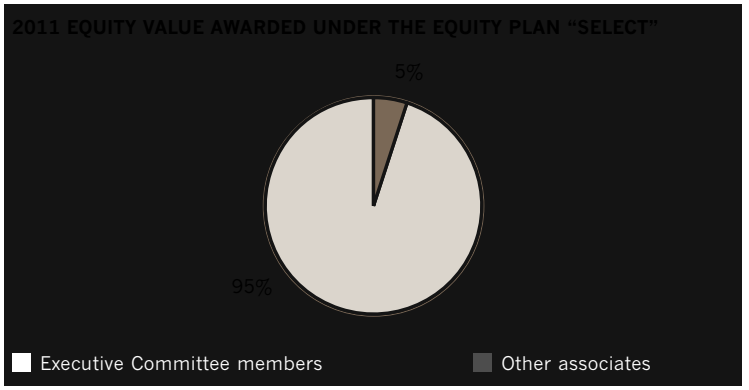
If a participant leaves Novartis for reasons other than retirement, disability or death, unvested shares, RSUs and share options are forfeited, unless determined otherwise by the Compensation Committee (for example, in connection with a reorganization or divestment). In Switzerland, the participants in this plan can choose between restricted shares or RSUs and tradable share options, or a combination of both.

A total of 12 768 participants received 1.0 million restricted shares, 6.5 million RSUs and 23.9 million tradable share options under the Novartis Equity Plan "Select" for their performance in 2011, representing a participation rate of about 10% of all full-time-equivalent associates worldwide.

As of December 31, 2011, 94 million tradable share options granted to associates were outstanding, covered by an equal number of shares and corresponding to 3.9% of the total number of outstanding Novartis shares.

Approximately 5% of the total equity value awarded under the Equity Plan "Select" was granted to the members of the Executive Committee.

2011 EQUITY VALUE AWARDED UNDER THE EQUITY PLAN "SELECT"



Long-Term Performance Plan

The Long-Term Performance Plan (LTPP) is an equity plan for key executives designed to foster long-term commitment by aligning the incentives of key executives to the performance of Novartis. The LTPP is offered to selected executives, who are in key positions and have a significant impact on the long-term success of Novartis. It is capped at 200% of target. For members of the Executive Committee, LTPP represents between 20% and 45% of their total variable compensation at target. The rewards are based on pre-determined rolling three year global performance objectives focused on the Novartis Economic Value Added (NVA) measured annually. The NVA is calculated based on Group operating income adjusted for interest, taxes and cost of capital charge. The performance realization of a plan cycle is obtained right after the end of the third plan year by adding together the annual NVA realizations of all plan years of the plan cycle. The performance ratio for a plan cycle is obtained by dividing the performance realization for the plan cycle with the performance target for the plan cycle, expressing the result as a percentage. The LTPP only allows a payout if the actual NVA exceeds predetermined target thresholds.

To support the alignment of our Executive Committee members' interests with those of the Group and our shareholders, the Long-Term Performance Plan represents a substantial and increasing fraction of Executive Committee members' variable compensation targets relative to incentives based on performance during a single year.

On January 19, 2012, 138 key executives were awarded 464 230 shares under the Long-Term Performance Plan, based on NVA achievement that exceeded our target performance for the performance period 2009 to 2011.

LONG-TERM PERFORMANCE PLAN PARTICIPANTS HISTORY

Grant year = Target setting	Performance period	Award year = Payout in shares	Plan participants (number of key executives)
2012	2012–2014	2015	139
2011	2011–2013	2014	139
2010	2010–2012	2013	142
2009	**2009–2011**	**2012**	**138**
2008	2008–2010	2011	117

VARIABLE COMPENSATION TARGET AND AWARD CALCULATION FORMULA

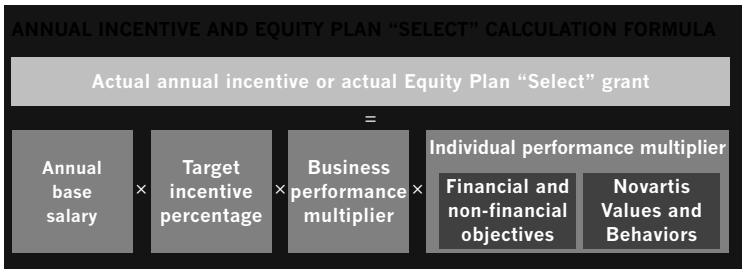
Annual incentive and Equity Plan "Select"

Under these plans, Novartis defines a target incentive as a percent of base compensation for each participating associate at the beginning of each performance period – traditionally the start of a calendar year. Depending on the role and the level of responsibility of the associates, target incentive percentages may reach up to 60% of

base compensation for the annual incentive and 200% for the Equity Plan "Select".

The amount of the incentive under both the annual incentive and the Equity Plan "Select" is determined on the basis of business and individual performance. No awards are granted for performance ratings below a certain threshold.

The Award Calculation Formula under both the annual incentive and the Equity Plan "Select" is the following:



The business and the individual performance multipliers have thus an equivalent weighting in the formula. The business performance multiplier is based on the performance of the Group or business area and may range from zero to 1.5.

The individual performance multiplier is based on achievement of individually set financial and non-financial objectives as well as meeting key behavioral standards, the Novartis Values and Behaviors. It may range from zero to 1.5. For the purpose of calculating the individual performance multiplier, the individually set financial and non-financial objectives and the Novartis Values and Behaviors have an equivalent weighting.

The business performance multiplier, combined with the individual performance multiplier, is subject to a cap at 200% of the target incentive.

This broad range of incentive percentages and multipliers allows for meaningful differentiation on a "pay for performance" basis.

For those who have chosen to receive their annual incentive under the ESOPs or LSSP plans, as well as for those receiving awards under the Equity Plan "Select" the number of shares awarded is determined by dividing the actual incentive amount by the closing price of the shares on the grant date. In North America, if associates choose to receive part or all of their grant under the Equity Plan "Select" in tradable share options on American Depositary Shares (ADSs), the resulting number of tradable share options is determined by dividing the respective incentive amount by a value that equals 95% of the value of the options on ADSs as determined in accordance with International Financial Reporting Standards (IFRS). For associates in other countries, the divisor equals 90% of the IFRS value of options on shares.

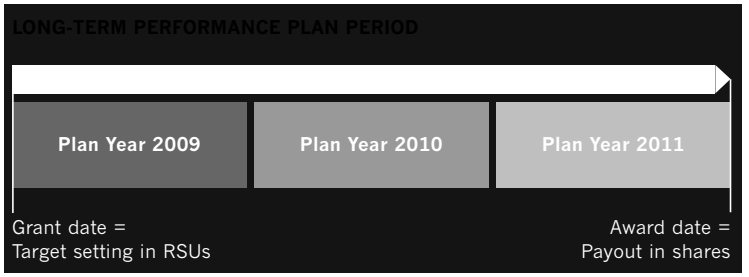
Typically, the annual incentive is paid out in February following the realization of the yearly objectives.

The three-year vesting of the Equity Plan "Select" is contingent on continued employment with Novartis.

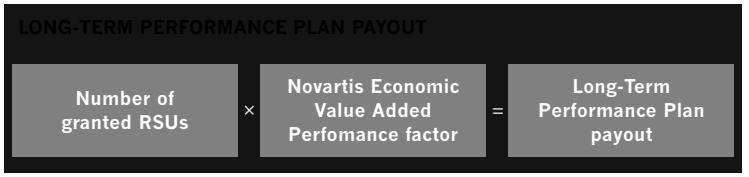
Long-Term Performance Plan

In the case of the LTPP, the performance objective (NVA) is determined over a three-year period commencing on January 1 of each grant year.

At the beginning of the performance period, plan participants are allocated RSUs, which will be converted into Novartis shares after the performance period.



At the end of the three-year performance period, the Compensation Committee adjusts the number of RSUs earned based on actual performance. RSUs are converted into unrestricted Novartis shares without an additional vesting period. In the United States, awards may also be delivered in cash under the US deferred compensation plan.



Depending on the role and the level of responsibility of the associates, the target incentive percentages may reach up to 175% of base compensation for LTPP. For outstanding NVA performance, the adjustment can go up to a maximum of 200% of the target incentive. No incentive is awarded if actual NVA performance fails to meet a predetermined threshold (or if the participant leaves Novartis during the performance period for reasons other than retirement, disability or death).

SPECIAL SHARE AWARDS

Selected associates may exceptionally receive special awards of restricted shares or RSUs. These Special Share Awards provide an opportunity to reward outstanding achievements or exceptional performance and aim at retaining key contributors. They are based

on a formal internal selection process, in which the individual performance of each candidate is thoroughly assessed at several management levels. In addition, Special Share Awards may also be granted to attract special expertise and new talents into the organization. These grants are consistent with the Novartis philosophy to attract, retain and motivate best-in-class talents around the world.

Restricted special awards generally have a five-year vesting period. If an associate leaves Novartis for reasons other than retirement, disability or death, unvested shares or RSUs are generally forfeited. Worldwide 597 associates at different levels in the organization were awarded a total of 1.5 million shares or RSUs in 2011.

SOURCE OF AWARDED SHARES

Novartis uses shares repurchased in the market to fulfill obligations to deliver shares as required by the variable compensation plans and special share awards, thus avoiding any dilution of shareholders.

Novartis does not have any approved conditional capital to obtain shares for delivery of our share awards.

BENEFITS

The primary purpose of pension and healthcare plans is to establish a level of security for associates and their dependents with respect to age, health, disability and death. The level of pension and healthcare benefits provided to associates is country-specific and influenced by local market practice and regulations, and is reviewed regularly.

The Group has a policy to change from defined-benefit pension plans (DB) to defined contribution-pension plans (DC). All the major plans have now been aligned with our benefits strategy with the exception of the Alcon DBs, for which Novartis has established a global timeline for their conversion into DCs.

Novartis may provide other benefits in a specific country according to local market practice and regulations, including length-of service awards and perquisites. Associates who have been transferred on an international assignment can also receive benefits in line with Novartis policies.

EXECUTIVE COMPENSATION SUMMARY

Compensation element	Compensation plan	Performance period	Method of payments	Main drivers	Performance metrics: At award	Performance metrics: At vesting	Number of participants
Base compensation	Base salary	–	Cash	Position, experience, sustained performance	–	–	All associates
Variable compensation							
Annual incentive	Cash or shares (ESOP, ESOP UK, LSSP) [1]	12 months [1]	Cash and/or shares	Financial measures such as net sales, operating income, free cash flow, market share, innovation and ongoing efforts to optimize organizational effectiveness and productivity	Achievement of individual, business and financial annual objectives or achievement of milestones in individual objectives or long-term strategic plans, Novartis Values and Behaviors	–	15 508
Long-term incentive	Equity Plan "Select"	from 3 to 10 years [2]	Restricted shares or RSUs	Financial measures such as net sales, operating income, free cash flow, market share, innovation and ongoing efforts to optimize organizational effectiveness and productivity	Achievement of individual, business and financial annual objectives or achievement of milestones in individual objectives or long-term strategic plans, Novartis Values and Behaviors	Share price	12 768
	Long-Term Performance Plan	3 years	Shares	Achievement of long-term profit, measured through Novartis Economic Value Added (NVA) targets at Group level	–	Novartis Value Added	138
	Special Share Awards	5 years	Restricted shares or RSUs	Rewarding particular achievements or exceptional performance	Selective assessment	Share price	597
Benefits				Position, experience, age, sustained performance	–	–	

[1] If the associate invests the annual incentive into a shares savings plan, the vesting/holding period will be three years (ESOP) or five years (LSSP).
[2] Three years for restricted share and/or RSUs. Ten years for tradable options.

COMPETITIVE POSITIONING

It is critical for Novartis to have competitive compensation plans at a global level. According to Novartis compensation philosophy, an associate who achieves his or her performance objectives is thus generally awarded compensation comparable to the median level of compensation provided by relevant benchmark companies. In case of over- or under-performance, the actual total compensation delivered is adjusted accordingly and may significantly differ from the benchmark median. To encourage and reward sustained superior performance, total compensation may, in case of exceptional performance, reach levels comparable to top-quartile levels of compensation offered by the relevant benchmark companies.

Novartis participates in several compensation benchmarking surveys that provide details on levels of salary, target and actual annual incentives and long-term incentives, the relative mix of short- and long-term incentives, and the mix of cash- and share-based compensation. For Executive Committee positions and for specific pharmaceutical positions, the benchmark group of industry competitors for our 2011 benchmark survey consisted of the following companies, which are all operating on a global level within the healthcare industry and having relevant business models, similar size, international needs, or similar talent skill sets:

BENCHMARK GROUP COMPANIES

Abbott Laboratories	Eli Lilly and Company	Pfizer
Amgen	GlaxoSmithKline	Roche
AstraZeneca	Johnson & Johnson	Sanofi
Bristol-Myers Squibb	Merck & Co.	

Benchmark criteria	Novartis	Healthcare Peers Median
Revenue [1]	50 624	40 249
Market Cap [1]	133 731	74 145
Net income [1]	9 969	5 070
Profit Margin	19.7%	12.6%
Employees	119 418	90 000

[1] In mio USD
Source: Equilar

For benchmarking other positions we include companies outside our industry, with stature, size, scope and complexity that approximate our own to recognize the fact that competition for senior executive talent is not limited to the healthcare industry.

The geographic scope of the benchmark companies depends on the nature of the positions. As a principle, global benchmarks are considered for the most senior executive positions, while regional and/or local benchmarks are applied in other situations. The compensation benchmarking surveys, which analyze factors such as recent market trends and best practices, are conducted by well-established global compensation consultancy firms. These surveys are checked and supplemented by input from the Compensation Committee's independent advisor. According to such surveys, projected 2012 merit salary increases for executives will be relatively modest, but will mainly depend on the demand for talents. Although target annual incentives and long-term incentives as a percentage of salary are expected to be relatively flat versus the previous year, the actual incentive or grants will be based on the achieved performance.

SAFEGUARDS

We believe that incentivizing our associates encourages performance, loyalty and entrepreneurship, and creates sustainable value that is in the interest of Novartis and our shareholders. However, shareholders also expect that risks are appropriately managed. At Novartis, appropriate objective setting combined with proper incentive-plan design and rigorous safeguard measures allow our leaders and associates to focus on long-term value creation.

RISK MANAGEMENT

The goal of our compensation system is to encourage high performance and entrepreneurship, but not to reward inappropriate or excessive risk taking or short-term profit maximization at the expense of the long-term health of Novartis. The following characteristics of our compensation system foster a culture of entrepreneurial risk management:

- Novartis Values and Behaviors: Compliance and ethical conduct are integral factors considered in all regular performance reviews, setting clear behavioral boundaries.
- People Performance Management Process: A rigorous People Performance Management process is in place based on agreed-upon objectives, values and behaviors reflecting compliance and meritocracy.
- Balanced Scorecard Approach to Performance-based Incentives: The annual and long-term incentive compensation plans are not overly focused on any single measure of performance. Instead, financial objectives include net sales, operating income, free cash flow as a percentage of sales, and Novartis Economic Value Added (NVA). Non-financial objectives emphasize the achievement of strategic and leadership objectives, and managing people, but also innovation as well as process and productivity improvement. Under the incentive plans, performance multipliers may not exceed 200%.
- Balanced Mix of Compensation Elements: The target compensation mix is not overly weighted toward annual incentive awards but represents a combination of cash and long-term share-based compensation vesting over three years.

– Performance Period and Vesting Schedules: For long-term incentives, performance period and vesting schedules overlap, reducing the motivation to maximize performance in any one period. The equity awarded under the Equity Plan "Select" vests after a period of three years. The Long-Term Performance Plan is an equity plan based on a three-year performance period.
– Clawback: We implemented "clawback" provisions in individual employment contracts of all Executive Committee members as well as in most incentive plans, and award letters to associates (see – "Safeguards – Clawback", on p.128).
– No Severance Payments or Change-of-Control Arrangements: No employment contracts with Executive Committee members contain unusually long notice periods, change-of-control clauses or severance payments. The CEO employment agreement can be terminated upon a 12-month notice period.
– Share Ownership requirements: Members of the Executive Committee, as well as selected key executives are required to own a certain multiple of their annual base salary in Novartis shares or share options (see – "Share Ownership Requirements" on p.128).

COMPENSATION GOVERNANCE

Legal Framework

The Swiss Code of Obligations as well as the Corporate Governance Guidelines of the SIX Swiss Exchange require listed companies to disclose certain information about the compensation of members of the Board of Directors and Executive Committee members, their equity participation in the Group as well as loans made to them. This Annual Report fulfills that requirement. In addition, our Annual Report is in line with the principles of the Swiss Code of Best Practice for Corporate Governance of the Swiss Business Federation (economiesuisse).

Decision-making authorities

Authority for decisions related to compensation are governed by the Articles of Incorporation, the Board Regulations and the Compensation Committee Charter, which are published on the Novartis website: www.novartis.com/corporate-governance. The main responsibilities of the Compensation Committee are shown under "Corporate Governance Report – Our Board of Directors – Role of the Board of Directors and the Board Committees".

The Compensation Committee serves as the supervisory and governing body for compensation policies and plans within Novartis and has overall responsibility for determining, reviewing and proposing compensation policies and plans for approval by the Board of Directors in line with the Compensation Committee Charter. The main discussion points and conclusions of each meeting of the Compensation Committee are summarized in a brief report to the next meeting of the full Board.

The Compensation Committee carefully analyzes and discusses on an ongoing basis (but at least annually) the trends and developments in the field of compensation and corporate governance as well as all compensation plans and levels with guidance from outside experts and consultants. The goal is to strengthen the interrelation between the compensation plans and the Group's performance. It also reviews the compensation system to ensure that it does not encourage inappropriate or excessive risk taking and instead encourages behaviors that support sustainable value creation.

The Compensation Committee is composed exclusively of members of the Board of Directors who meet the independence criteria set forth in our Board Regulations. Currently, the Compensation Committee has the following five members: Marjorie M.T. Yang (chair), William Brody, Srikant Datar, Ulrich Lehner and Enrico Vanni.

In 2011, the Compensation Committee held five meetings.

COMPENSATION AUTHORIZATION LEVELS

Decision on	Recommendation	Authority
Compensation of Board members	Compensation Committee	Board of Directors
Compensation of the Chief Executive Officer	Chairman of the Board	Compensation Committee
Compensation of the other Executive Committee members and other selected key executives	Chief Executive Officer	Compensation Committee
Special Share Awards	Chairman of the Board or Chief Executive Officer	Compensation Committee

The General Meeting holds a consultative vote on the Compensation System of Novartis. This vote takes place before every significant change to the Compensation System, but at least every third Annual General Meeting.

ROLE OF THE COMPENSATION COMMITTEE INDEPENDENT ADVISORS

The advisor to the Compensation Committee is independent of management and does not perform any other consulting work for Novartis. The key task of the advisor is to assist the Compensation Committee in ensuring that the Novartis compensation policies and plans are competitive, correspond to market practice, and are in line with our compensation principles.

The Compensation Committee enters into a consulting agreement with its independent advisor on an annual basis. In determining whether or not to renew the engagement with the advisor, the Compensation Committee evaluates the quality of the consulting service and the benefits of rotating advisors. In addition, the Compensation Committee assesses on an annual basis the projected scope of work for the coming year. The Compensation Committee

used Pearl Meyer & Partners LLC as its independent external compensation advisor and decided that after several years of service a new advisor should be hired. The Compensation Committee designated a new advisor, Frederic W. Cook & Co, Inc., in October 2011.

The Compensation Committee determined that the advisor is free of any relationship that would impair professional judgment and advice to the Compensation Committee, and has never been hired for work by the management of Novartis.

CLAWBACK

Any incentive compensation paid to certain key executives, including Executive Committee members, is subject to "clawback". This means that Novartis may choose not to pay future incentive compensation or seek to recover incentive compensation where the payout has been proven to conflict with internal management standards (including company policies and Novartis Values and Behaviors), accounting procedures or a violation of law.

SHARE OWNERSHIP REQUIREMENTS

In line with our share ownership principle, key executives are required to own at least a certain multiple of their annual base salary in Novartis shares or share options. The CEO is required to own Novartis equity worth 5 times, the other Executive Committee members 3 times, and other key executives, 1 to 2 times (position-specific) their respective base compensation within three years of hire or promotion. In the event of a substantial drop in the share price, the Board of Directors may, at its discretion, extend that time period.

CEO	5 x base salary
Executive Committee members	3 x base salary
Selected key executives	1 x or 2 x base salary

In determining equity amounts against the share ownership requirement includes vested and unvested shares or ADSs acquired under the Novartis compensation plans, as well as RSUs thereof, with the exception of unvested matching RSUs from leveraged share savings plans and unvested RSUs from the Long-Term Performance Plan. In addition, it includes other shares as well as vested options on Novartis shares or ADSs that are owned directly or indirectly by "persons closely linked"[1].

The Compensation Committee reviews compliance with the share ownership guideline on an annual basis.

[1] "Persons closely linked" are (i) their spouse, (ii) their children below age 18, (iii) any legal entities that they own or otherwise control, and (iv) any legal or natural person who is acting as their fiduciary.

2011 COMPENSATION OF THE MEMBERS OF THE EXECUTIVE COMMITTEE

PERFORMANCE IN 2011

At its meeting on January 19, 2012, the Compensation Committee decided on the amounts of variable compensation for 2011 for the CEO and Executive Committee members by applying the principles described previously in this Compensation Report. The specific compensation decisions made for the CEO and Executive Committee members reflect their achievements against the financial and non-financial performance objectives established for them at the beginning of the year. The achievements were assessed from both a quantitative and a qualitative perspective, with the Compensation Committee using its judgment, where appropriate, in concert with a review of metrics. In line with our compensation philosophy and performance principles, the actual payout of the variable compensation reflects the key individual achievements and the actual business performance of the organization taking into account the various following accomplishments and events, which occurred in 2011:

– Novartis management delivered against the critical goals of the organization, including financial and non-financial targets, to support the long term health of Novartis. These targets were established at the beginning of the year and were categorized under four categories: Financial targets, Innovation and Growth, Organizational Health, and Customer Satisfaction.
– The financial targets of net sales, free cash flow, and the long-term, 3-year rolling NVA were met or exceeded. However, the target of operating income was not achieved as a result of the exceptional provisions made in the fourth quarter of 2011.
– In the area of Innovation and Growth, each division was given specific targets to enhance their respective pipelines with new products. These were measured by the number of new compounds moving from research through proof of concept, submissions to regulatory agencies for marketing authorization, and approvals. These targets were met or exceeded in 2011, and included among others, the marketing authorization of *Gilenya* the first oral treatment for multiple sclerosis in the EU and *Arcapta* for chronic obstructive lung disease in the US. As expected not all trials and submissions were successful. The regulatory approvals of *Ilaris* for the treatment of gouty arthritis and SOM230 for the treatment of Cushing Syndrome were delayed while the regulatory submissions INC424, NVA237, ACZ885 for various indications occurred on time. The results of a long-term *Tekturna/Rasilez* study in hypertensive patients with concomitant renal and cardiovascular disease showed negative results, which led to the early termination of the study. Overall, the Pharmaceuticals Division gained market share.

– Importantly, the Alcon integration was planned and executed according to plan, without disruption to the business. The ambitious synergy and growth targets were exceeded. It should also be mentioned that Sandoz performed at a very high level, exceeding expectations significantly and the Vaccines and Diagnostics Division not only achieved the fastest growth among its competitors, but also gained a respectable market share with *Menveo*, a vaccine to protect against certain types of bacterial meningitis. The performance of OTC and Animal Health were on track. Finally, growth was accelerated in key emerging markets, particularly in China.
– In the area of Organizational Health, specific objectives were set in the area of productivity within manufacturing, procurement, IT and the finance function. These productivity targets were met or exceeded. Additionally, objectives to strengthen Quality Assurance were established. Capital investment and operating plans were developed and executed in key Novartis facilities to strengthen QA. However, the warning letter from the FDA covering three Sandoz facilities in the U.S. and Canada indicates that additional work will be required in this area. Additionally, compliance with quality standards has to be upgraded in the Nebraska OTC plant. In the area of associates' behavior, the Compliance group was significantly strengthened to manage adherence to the Novartis Code of Conduct, including ethical business practices. Customer satisfaction was measured by market share gains around the world. Nearly all market share targets which were established at the beginning of the year, were met or exceeded. Management also successfully implemented the Corporate Citizenship strategy and delivered among other programs over 100 million treatments of *Coartem* against malaria to developing countries. An estimated one million lives, mostly children, were saved since the launch of this product. Novartis also continued successfully its Leprosy eradication program with WHO by donating all necessary medications for free.
– The Board of Directors took note of the high retention rates of key performers, the high quality continuous education programs and the strength and good collaboration of the leadership team.
– Finally, Novartis was named the number one pharmaceutical company in *Fortune*'s "Worlds most admired companies", and strong rankings in the Dow Jones Sustainability World Index reflecting the overall good reputation of the company.

COMPENSATION IN 2011

The compensation table on the following page discloses the compensation earned by the CEO and Executive Committee members for performance in 2011. The following paragraphs describe the principles underlying the data in the table.

ALIGNMENT OF REPORTING AND PERFORMANCE

The compensation table synchronizes the reporting of annual compensation with the performance in the given year, i.e., all amounts awarded for performance in 2011, including the future ESOP/LSSP match, are disclosed in full.

DISCLOSURE STRUCTURE

The compensation table shows the compensation granted to the CEO and each Executive Committee member for performance in 2011 for all compensation elements – base compensation, variable compensation and benefits – as previously described.

The column "Future ESOP/LSSP match" reflects shares to be awarded in the future if the Executive Committee member remains with Novartis for at least three or five years, respectively.

VALUATION PRINCIPLES

In order to allow a comparison with other companies, the Compensation Committee decided to disclose shares, restricted shares, RSUs and ADS at their market value on the date of grant. Market value is the current quoted share price at which a director or an associate is granted a share, a restricted share or a restricted stock unit at grant date. The market value of share options is calculated by using an option pricing valuation model as per grant date.

As shares, RSUs and share options under the variable compensation plans are generally granted with a vesting[1] period, and associates in Switzerland (including Executive Committee members) may block[2] shares received under any variable compensation plan for up to 10 years, equity based compensation is also provided at tax value in accordance with Novartis past disclosure practice. According to the Swiss Federal Tax Administration and as the Compensation Committee also firmly believes, such restrictions affect the value of shares, RSUs and share options negatively. In its "Kreisschreiben Nr. 5", the Swiss Tax Administration provides for a methodology pursuant to which unvested or blocked shares or share options shall be valued with a discount for each year they are unvested or blocked. In addition, for the valuation of share options, the Swiss Tax Authorities apply – in a standing practice for Novartis (since 1997) – an option valuation model based on Black-Scholes.

See also Note 27 to the Group's consolidated financial statements for information on executive officer and non-executive director compensation in accordance with IFRS.

[1] Vesting refers to the waiting period under a share-based incentive plan that must expire before the associate becomes irrevocably entitled to the shares, RSUs or share options involved. The associate cannot sell or exercise unvested share, RSUs or share options. If an associate leaves Novartis prior to the expiration of the vesting period for reasons other than retirement, disability or death, the associate will generally forfeit rights to such shares, RSUs or share options.

[2] Blocking refers to the ability of associates in Switzerland to opt for an extended trading restriction period of up to 10 years from the award date (including vesting). Novartis encourages associates to block their shares because doing so aligns the associates' interests with those of shareholders.

EXECUTIVE COMMITTEE MEMBER COMPENSATION FOR PERFORMANCE YEAR 2011 (MARKET VALUE)[1]

	Base compensation	Variable compensation			Benefits		Total		Total compensation
		Short-term incentive plans	Long-term incentive plans						
			Equity Plan "Select"	Long-Term Performance Plan	Special share awards	Pension benefits	Other benefits	Future ESOP/LSSP match	Including future ESOP/LSSP

EXECUTIVE COMMITTEE MEMBER - EQUITY AWARDS FOR PERFORMANCE YEAR 2011 (NUMBER OF EQUITY INSTRUMENTS AND TAX VALUE)

		Variable compensation											
		Short-term incentive plans		Long-term incentive plans									
				Equity Plan "Select"				Long-Term Performance Plan		Special share awards		Future ESOP/LSSP match	
	Currency	Shares (Number)	Shares (Tax value)[2,3]	Shares (Number)	Shares (Tax value)[2,4]	Options (Number)	Options (Tax value)[2]	Shares (Number)	Shares (Tax value)[2,5]	Shares (Number)	Shares (Tax value)[2,6]	Shares (Number)	Shares (Tax value)[2,7]
Joseph Jimenez (Chief Executive Officer)	CHF	19 484	789 131	113 654	5 172 099	0	0	83 958	4 550 524	0	0	19 484	789 131
Juergen Brokatzky-Geiger	CHF	11 366	460 340	22 731	1 034 429	0	0	10 745	582 379	0	0	11 366	460 340
Kevin Buehler (since April 8, 2011)	USD	18 496	806 207	46 566	2 280 588	0	0	22 506	1 312 788	0	0	18 496	806 207
David Epstein	USD	10 003	436 008	47 900	2 345 904	0	0	22 175	1 293 468	0	0	10 003	436 008
Mark C. Fishman	USD	16 309	710 871	66 193	3 241 804	0	0	23 107	1 347 831	0	0	16 309	710 871
Jeff George	CHF	6 747	307 038	26 984	1 227 972	0	0	8 181	443 410	20 000	702 424	3 374	153 542
George Gunn	CHF	0	0	20 388	927 805	0	0	17 166	930 397	0	0	0	0
Andrin Oswald	CHF	0	0	25 185	639 979	0	0	8 181	443 410	20 000	702 424	0	0
Jonathan Symonds	CHF	14 613	591 848	36 532	1 662 477	0	0	14 136	572 529	0	0	14 613	496 924
Thomas Werlen (until September 30, 2011)	CHF	7 611	346 357	0	0	0	0	0	0	0	0	0	0
Naomi Kelman (as from March 2, 2011)[1]	USD	0	0	9 001	440 824	0	0	1 401	81 720	88 000	4 004 689	0	0
Felix R. Ehrat (as from October 1, 2011)[1]	CHF	2 406	97 447	4 812	218 982	0	0	1 414	57 269	0	0	2 406	81 818
Total[8]	**CHF**	**107 035**	**4 320 556**	**419 946**	**18 236 947**	**0**	**0**	**212 970**	**11 151 429**	**128 000**	**4 948 821**	**96 051**	**3 710 150**

[1] The table reflects the compensation as Permanent Attendee to the Executive Committee from date of hiring until December 31, 2011.

[2] Values of shares and RSUs granted are discounted by 6% per year depending on the length of the combined vesting and blocking period. For example, the value of a share award subject to a three-year vesting/blocking period calculated in accordance with the methodology described in the Kreisschreiben Nr. 5 equals 83.962% of its market value at the grant date. The value of a share award with a combined vesting/blocking period of ten years equals 55.839% of its market value at the grant date. The closing share price on the grant date (January 19, 2012) was CHF 54.20 per Novartis share and USD 58.33 per ADS. The values of share options granted are reported based on the valuation principles contained in a tax ruling from the Swiss tax authorities, reflecting the principles as disclosed in the aforementioned Kreisschreiben Nr. 5. According to this methodology, tradable share options under the Equity Plan "Select" with a vesting period of three years have a value of CHF 0.40 per option at grant.

[3] These shares have a five-year vesting period under LSSP and a three-year vesting period under ESOP.

[4] Andrin Oswald has voluntarily blocked these RSUs for ten years in addition to the three-year vesting period.

[5] Jonathan Symonds and Felix R. Ehrat have voluntarily blocked these shares for five years.

[6] The special RSU awards granted to Jeff George and Andrin Oswald have a five-year vesting period. The special share award granted to Naomi Kelman has a staggered vesting of up to seven years.

[7] Jonathan Symonds and Felix R. Ehrat have voluntarily blocked these LSSP matching share units for eight years including the five-year vesting period.

[8] Amounts in USD for Kevin Buehler, David Epstein, Mark C. Fishman and Naomi Kelman were converted at a rate of CHF 1.00 = USD 1.130, which is the same average exchange rate used in the Group's consolidated financial statements.

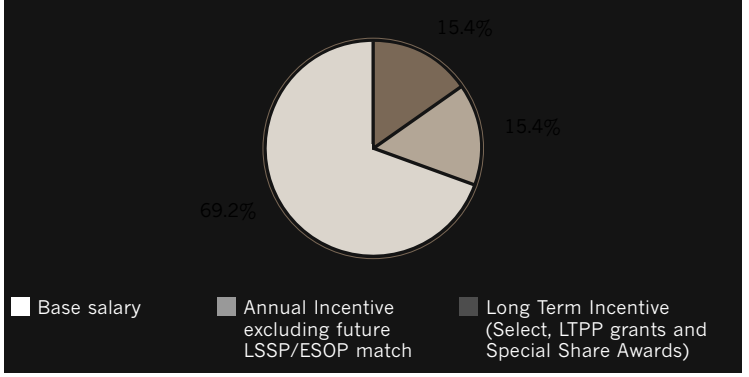
As the table below shows, most executive compensation is variable and awarded in the form of restricted equity. This ensures alignment with the interests of Novartis and its shareholders.

EXECUTIVE COMMITTEE MEMBER ACTUAL COMPENSATION MIX IN 2011 – BASE AND VARIABLE COMPENSATION[1]

		Variable	
	Base salary	Annual Incentive[2]	Long Term Incentive[3]
Joseph Jimenez	13.3%	12.2%	74.4%
Juergen Brokatzky-Geiger	22.3%	19.7%	58.0%
Kevin Buehler	12.3%	26.0%	61.7%
David Epstein	15.5%	16.4%	68.0%
Mark C. Fishman	13.8%	13.5%	72.7%
Jeff George	17.0%	17.0%	66.0%
George Gunn	23.9%	18.7%	57.4%
Andrin Oswald	17.6%	16.4%	66.0%
Jonathan Symonds	20.1%	17.9%	62.0%
Naomi Kelman (as from March 2, 2011)[4]	8.1%	4.3%	87.6%[5]
Felix R. Ehrat (as from October 1, 2011)[4]	27.2%	20.3%	52.5%
Total[6]	**15.4%**	**15.4%**	**69.2%**

[1] Excludes pension, other benefits and future ESOP/LSSP match.
[2] Excludes future ESOP/LSSP match.
[3] Long Term Incentive includes Select, LTPP grants and Special Share Awards.
[4] Permanent Attendee to the Executive Committee.
[5] Includes the special award of 88 000 shares granted to Naomi Kelman to compensate her loss of equity from her former employer.
[6] Excludes Thomas Werlen who stepped down from the Executive Committee as per September 30, 2011.

EXECUTIVE COMMITTEE ACTUAL COMPENSATION MIX IN 2011 – BASE AND VARIABLE COMPENSATION



SHARES AND SHARE OPTIONS OWNED BY MEMBERS OF THE EXECUTIVE COMMITTEE

The following tables show the total number of vested and unvested Novartis shares (including share units but excluding unvested matching share units from leveraged share savings plans and unvested target units from the Long-Term Performance Plan) and the total number of share options owned by Executive Committee members as of January 19, 2012.

As of January 19, 2012, none of the Executive Committee members together with "persons closely linked" to them (see definition under "Share Ownership – Ownership Guidelines") owned 1% or more of the outstanding shares of Novartis, either directly or through share options.

As of December 31, 2011, all Executive Committee members who have served at least three years on the Executive Committee have met or exceeded their personal Novartis ownership requirements.

SHARES OWNED BY EXECUTIVE COMMITTEE MEMBERS

	Number of shares[1]
Joseph Jimenez	461 487
Juergen Brokatzky-Geiger	232 858
Kevin Buehler (as from April 8, 2011)	445 287[2]
David Epstein	279 395
Mark C. Fishman	435 071
Jeff George	109 525
George Gunn	251 459
Andrin Oswald	135 713
Jonathan Symonds	144 829
Naomi Kelman (as from March 2, 2011)[3]	97 906
Felix R. Ehrat (as from October 1, 2011)[3]	9 132
Total[4]	**2 602 662**

[1] Includes holdings of "persons closely linked" to members of the Executive Committee (see definition under – Share and Share Options by Members of the Board of Directors).
[2] Excludes performance share units from former Alcon equity plans to vest after January 19, 2012.
[3] Permanent attendee to the Executive Committee.
[4] Excludes Thomas Werlen who stepped down from the Executive Committee as per September 30, 2011.

SHARE OPTIONS OWNED BY EXECUTIVE COMMITTEE MEMBERS

	Number of share options[1]						
	2012	2011	2010	2009	2008	Other	Total
Joseph Jimenez				552 076	157 266		709 342
Juergen Brokatzky-Geiger				75 705	109 016	146 436	331 157
Kevin Buehler (as from April 8, 2011)						782 485[2]	782 485
David Epstein						267 777	267 777
Mark C. Fishman					184 870	587 149	772 019
Jeff George		141 396				114 979	256 375
George Gunn						94 371	94 371
Andrin Oswald						5 633	5 633
Jonathan Symonds						54 348	54 348
Naomi Kelman (as from March 2, 2011)[3]							
Felix R. Ehrat (as from October 1, 2011)[3]							
Total[4]	**–**	**141 396**	**–**	**627 781**	**451 152**	**2 053 178**	**3 273 507**

[1] Share options disclosed for a specific year were granted in that year under the Novartis Equity Plan "Select." The column "Other" refers to share options granted in 2007 or earlier, to share options granted to these executives while they were not Executive Committee members, and to share options bought on the market by the Executive Committee members or "persons closely linked" to them (see definition under – Share and Share Options Owned by Members of the Board of Directors).
[2] Consists of non tradable options and share settled appreciation rights resulting from conversion of Alcon equity into Novartis equity.
[3] Permanent Attendee to the Executive Committee.
[4] Excludes Thomas Werlen who stepped down from the Executive Committee as per September 30, 2011.

LOANS AND OTHER PAYMENTS

LOANS TO EXECUTIVE COMMITTEE MEMBERS

No loans were granted to current or former Executive Committee members during 2011. No such loans were outstanding as of December 31, 2011.

OTHER PAYMENTS TO EXECUTIVE COMMITTEE MEMBERS

During 2011, no payments (or waivers of claims) other than those set out in the Executive Committee Member Compensation table were made to current Executive Committee members or to "persons closely linked" to them (see definition under "Compensation of the Board of Directors – Shares and Share Options Owned by Members of the Board of Directors").

PAYMENTS TO FORMER EXECUTIVE COMMITTEE MEMBERS

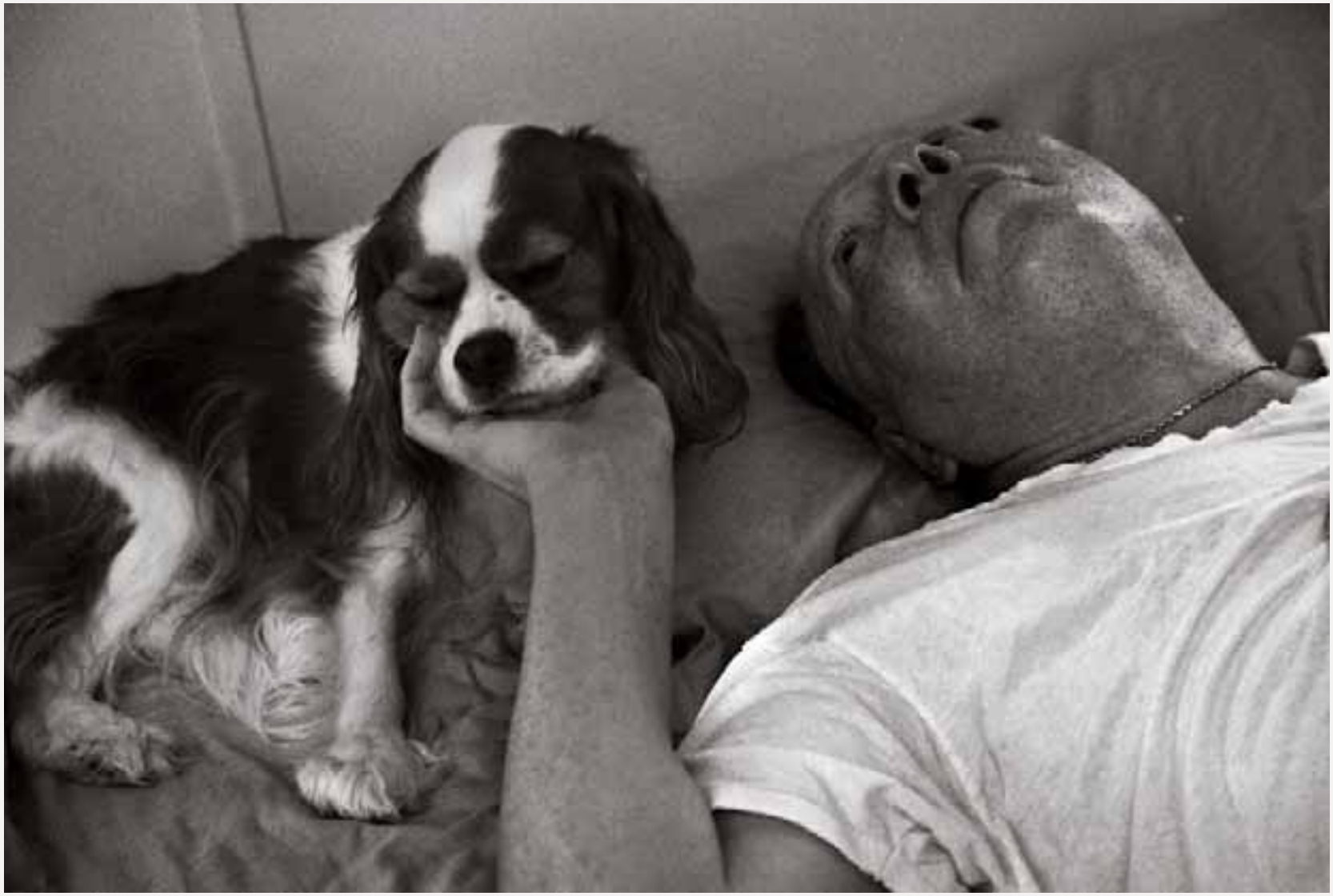
During 2011, no payments (or waivers of claims) were made to former Executive Committee members or to "persons closely linked" to them (see definition under "Compensation of the Board of Directors – Shares and Share Options Owned by Members of the Board of Directors"), except for an amount of CHF 25 596, which was paid to a former member of the Executive Committee as deferred compensation.

NOTES 27 TO THE GROUP'S AUDITED CONSOLIDATED FINANCIAL STATEMENTS AND 12 TO THE AUDITED FINANCIAL STATEMENTS OF NOVARTIS AG

The compensation awarded to the members of the Board of Directors and the Executive Committee members is also presented in our Financial Report in note 27 to the Group's audited consolidated financial statements and in note 12 to the audited financial statements of Novartis AG.

A

JOE CRISMAN:



FINANCIAL REPORT

CONTENTS

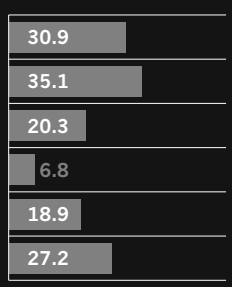
FINANCIAL HIGHLIGHTS 2011

	2011 USD millions	2010 USD millions	Change %
Net sales	58 566	50 624	16
Operating income	10 998	11 526	– 5
Return on net sales (%)	18.8	22.8	
Net income	9 245	9 969	– 7
Basic earnings per share (USD)[1]	3.83	4.28	– 11
Core[2]			
Operating income	15 909	14 006	14
Core return on net sales (%)	27.2	27.7	
Net income	13 490	12 029	12
Basic earnings per share (USD)[1]	5.57	5.15	8
Change in net debt	– 301	– 18 314	
Equity at year-end	65 940	69 769	– 5
Dividend (CHF)[3]	2.25	2.20	2

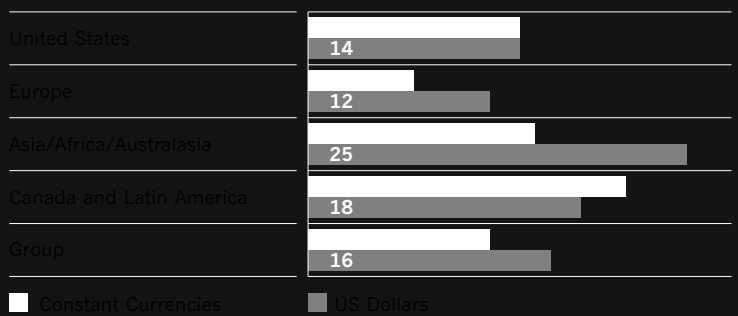
NET SALES GROWTH BY SEGMENT[4]
(in %)

CORE OPERATING INCOME USD GROWTH
(in %)[2,4]

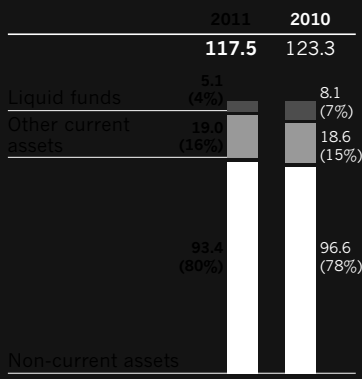
CORE OPERATING MARGIN (in %)[2]



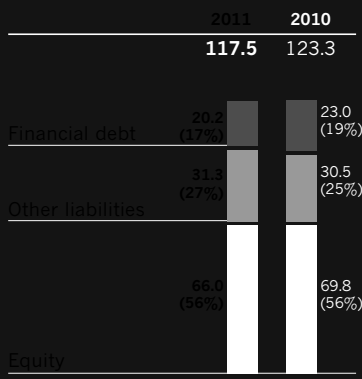
NET SALES GROWTH BY REGION
(in %)



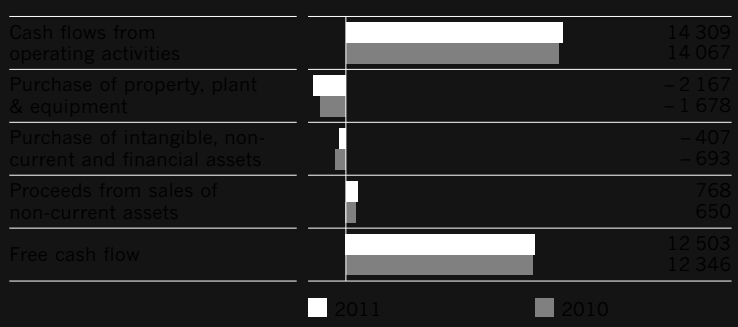
TOTAL ASSETS
(in USD billions and %)



TOTAL EQUITY AND LIABILITIES
(in USD billions and %)



CASH FLOWS FROM OPERATING ACTIVITIES AND FREE CASH FLOW
(in USD millions)



[1] 2011 average number of shares outstanding: 2 382.5 million (2010: 2 285.7 million)
[2] Core results for operating income, net income and earnings per share (EPS) eliminate the impact of acquisition-related factors and other significant exceptional items. These adjustments are explained in detail starting on page 179
[3] Dividend payment for 2011: proposal to 2012 Annual General Meeting
[4] Restated to reflect new segment allocation introduced during 2011 as explained in detail on page 159
[5] Basis for growth is full year 2010 on a pro forma basis as explained on page 184

KEY FINANCIAL DEVELOPMENTS IN 2011

NOVARTIS IN 2011	Innovation underpinned continued double-digit growth with a strong contribution from recently launched products.
NET SALES	Net sales rose 16% (+12% in constant currencies (cc)) to USD 58.6 billion on the underlying business expansion and from the Alcon acquisition.
PHARMACEUTICALS[1]	Net sales were up 7% (+4% cc) to USD 32.5 billion with impressive volume growth (9 percentage points) offsetting the impact of generics entries, product divestments and pricing. Products launched since 2007 comprised 28% of net sales.
ALCON[2]	Alcon net sales of USD 10.0 billion rose 10% (+7% cc) on a pro forma basis, driven by the Ophthalmic Pharmaceuticals and Surgical product categories, as well as strong growth in emerging markets.
SANDOZ[1]	Net sales advanced 10% (+7% cc) to USD 9.5 billion, driven by strong growth in the US, with enoxaparin reaching USD 1 billion in sales, as well as other key regions and differentiated products, which now account for 47% of Sandoz global sales.
VACCINES AND DIAGNOSTICS	Net sales were USD 2.0 billion, down 32% (–34% cc) from 2010. Underlying net sales (excluding A(H1N1) in 2010) achieved growth of 22% cc, driven by all franchises, with a particularly strong contribution from the meningococcal disease franchise.
CONSUMER HEALTH[1]	Net sales were up 6% (+3% cc) to USD 4.6 billion. In OTC, net sales declined at the end of 2011 due to a temporary suspension of operations and voluntary product recall at one of the US sites. Animal Health continued to grow ahead of the market in most regions.
OPERATING INCOME	Operating income was down 5% (+1% cc) to USD 11.0 billion, following net exceptional charges of USD 1.9 billion. Core operating income grew 14% (+16% cc) to USD 15.9 billion, delivering strong operating leverage. Core operating income margin was 27.2%.
NET INCOME	Net income decreased 7% (–2% in cc) to USD 9.2 billion in line with the decline in operating income. Core net income rose 12% (+15% cc) to USD 13.5 billion.
BASIC EARNINGS PER SHARE	Basic earnings per share (EPS) fell 11% (–5% cc) to USD 3.83 from USD 4.28 in 2010, while core EPS rose 8% (11% in cc) to USD 5.57.
FREE CASH FLOW	Free cash flow reached USD 12.5 billion, up 1% over 2010.
DIVIDEND	Proposed dividend of CHF 2.25 per share for 2011 represents 15th consecutive annual increase, up 2% from CHF 2.20 in 2010, a dividend yield of 4.2%.

[1] Restated to reflect new segment allocation introduced during 2011 as explained in detail on page 159
[2] Basis for growth is full year 2010 on a pro forma basis as explained in detail starting on page 184

OPERATING AND FINANCIAL REVIEW 2011

This operating and financial review should be read together with the Group's consolidated financial statements in this Annual Report, which have been prepared in accordance with International Financial Reporting Standards (IFRS) as published by the International Accounting Standards Board.

OVERVIEW

Novartis provides healthcare solutions that address the evolving needs of patients and societies worldwide. Our focused, diversified portfolio of businesses is made up of six global operating divisions and reports its results in five segments:

- Pharmaceuticals: Innovative patent-protected prescription medicines
- Alcon: Surgical, ophthalmic pharmaceutical and vision care products
- Sandoz: Generic pharmaceuticals
- Vaccines and Diagnostics: Human vaccines and blood-testing diagnostics
- Consumer Health: OTC (over-the-counter medicines) and Animal Health

The Group established its newest and second largest division, Alcon, after securing 100% ownership of Alcon, Inc., on April 8, 2011. The new division includes the CIBA Vision contact lens and lens care business and selected ophthalmic medicines from the Pharmaceuticals Division and is a world leader in eye care, offering the widest spectrum of innovative surgical, pharmaceutical and vision care products to address the world´s eye care needs.

Novartis has leadership positions in each of the five businesses, giving us the capacity to address customer and patient needs across segments of the healthcare marketplace. We believe that our ability to innovate in all these segments will allow us to tailor our portfolio in response to market opportunities and will enable Novartis to continue as an industry leader.

Headquartered in Basel, Switzerland, the Novartis Group companies employed approximately 124 000 full-time equivalent associates as of December 31, 2011, with operations in more than 140 countries around the world.

FACTORS AFFECTING RESULTS OF OPERATIONS

A number of key factors influence the Group's results of operations and the development of our businesses.

The fundamentals of the healthcare industry remain robust due to long-term demographic and socioeconomic trends worldwide, which are increasing the demand for and use of medicines and other healthcare products. Consistent investments in innovation and advancing technologies are also supporting the development of new medicines to better treat many diseases.

At the same time, other factors have created a business environment that has significant risks, such as the growing burden of healthcare costs in many countries, which has led governments and payors to focus on controlling spending ever more tightly, and more stringent regulatory demands, which have made securing approvals for new drugs increasingly costly and difficult and increased the risk of disruptions in our supply chain.

We believe that Novartis is strategically well-positioned to operate successfully in this evolving landscape. We expect that our broad, focused portfolio, our capacity to innovate resulting in a rich pipeline of potential new medicines that address unmet medical needs, and our established presence across regions should enable us to adapt to the evolving healthcare marketplace.

TRANSFORMATIONAL CHANGES FUELING DEMAND

Long-term trends in the composition and behavior of the worldwide population are fueling demand for and access to healthcare, while scientific advances continue to open new frontiers in patient treatment, creating major opportunities for improved care. These trends are expected to sustain steady growth in the healthcare market overall in the coming years and to drive accelerating growth in key segments.

AGING GLOBAL POPULATION AND SHIFTING DEMOGRAPHICS

Scientific advances in treating diseases and increased access to healthcare worldwide have enabled people across the globe to enjoy longer and healthier lives. The rise in life expectancy is coincident with a decline in birth rates, increasing the proportion of the elderly around the world. Over the next decade, there is expected to be a 75% increase in the number of people over the age of 60. In the developed world, by 2040 there are predicted to be twice as many people over the age of 60 as there will be under 15; in the United States, the number of people over the age of 60 will more than double by 2050. The proportion of the elderly is growing even faster in the developing world. For example, according to the United Nations, in China the ratio of people over 60 to the rest of the pop-

ulation is projected to rise by more than 15% annually until 2040. As the global population ages, there will continue to be an accelerating need for treatments for the diseases and conditions that disproportionately afflict the elderly.

One area where this unmet medical need is particularly evident is eye care. The aging of the world's population is linked to an increase in eye diseases, with several hundred million people living with blindness or serious vision impairment around the world. With the addition of Alcon, we have the resources and expertise to help meet these needs, with the goal of reducing preventable blindness and treating diseases and disorders of the eye.

Another major trend in worldwide health is an increase in rates of obesity. In fact, there are now more obese people in the world than there are malnourished people, and the World Health Organization (WHO) currently ranks obesity as the world's largest public health problem. Global obesity rates have doubled since 1980; one in three adults worldwide are overweight and one in nine are obese, according to a 2011 study in the British medical journal *The Lancet*. Once considered a problem only in wealthy countries, due to economic growth and shifting nutritional habits, the prevalence of people who are overweight or obese is significantly increasing in low- and middle-income countries as well, according to the WHO. The problem is only predicted to grow worse: by 2030, the majority of the world's population will be overweight or obese, according to a study conducted by Tulane University in the United States. Obesity and inactive lifestyles are important risk factors for diabetes, cardiovascular conditions and other serious diseases, including cancer. The WHO estimates that globally 44% of the diabetes burden, 23% of the incidence of ischemic heart disease and up to 41% of certain cancer burdens are attributable to obesity.

Increased rates of obesity, as well as habits such as cigarette smoking, have contributed to a worldwide rise in the prevalence of chronic diseases – including cardiovascular disease, diabetes, glaucoma and chronic respiratory diseases. Chronic diseases now account for 60% of deaths around the world. Chronic obstructive pulmonary disease (COPD) alone affects more than 200 million people worldwide, and is projected to become the world's third leading cause of death by the end of this decade. Our Pharmaceuticals and Sandoz Divisions offer several products to help address the needs of patients with COPD and other chronic diseases, and we will continue to make significant investments in new treatments to address this growing health threat.

GLOBAL RISE IN HEALTHCARE SPENDING

Across the world, healthcare spending is increasing. Factors driving this increase include aging populations, the rising incidence of chronic diseases and technological and medical advances that make it possible to treat more diseases – and patients – than ever before. Healthcare spending among members of the Organization for Economic Cooperation and Development (OECD) and emerging markets of China, Russia, Brazil and India is expected to rise from USD 5.3 trillion in 2010 to USD 7.9 trillion in 2020, an increase of approximately 50%, according to research from auditing and advisory firm PricewaterhouseCoopers (PwC). The United States remain the biggest spender by far, with expenditure on health as a percentage of gross domestic product (GDP) expected to rise to approximately

SCIENTIFIC ADVANCES OPENING NEW OPPORTUNITIES FOR TARGETED THERAPIES

Ongoing developments in technology and advances in scientific understanding, particularly around the human genome, are laying the foundation for the creation of new treatments for medical conditions for which current treatment options are inadequate or nonexistent. Further, we are gaining a greater capability to identify the specific biological factors, called "biomarkers," that indicate whether or not a given drug will be effective for a particular patient. It is estimated that up to 95% of the variability in drug response may be due to genetic differences. Effectively pairing treatments and genetic biomarkers has tremendous potential both in terms of patient health and healthcare savings.

The science of biomarkers is just one element of a new healthcare paradigm known as "personalized medicine." By delivering the right medicine to the right patient at the right time, this more targeted approach has the potential to significantly improve the response rates and outcomes of patients. Personalized medicine is expected to be a major growth driver for the industry, with the market expected to quadruple in size over the next five years, expanding to approximately USD 160 billion.

At Novartis, our research and development strategy is based on innovative science guided by patient needs. We employ state-of-the-art technology in order to achieve an understanding of the underlying mechanism of disease, and then use this understanding as the basis for the development of targeted therapies, a number of which have already been brought to market. Consistent with our science-focused strategy, Novartis has established a Molecular Diagnostics unit within our Pharmaceuticals Division to support our efforts to develop and commercialize personalized medicines. Additionally, in the Alcon Division, we are combining Novartis research operations with Alcon's expertise in development to provide a new innovation engine for the Group. Alcon scientists can now leverage the resources and capabilities of the Novartis Institutes for BioMedical Research, our global pharmaceutical research organization, to accelerate product innovation for the eye.

NEW TECHNOLOGIES CHANGING THE DELIVERY OF HEALTHCARE

New and innovative technologies have the potential to transform the delivery of healthcare and the relationships between patients, providers and payors. The spread of broadband networks coupled with the ability to embed wireless sensors in an array of devices and everyday materials is beginning to increase the use of telemedicine, or remote patient monitoring. Advances in imaging and diagnostic technologies are paving the way for new forms of preventive medicine, while the growth of electronic medical records promises to improve patient care and medical research.

Novartis is investigating new ways to use technology to improve patient outcomes beyond traditional research and development. We are actively exploring telehealth technology, which allows remote monitoring of key health indicators and patient compliance. Such technologies could both reduce healthcare costs and improve patient outcomes by allowing healthcare professionals to assess treatments and identify problems remotely and in real time.

We are also embracing new technologies and information channels to better engage with our stakeholders, from patients to physicians to payors and retailers. For example, Novartis Vaccines and Diagnostics developed VaxTrak, an iPhone application that allows families to better track and plan their children's vaccinations. The application also uses GPS technology to locate nearby retail clinics offering and administering flu vaccines.

INCREASINGLY CHALLENGING BUSINESS ENVIRONMENT

Medical and technological innovation, coupled with the increasing demand for healthcare worldwide, offers healthcare companies opportunities for growth and, more importantly, the chance to improve patient outcomes. However, the operating environment for healthcare companies has become increasingly challenging. The ongoing effects of the global financial crisis, combined with rising demands on healthcare systems, have led to a renewed focus on cost containment by governments and payors across the globe. Research and development of new products has been made more complicated and costly due to high levels of regulatory and safety scrutiny. In addition, the industry faces the continued expiration of patents and the growing market prominence of generic products, which, while offering an opportunity to our Sandoz Division, represents a significant challenge to our Pharmaceuticals and Alcon Divisions.

GREATER PRESSURE TO CONTAIN HEALTHCARE SPENDING

The ongoing financial crisis and its resultant drag on economic growth continue to impact the debt burden of many economies, most notably in Europe, where Greece is facing possible default of its sovereign debt obligations, and countries such as Spain and Italy have had their sovereign debt obligations downgraded. With budgets under pressure and a shaky global economy, stringent cost-containment measures have been implemented in countries around the world.

Given the growth of overall healthcare costs as a percentage of GDP in many countries, some governments and payors have introduced price reductions and/or rebate increases for patented and generic medicines, as well as other healthcare products and services. Other initiatives to contain healthcare costs include mandatory pricing systems, reference pricing initiatives, an increase in imports of drugs from lower-cost countries to higher-cost countries, shifting of the payment burden to patients through higher co-payments, limiting physicians' ability to choose among competing medicines, mandatory substitution of generic drugs, and growing pressure on physicians to reduce the prescribing of patented prescription medicines.

These ongoing pressures affect all of our businesses that rely on reimbursement, including Pharmaceuticals, Alcon, Sandoz, and Vaccines and Diagnostics. To mitigate these pressures, which we expect to continue in 2012, we have strengthened dialogue with

health authorities and payors to develop innovative pricing models that allow us to provide treatment options that result in better outcomes for patients. For example, in the UK, Novartis offers dose-capping arrangements for *Lucentis* for patients with wet age-related macular degeneration, whereby up to 14 injections per patient and per eye are paid by the UK National Health Service (NHS), with Novartis reimbursing NHS for the cost of additional vials the patients may need. Novartis offers similar dose-capping arrangements for *Lucentis* in many other countries.

Where we have unique, often critical medications, Novartis is committed to providing access for patients most in need through access-to-medicines programs. These programs provide assistance to those experiencing financial hardship or living in the developing world who would otherwise not be able to receive treatment.

PATENT EXPIRATIONS, GENERIC COMPETITION PRESSURE THE INDUSTRY

The pharmaceutical industry faces an unprecedented number of patent expirations in the coming years, a primary factor cited by experts as limiting industry growth. For the industry as a whole, the introduction of new products is not expected to generate the same magnitude of industry sales as the products losing market exclusivity.

The ability to successfully secure and defend intellectual property rights is particularly relevant with regard to the Pharmaceuticals and Alcon Divisions, as well as key products of our other divisions. The loss of exclusivity for one or more important products – due to patent expiration, generic challenges, competition from new patented products, or changes in regulatory status – will have a material negative impact on the Group's results of operations. Novartis takes legally permissible steps to defend its intellectual property rights, including initiating patent infringement lawsuits against generic drug manufacturers.

Some of our best-selling products have begun to face significant competition due to the end of market exclusivity resulting from the expiry of patent protection.

– The patent on valsartan, the active ingredient of *Diovan/Co-Diovan/Diovan HCT* (high blood pressure), expired in the major countries of the EU in November 2011, and generic competitors have launched there. In addition, patent protection is scheduled to expire in the US in September 2012 and in Japan in 2013. Valsartan is also used in the single-pill combination therapies *Exforge* and *Exforge HCT* (high blood pressure). While market exclusivities for *Exforge/Exforge HCT* will remain in the EU and Japan due to regulatory exclusivities, there is a risk that generic manufacturers may circumvent regulatory exclusivity and gain approval of a combination valsartan-amlodipine product in Europe. In the US, under a license agreement with a generics manufacturer, the product is expected to face generic competition in the US beginning in October 2014.
– The patent on *Femara* (cancer) expired in 2011 in the US and in major European markets, and generic competitors have launched in those markets.
– The patent on zoledronic acid, the active ingredient in *Zometa* (cancer), as well as in *Reclast/Aclasta* (osteoporosis), will expire in 2013 in the US and in 2012 and 2013 in other major markets.
– The patent on *Glivec/Gleevec* (cancer) will expire in 2015 in the US, in 2016 in the major EU countries and 2014 in Japan, in each case including extensions.

We aim to replace revenue lost from such products with revenue from our recently launched products (products launched since 2007 comprised 25% of our sales in 2011) and we believe that these products have the potential for significant additional sales. Nevertheless, the loss of sales from key products remains a major challenge to our business.

INCREASING REGULATORY, SAFETY HURDLES

Our ability to continue to grow our business and replace sales lost due to the end of market exclusivity in the mid- to long-term depends upon the success of our research and development activities in identifying and developing breakthrough products that address unmet needs, are accepted by regulators, patients and physicians, and are reimbursed by payors. Developing new pharmaceutical, biologic, medical device and vaccine products and bringing them to market, however, is a costly, lengthy and uncertain process. In an effort to ensure product safety, authorities are placing greater emphasis on the risk/benefit profile of healthcare products, with particular attention to the value-add and differentiation of products. This focus has led to requests for more clinical trial data, the inclusion of a significantly higher number of patients in clinical trials and more detailed analysis of the trials. As a result, the process of obtaining regulatory approvals for products has become even more arduous.

The post-approval regulatory burden on healthcare companies has also been growing. Increasingly, approved drugs have been subject to requirements such as Risk Evaluation and Mitigation Strategies (REMS), Risk Management Plans, comparative effectiveness studies, Health Technology Assessments and requirements to conduct post-approval Phase IV clinical trials to gather detailed safety and other data on products. These requirements make the maintenance of regulatory approvals and achievement of reimbursement for our products increasingly expensive and further heighten the risk of recalls, product withdrawals, or loss of market share. Going forward, we expect that there will be even greater regulatory attention to minimizing risk and maximizing benefit on the level of the individual patient.

While Novartis continues to be one of the industry leaders in approvals, similar to our industry peers we have been required by health authorities to conduct additional clinical trials and to submit additional analyses of our data in order to obtain product approvals. We have also had REMS and other such requirements imposed as a condition of approval of our new drugs. These factors have increased our costs and caused delays in obtaining approvals of new products, and have created a risk that safe and effective prod-

ucts will not be approved or will be removed from the market after having been approved. For example, in late December, following the seventh interim review of data from the ALTITUDE study with *Tekturna*/*Rasilez* (aliskiren), Novartis announced that the trial was halted on the recommendation of the independent Data Monitoring Committee (DMC) overseeing the study. The DMC concluded that patients were unlikely to benefit from treatment on top of standard anti-hypertensive medicines, and identified higher adverse events in patients receiving *Tekturna*/*Rasilez* in addition to standard of care as part of the trial. Following discussions with health authorities, Novartis wrote to healthcare professionals worldwide recommending that hypertensive patients with diabetes should not be treated with *Tekturna*/*Rasilez*, or combination products containing aliskiren, if they are also receiving an angiotensin-converting enzyme (ACE) inhibitor or angiotensin receptor blocker (ARB). As an additional precautionary measure, Novartis ceased promotion of *Tekturna*/*Rasilez*-based products for use in combination with an ACE inhibitor or ARB.

Novartis aims to counter such challenges through our focus on innovation and our emphasis on understanding disease pathways, which we believe will enable us to continue to bring differentiated new medicines to the market that effectively address patients' unmet medical needs. Alcon, for example, is the market leader in ophthalmic surgical products, and its line of *AcrySof* intraocular lenses has revolutionized cataract treatment, with over 40 million lenses implanted worldwide. Similarly, in the development of *Bexsero*, our vaccine candidate against the B serogroup of meningococcal disease (MenB, the most common cause of bacterial meningitis), Novartis Vaccines has pioneered a new approach called "reverse vaccinology." This approach involves decoding the genetic makeup of MenB and selecting those proteins that are most likely to be broadly-effective vaccine candidates. While *Bexsero* is still under regulatory review, it could potentially provide a solution to a major public health concern for which there is no effective routine vaccine.

RISK OF LIABILITY AND SUPPLY DISRUPTION FROM MANUFACTURING ISSUES

The manufacture of our products is heavily regulated by governmental health authorities around the world, and such health authorities continue to intensify their scrutiny of manufacturers' compliance. If we or our third-party suppliers fail to comply with their requirements, then we could be faced with product shortages or an inability to supply product to patients, resulting in a loss of revenue and potential third-party litigation. In addition, health authorities have begun to impose significant penalties for failures to comply with current Good Manufacturing Practices regulations (cGMP), and have the power to delay the approval of new products to be manufactured at the impacted site.

Like our competitors, we have faced, and continue to face, significant manufacturing issues. For example, in November 2011, we received a Warning Letter from the FDA with respect to three of our Sandoz facilities: Broomfield, Colorado; Wilson, North Carolina; and Boucherville, Canada. The Warning Letter raised concerns regarding compliance with FDA cGMP regulations at these facilities, and stated that until the FDA confirms that the situation has been rectified, it may recommend disapproval of any pending applications or supplements listing Novartis affiliates as a drug manufacturer. Novartis is collaborating with the FDA to promptly correct all concerns raised in the Warning Letter, and to ensure that our products are safe, effective and meet the highest quality standard for the patients who rely on them. However, if we are unable to fully resolve the issues raised in the Warning Letter, then we could be subject to legal action without further notice.

Additionally, in December 2011, Novartis Consumer Health voluntarily suspended operations at its US manufacturing facility in Lincoln, Nebraska, and subsequently recalled certain products. As of the date of this report, it is not possible to determine when the plant will resume full operations. The Lincoln facility produces a variety of products with annual sales value of less than 2% of Novartis Group sales. Should we fail to complete the planned improvements at the site in agreement with the FDA in a timely manner, then we may suffer a significant loss in sales. While this action was taken as a precautionary measure, it reinforced our commitment to a single high quality standard for the entire Novartis Group, and we are making the necessary investments to implement this standard across the network. However, ultimately, there can be no guarantee of the outcome of these matters. Nor can there be any guarantee that we will not face similar issues in the future, or that we will successfully resolve such issues when they arise.

In addition to regulatory requirements, many of our products involve technically complex manufacturing processes or require a supply of highly specialized raw materials. For some products and raw materials, we may also rely on a single source of supply. In particular, an increasing portion of our portfolio, including products from our Pharmaceuticals, Alcon, Vaccines and Diagnostics, and Sandoz Divisions, are "biologic" products. Unlike traditional "small-molecule" drugs, biologic drugs or other biologic-based products cannot be manufactured synthetically, but typically must be produced from living plant or animal micro-organisms. As a result, the production of biologic-based products that meet all regulatory requirements is especially complex. Even slight deviations at any point in the production process may lead to batch failures or recalls. In addition, because the production process is based on living micro-organisms, the process could be affected by contaminants, which could impact those micro-organisms. As a result, the inherent fragility of certain of our raw material supplies and production processes may cause the production of one or more of our products to be disrupted, potentially for extended periods of time.

Also as part of the Group's portfolio of products, we have a number of sterile products, including oncology products, which are considered to be technically complex to manufacture and require strict environmental controls. Any change in the environment may impact production schedules and inadvertently affect supply until remediated.

POTENTIAL LIABILITY ARISING FROM LEGAL PROCEEDINGS

In recent years, there has been a trend of increasing litigation against the industries of which we are a part, especially in the United States. A number of our subsidiaries are, and will likely continue to be, subject to various legal proceedings that arise from time to time. As a result, we may become subject to substantial liabilities that may not be covered by insurance. Litigation is inherently unpredictable, and large verdicts can occur. As a consequence, we may in the future incur judgments or enter into settlements of claims that may have a material adverse effect on our results of operations or cash flows.

In recent years, governments and regulatory authorities have been stepping up their compliance and law enforcement activities in key areas, including marketing practices, antitrust, trade sanctions and corruption. Our businesses have been subject to significant civil litigation as well as governmental investigations and information requests by regulatory authorities.

For example, in 2010 our US affiliate Novartis Pharmaceuticals Corporation (NPC) settled parallel civil and criminal investigations by the US government into allegations of potential inappropriate marketing and promotion of six Novartis drugs. As part of the settlement, NPC agreed to plead guilty to one misdemeanor, and to resolve civil charges against it, agreed to pay a total of USD 422.5 million and enter into a five-year Corporate Integrity Agreement.

At the same time, our Sandoz Division may, from time to time, seek approval to market a generic version of a product before the expiration of patents claimed by the marketer of the patented product. We do this in cases where we believe that the relevant patents are invalid, unenforceable, or would not be infringed by our generic product. As a result, affiliates of our Sandoz Division frequently face patent litigation, and in certain circumstances, we may elect to market a generic product even though patent infringement actions are still pending. Should we elect to proceed in this manner and conduct a "launch at risk," we could face substantial damages if the final court decision is adverse to us.

Adverse judgments or settlements in any of these cases could have a material adverse effect on our business, financial condition and results of operations. See note 20 to our consolidated financial statements for further information on legal proceedings. At the same time, we have in place, and always seek to strengthen a significant compliance with law program. As part of our broad commitment to compliance, we are implementing a revised Code of Conduct, containing our fundamental principles and rules concerning ethical business conduct.

THE GLOBAL ECONOMIC CRISIS THREATENS OUR RESULTS

Many of the world's largest economies and financial institutions continue to be impacted by the ongoing global economic and financial crisis, with some continuing to face financial difficulty, a decline in asset prices, liquidity problems and limited availability of credit. It is uncertain how long these effects will last, or whether economic and financial trends will worsen or improve. Such uncertain economic times may have a material adverse effect on our revenues, results of operations, financial condition and ability to raise capital. For example, the ongoing debt crisis in certain countries in Europe has increased pressures on those countries, and on payors in those countries to force healthcare companies to decrease the prices at which we may sell them our products. The debt crisis has also given rise to concerns that some countries may not be able to pay us for our products at all. This situation could deteriorate as a result of potential developments in countries of key concern such as Greece, which is facing possible default of its sovereign debt obligations, as well as Spain and Italy, the sovereign debt obligations of which were recently downgraded.

Current economic conditions may adversely affect the ability of our distributors, customers, suppliers and service providers to obtain the liquidity required to pay for our products, or otherwise to buy necessary inventory or raw materials, and to perform their obligations under agreements with us, which could disrupt our operations, and negatively impact our business and cash flow. Although we attempt to monitor these third parties' financial condition and their liquidity, our ability to do so is limited, and some of them may become unable to pay their bills in a timely manner, or may even become insolvent, which could negatively impact our business and results of operations. These risks may be elevated with respect to our interactions with third parties with substantial operations in countries where current economic conditions are the most severe, particularly where such third parties are themselves exposed to sovereign risk from business interactions directly with fiscally-challenged government payers.

In addition, the varying effects of difficult economic times on the economies and currencies of different countries has impacted, and may continue to unpredictably impact, the conversion of our operating results into US dollars, our reporting currency. This is particularly so given recent financial troubles in the US and in many European economies, investor concerns about the future of the Euro, and the flight of investor capital to the perceived safety of the Swiss franc.

NOVARTIS STRATEGIES FOR SUSTAINABLE GROWTH

The cornerstone of Novartis strategy is our diversified healthcare portfolio across high-growth segments of the healthcare industry and geographies. Novartis is the only healthcare company with leading positions in pharmaceuticals, eye care, generics, vaccines and diagnostics, over-the-counter medicines and animal health.

We believe that the diversity of our business and product portfolio allows us to capture opportunities across the global healthcare market, while balancing our risk and exposure to macroeconomic effects. We expect our broad portfolio will help us maintain growth despite the loss of revenues due to patent expiration.

OUR PRIORITIES: INNOVATION, GROWTH AND PRODUCTIVITY

Novartis is committed to becoming the most successful and respected healthcare company in the world. To achieve this, we

base our operations on three strategic priorities: leading innovation through new research methods and new collaborations with industry stakeholders to better address customer and patient needs; accelerating growth by responding to key market opportunities and delivering new treatments quickly and efficiently to customers and patients; and improving productivity by streamlining our organization in order to improve profitability and free up resources for new research and development investments. We believe that by focusing on these principles we can enhance our capabilities in meeting the world's healthcare needs and continue to drive value for our shareholders.

EXTENDING OUR LEAD IN INNOVATION

Our commitment to scientific innovation underpins all our strategic principles. Sustaining innovation and R&D productivity across our businesses requires substantial investment and commitment, and we plan to continue to invest at the high end of the industry average. In 2011, we invested more than 20% of Pharmaceuticals Division sales. Our research approach, which focuses on understanding diseases and their molecular pathways, has fundamentally changed how we do business. Researching these pathways allows us to establish "proof of concept" via small clinical studies, sometimes in rare diseases, early in the research and development process. In some of those cases, regulatory approval may be achieved relatively quickly because of the urgent unmet need of patients with such rare diseases. While growth is supported by the initial launch of the given compound in the targeted population, we are sometimes also able to conduct parallel development into other potential treatment applications, which may have much larger patient populations.

For example, *Afinitor*, our kidney cancer treatment, received approval from the FDA and EMA in 2011 for the treatment of advanced pancreatic neuroendocrine tumors. The active ingredient in *Afinitor*, everolimus, was also approved as *Votubia* in the EU for the treatment of subependymal giant cell astrocytoma associated with tuberous sclerosis complex for which surgery is not a treatment option. Late-stage studies also showed that *Afinitor*, in combination with exemestane, significantly lengthens the amount of time women with advanced breast cancer live without the disease progressing.

Our track record of bringing new medicines to the market continues to be among the best in the industry. In 2011, our Pharmaceuticals Division secured approval for 15 new products and important indication extensions in the US, EU and Japan.

We believe that our focus on innovation will enable us to continue to produce breakthroughs that address unmet patient need and further grow our business.

ACCELERATING GROWTH ACROSS OUR FIVE PLATFORMS

Novartis aims to drive growth in two key ways: via the introduction of innovative new products as described above, and through expansion of our business in fast-growing emerging markets.

Innovative products from across our portfolio are making a major contribution to the Group's overall growth, with recently launched products growing 38% in 2011 versus the previous year, now representing 25% of total sales. In the Pharmaceuticals Division, recently launched products include: *Gilenya*, the first oral multiple sclerosis treatment; *Lucentis*, our treatment for wet age-related macular degeneration, which is being expanded to new indications; our kidney cancer treatment *Afinitor*, which has been granted additional indications; and *Galvus*, our oral medication for treatment of type-2 diabetes.

The addition of Alcon, our newest and second largest division, brings more new products to our portfolio, such as advanced technology intraocular lenses used in cataract surgery. In Sandoz, strong growth of biosimilars, the generic versions of biologic drugs, and generic injectables, such as the blood-thinning medication enoxaparin, are also helping to transform the growth prospects of the Group. In Vaccines and Diagnostics, our meningococcal disease franchise is also growing strongly, driven by the increase of *Menveo* market share in the United States and the growth of our meningitis C vaccine in emerging markets.

Given the current cost pressures in the market for prescription medicines, we believe there is ample scope to expand our Sandoz Division, as well as our Consumer Health businesses. We have refocused the portfolio of Consumer Health, which comprises OTC and Animal Health, on core priority brands, a strategy that has enabled Consumer Health to post 3% sales growth in constant currencies in 2011.

The prosperity of the developing world is expected to increase in the coming years, driving growth in our industry. It is estimated that by 2030 emerging markets will account for about 60% of global GDP. This economic growth is greatly expanding access to healthcare in these geographies. Consistent with our long-term growth strategy, we continue to build our presence in high-growth markets around the world, particularly in our top six emerging markets, comprising Brazil, China, India, Russia, South Korea and Turkey. Long-term investments in these areas are crucial to winning market share and being well-positioned to capture the opportunities that expected growth in these markets will offer.

Many of these emerging markets have little, if any, distinction between pharmaceutical, OTC and generic products. Given the Novartis Group's portfolio, we believe that we have an advantage in such markets, since we offer a broad spectrum of medicines to treat a range of diseases. To take full advantage of the growth opportunities in emerging markets, we have launched many market-tailored initiatives. In China, we plan to continue to expand our commercial infrastructure and capabilities, while also pursuing targeted licensing, acquisition and alliance opportunities. In Brazil, we are leveraging our broad portfolio in order to gain scale to compete with consolidating retail channels and provide key accounts with the full range of Novartis offerings. In India, we are leveraging the capabilities of Pharmaceuticals, Sandoz, and Vaccines and Diagnostics to gain critical mass, and investing in localized products and commer-

cial infrastructure. In Russia, we are building alliances with government, regions and local companies and strengthening key account management to expand our reach.

As a result of such initiatives, in 2011 Novartis generated USD 5.8 billion, or approximately 10% of net sales, from the Group's top six emerging markets. However, combined net sales in the top six emerging markets grew at the more rapid pace of 17% in constant currencies in 2011, compared to 11% constant currency growth achieved in the seven largest developed markets. Hence, emerging markets are making increasingly significant contributions to our results, a trend we expect to continue, as we plan to continue investing in these markets.

DRIVING PRODUCTIVITY

Novartis integrates efforts toward greater productivity and increased efficiency into all our operations, constantly seeking ways to simplify and streamline processes and to reduce costs to improve margins. We are committed to freeing up resources that can be devoted to customer and growth initiatives, research and development of new offerings for patients with unmet needs, and shareholder returns. There are four key areas where we target productivity improvements across our businesses: our manufacturing footprint, Procurement, General & Administration expenses and Marketing & Sales spend.

In 2010, we initiated a Group-wide program to review our manufacturing footprint, which continued to progress in 2011. The program has two aims: first, to optimize the network by creating Manufacturing Centers of Excellence to best support the global operations of the Group across divisions, and second, to optimize the cost structure across divisions and enhance utilization rates at strategic sites to 80 percent of capacity. To these ends, we announced the exit or partial exit of 14 sites since the program started in 2010, thereby reducing excess capacity and enabling the shift of strategic production to technology competence centers.

Additional efficiencies are expected through Marketing & Sales spend, as Novartis continues to reallocate resources geographically and simplify prevailing processes. As a percentage of sales, Marketing & Sales spend has decreased from 26.3% in 2010 to 25.7% in 2011, down 3.5 percentage points since 2007.

In addition, we made Procurement a major source of savings by leveraging our scale, implementing global category management and creating country Centers of Excellence in key markets, which generated annual savings in 2011 of approximately USD 1.3 billion.

Novartis also continuously looks for ways to simplify its structures, especially with regard to General & Administration expenses. The streamlining of core processes across the Group and the implementation of core service centers for functions such as Human Resources and Finance will further provide leverage and resources for reinvestment.

NOVARTIS BUSINESSES FACE OPPORTUNITIES AND CHALLENGES

Novartis believes that its portfolio of healthcare businesses gives us a strong position to meet many of the needs of customers and patients in today's healthcare marketplace, which is expected to grow 5.5% (CAGR) between 2011 and 2016. In the view of Novartis, sustained growth in the healthcare industry requires the capacity to adapt to changing and expanding markets worldwide, to collaborate with industry stakeholders, and to deliver new treatments based on new medical advancements that improve patient health. We believe that Novartis has both the scope and innovative capacity to succeed in all these areas. For example, we have a highly competitive and robust pipeline with more than 130 projects in clinical development, including 66 new molecular entities. We have also achieved a strong level of launch excellence, with recently launched products growing 38% (excluding A(H1N1)) over the previous year.

Novartis maintains a leadership position in developing and delivering prescription medicines (Pharmaceuticals, which represents 56% of net sales in 2011), innovative eye care products (Alcon, 17%), complex, differentiated generics and biosimilars (Sandoz, 16%), preventative vaccines and diagnostic tools (Vaccines and Diagnostics, 3%), and market-leading over-the-counter offerings and medicines for animals (Consumer Health, 8%). According to IMS, these sectors are expected to grow between 2% per year (Pharmaceuticals) and 8% per year (Vaccines) from 2011 to 2016. Additionally, we have positioned ourselves to capture significant marketplace opportunities across geographies, with 37% of 2011 net sales in Europe, 33% in the US, 21% in Asia, Africa and Australasia, and 9% in Canada and Latin America, helping to mitigate the impact of currency fluctuations. Consequently, Novartis is not dependent for growth on any one product, region, or market. Our growth is sustained by our strong position in diverse market segments, with a focus on the areas of greatest customer and patient need.

While Sandoz can benefit from government pressure on prices, the healthcare landscape continues to offer growth opportunities for patented pharmaceuticals as well. We believe that the Novartis portfolio will allow us to continue to grow and to improve healthcare outcomes for patients across treatment categories all over the world.

PHARMACEUTICALS: FILLING UNMET NEED THROUGH DIFFERENTIATED DRUGS

Novartis has developed innovative medicines for the treatment of cancer, cardiovascular disease, and neurological conditions, among others. Yet urgent patient needs remain, as many diseases and conditions lack effective treatments or any treatment at all. This is why we continue to focus our research on areas of high unmet medical need and where the fundamental science is well understood. Our dedicated Molecular Diagnostics unit seeks to improve the efficacy of our medicines by identifying biomarkers in patient groups that respond to the new medicines. This is intended to enable us to focus our research on smaller, narrowly defined groups of patients. Such patient segmentation is intended to assist us in accelerating the

development of therapies that have the potential to be more targeted and effective with better patient outcome and fewer side effects.

Furthering our commitment to individualized treatment, we acquired United States-based oncology laboratory Genoptix, which diagnoses bone, blood and lymph cancers and disorders for hematologists and oncologists. The acquisition enhances the Group's tools and services that aim to improve health outcomes by advancing the ability to define and monitor individualized treatment programs. The business provides a strategic fit with our current portfolio of companion diagnostic programs within the Novartis Molecular Diagnostics unit.

Underpinning our Pharmaceuticals Division's growth is our ability to rejuvenate our portfolio through innovative new products. This is expected to allow us to sustain growth even in the face of factors such as patent loss, increased generics competition and government pricing caps. Although hypertension medication *Diovan* and breast cancer treatment *Femara* lost patent protection in several core markets in 2011, losses are expected to be offset in the years ahead by sales growth from recently launched products, including *Lucentis*, *Tasigna*, *Galvus*, *Gilenya*, *Afinitor*, *Xolair* and *Onbrez Breezhaler*. In 2011, recently launched products (those launched since 2007) accounted for 28% of net sales, compared to 22% in 2010. We expect these products, as well as new products anticipated to be launched over the next five years, to generate an increasing proportion of our sales.

Our Pharmaceuticals pipeline is one of the most productive in the industry – with higher success rates at every stage of development, preclinical through registration, than our competitors – which we expect to compensate for the anticipated loss of revenues from patent expirations. For example, our investigational compound INC424 has shown significant potential in treating patients with myelofibrosis, a life-threatening blood cancer, in Phase III trials. Another Phase III study showed that 45% of children with active systemic juvenile idiopathic arthritis were able to substantially reduce their use of steroids following treatment with ACZ885, and were nearly three times less likely to suffer a new flare versus placebo. We plan to continue to invest in R&D at the high end of the industry average to sustain our industry-leading investment in R&D, which we believe will allow us to discover and develop new targeted therapies like these to better meet the needs of patients worldwide.

ALCON: THE WORLD LEADER IN EYE CARE

As the global population continues to age, healthcare demands in eye care are expected to accelerate. For example, it is estimated that by 2020, 60 million people will have open-angle glaucoma and 2.5 billion will be affected by myopia (nearsightedness) globally. As a result, eye care has been one of the fastest growing therapeutic areas in the healthcare industry.

Novartis has long held an established position in the eye care segment through CIBA Vision and our Novartis Ophthalmics portfolio. In 2011, we secured 100% ownership of Alcon, Inc., the world's largest eye care company, and merged it into Novartis. The merger with Alcon gives us an even larger footprint in the attractive, high-growth sector of eye care.

By combining our complementary businesses, Novartis and Alcon are better able to address patient need and create value for shareholders. The new Alcon Division now holds competitive positions in highly complementary product areas, spanning surgical equipment and technology, prescription medicines, contact lenses and lens care products. The world leader in ophthalmic surgery, Alcon offers advanced surgical technology such as intraocular lenses that simultaneously correct for presbyopia, which affects all cataract patients, and astigmatism, which affects about one-third of these patients.

We have also strengthened our innovation capabilities, with Alcon scientists working alongside Novartis associates at NIBR to discover expanded ophthalmic research targets and develop chemical and biologic compounds for diseases of the eye, with a particular focus on diseases such as glaucoma and macular degeneration.

We believe the integration of Alcon into the broader Group will also enable us to realize annual cost synergies of USD 350 million by 2013.

SANDOZ: CREATING AFFORDABLE, EFFECTIVE ALTERNATIVES TO COMPLEX DRUGS

By 2016, patented pharmaceuticals with global annual sales totaling around USD 200 billion are expected to lose their patent protection and face potential competition from generic alternatives, according to the research firm EvaluatePharma. In addition, governments and healthcare providers worldwide are increasingly transitioning to generic medicines as an alternative to patented prescription products in order to contain overall healthcare spending.

There is a particular demand for generic alternatives to complex patented treatments, as these treatments are often among the most costly. This demand has made the market for differentiated, "difficult-to-make" generics one of the fastest growing and most attractive segments of the generics industry. Sandoz has established itself as a leader in developing differentiated products, including inhalers, oncology injectables, patches, and biosimilars, generic versions of biologic drugs. The significant technological capabilities and expertise required make the development of such treatments difficult for most companies. However, Sandoz has been effective in leveraging the innovative and technological capabilities and commercial scope of the entire Novartis Group in order to overcome these hurdles. In 2011, Sandoz achieved blockbuster success with generic enoxaparin based on a strong first-to-market launch in 2010, underscoring our leadership in differentiated products.

Sandoz has also had success in creating highly complex biosimilars, achieving global sales of USD 261 million in 2011, an increase of 37% in constant currencies over the previous year. Sandoz is also the first and only company with more than one biosimilar on the market in Europe and achieved the first-ever biosimilar approvals in the US, Japan and Canada. With patents expected to expire over the next four years on biologics with global sales of USD 64 billion,

our leading position in biosimilars gives us an advantage within the competitive generics industry. Moreover, our strong biosimilars pipeline, with more than eight molecules in development and two projects in Phase III as of the end of 2011, gives us an opportunity to remain at the forefront of this key sector, driving continued growth and making healthcare more affordable for patients.

We also plan to continue to expand our generics success in emerging markets and accelerating growth in mature markets such as the United States. With the full integration of Alcon into the Novartis Group, the Sandoz US portfolio has been broadened with the ophthalmic and optic products of Falcon Pharmaceuticals, Ltd., Alcon's US generics business. The addition of this new portfolio has made Sandoz the largest manufacturer and marketer of generic ophthalmic and optic products in the US.

VACCINES AND DIAGNOSTICS: PREVENTING DISEASE

As global healthcare costs rise and chronic diseases become a greater burden in emerging markets, the prevention of disease has taken on new urgency. Governments and payors are increasingly recognizing the essential roles of vaccines and blood screening in prevention, and in generally maintaining worldwide health.

The vaccines market continues to expand, with expected growth of approximately 8-10% annually for the next five years. We are focused on developing safe and effective methods to better prevent various forms of the flu as well as other major causes of human illness. Novartis Vaccines research is leading advances in the way vaccines are made so that we can bring patients novel offerings to effectively prevent devastating infectious diseases. Our meningococcal disease franchise is growing strongly, driven by the increase of *Menveo* market share in the United States and the growth of our meningitis C vaccine, *Menjugate*, in emerging markets. *Menveo* sales achieved USD 142 million in 2011, and we continue to expand this franchise. In June, the FDA accepted our application to expand the *Menveo* indication to include infants and toddlers as young as two months, supported by clinical data from more than 6 000 children worldwide between the ages of 2 and 23 months. If approved, *Menveo* would be the first quadrivalent meningococcal conjugate vaccine to provide protection in the first year of life, when the majority of infections occur. Meanwhile, our vaccine candidate against the B serogroup of meningococcal disease, *Bexsero,* is nearing the completion of the regulatory review process in Europe, Canada and other regions with high disease incidence.

We have successfully incorporated cutting-edge technologies into our Vaccines and Diagnostics research practices, including the use of genomics and reverse vaccinology. These processes were essential, for instance, in the development of our response to the A(H1N1) pandemic flu in 2009, and in our development of *Bexsero*. Work is ongoing on vaccine candidates in our earlier development pipeline, including, for example, vaccines against Group B streptococcus, staph aureaus and pseudomonas aeruginosa.

In 2011 we completed our acquisition of majority control of Zhejiang Tianyuan, a Chinese vaccines manufacturer, facilitating greater access to China as part of our strategy to strengthen our presence in key emerging markets and provide vaccines for patients with critical unmet needs.

CONSUMER HEALTH: OFFERING SELF-MEDICATION OPTIONS TO PATIENTS AND VETERINARY MEDICINES FOR ANIMALS

Accelerated healthcare spending is leading governments, payors and other healthcare providers to seek ways to reduce overall healthcare costs. In many cases, over-the-counter (OTC) medicines represent a cheaper, effective alternative to prescription options. In addition, wider availability of health information via the Internet, which empowers patients to play a greater role in their own healthcare, can lead them to choose OTC offerings in treating or preventing illness. Our continued focus on priority brands within OTC delivered strong results, with several of those brands growing at a double-digit rate over the prior year, offsetting the negative impact of expired distribution contracts and divested brands. However, at the end of 2011, OTC experienced net sales decline due to a temporary suspension of operations and voluntary product recall at one of the US manufacturing sites. We are focused on driving growth by increasing the scale of business in top markets and expanding our portfolio in core disease areas, such as gastrointestinal and pain relief. OTC sales in the top six emerging markets also grew at a double-digit rate in 2011, led by Russia, Brazil and China, where the division launched *Lamisil* to compete in the growing anti-fungal market.

Another way we can maximize our return on investment in research into new medicines is by leveraging that investment by extending our work in Animal Health, potentially generating incremental sales on the dollars invested in R&D. In many cases, our Pharmaceuticals Division's medicines, in adjusted doses and dosage forms, have applications for pets and farm animals. In fact, about a third of the Animal Health R&D portfolio consists of projects from the human health pipeline. We have been able to leverage synergies across R&D and manufacturing to make Animal Health an important second stream of growth for our new and existing treatments. We continue to sustain Animal Health's leading position in specialty segments, with strong performance of the pig therapeutic *Denagard* in the United States, China and Brazil. In Europe, *Milbemax* remained the number one de-wormer for cats and dogs, with the new chewy formulation accelerating growth. Key emerging markets continue to contribute strong double-digit growth to our Animal Health business globally.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our principal accounting policies are set out in note 1 to the Group's consolidated financial statements and are prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB). Given the uncertainties inherent in our business activities, we must make certain estimates and assumptions that require difficult, subjective and complex judgments. Because of uncertainties inherent in such judgments, actual outcomes and results may differ from our assumptions and estimates which could materially affect the Group's consolidated financial statements. Application of the following accounting policies requires certain assumptions and estimates that have the potential for the most significant impact on our consolidated financial statements.

REVENUE

We recognize product sales when there is persuasive evidence that a sales arrangement exists, title and risk and rewards for the products are transferred to the customer, the price is determinable, and collectability is reasonably assured. Where contracts contain customer acceptance provisions we recognize sales upon the satisfaction of acceptance criteria.

At the time of recognizing revenue, we also record estimates for a variety of sales deductions, including rebates, discounts, refunds, incentives and product returns. Sales deductions are reported as a reduction of revenue.

DEDUCTIONS FROM REVENUES

As is typical in the pharmaceuticals industry, our gross sales are subject to various deductions that are composed primarily of rebates and discounts to retail customers, government agencies, wholesalers, health insurance companies and managed healthcare organizations. These deductions represent estimates of the related obligations, requiring the use of judgment when estimating the effect of these sales deductions on gross sales for a reporting period. These adjustments are deducted from gross sales to arrive at net sales.

The following summarizes the nature of some of these deductions and how the deduction is estimated. After recording these, net sales represent our best estimate of the cash that we expect to ultimately collect. The US market has the most complex arrangements related to revenue deductions.

US SPECIFIC HEALTHCARE PLANS AND PROGRAM REBATES

– The US Medicaid Drug Rebate Program is administered by State governments using State and Federal funds to provide assistance to certain vulnerable and needy individuals and families. Calculating the rebates to be paid involves interpreting relevant regulations, which are subject to challenge or change in interpretative guidance by government authorities. Provisions for estimating Medicaid rebates are calculated using a combination of historical experience, product and population growth, product price increases and the mix of contracts and specific terms in the individual State agreements. These provisions are adjusted based on established processes and experiences from re-filing data with individual States.
– The US Federal Medicare program, which funds healthcare benefits to individuals age 65 or older, provides prescription drug benefits under Part D of the program. This benefit is provided through private prescription drug plans. Provisions for estimating Medicare Part D rebates are calculated based on the terms of individual plan agreements, product sales and population growth, product price increases and the mix of contracts.
– We offer rebates to key managed healthcare plans to sustain and increase market share for our products. These rebate programs provide payors a rebate after they attain certain performance parameters related to product purchases, formulary status or pre-established market share milestones relative to competitors. These rebates are estimated based on the terms of individual agreements, historical experience and projected product growth rates. We adjust provisions related to rebates periodically to reflect actual experience.
– There is often a time lag of several months between us recording the revenue deductions and our final accounting for the revenue deductions.

NON-US SPECIFIC HEALTHCARE PLANS AND PROGRAM REBATES

– In certain countries, other than the US, we provide rebates to governments and other entities. These rebates are often mandated by laws or government regulations.
– In several countries we enter into innovative pay-for-performance arrangements with certain healthcare providers, especially in the UK, Germany and Australia. Under these agreements, we may be required to make refunds to the healthcare providers or to provide additional medicines free of charge if anticipated treatment outcomes do not meet predefined targets. Potential refunds and the delivery of additional medicines at no cost are estimated and recorded as a deduction of revenue at the time the related revenues are recorded. Estimates are based on historical experience and clinical data. In cases where historical experience and clinical data are not sufficient for a reliable estimation of the outcome, revenue recognition would be deferred until such history would be available.
– There is often a time lag of several months between us recording the revenue deductions and our final accounting for the revenue deductions.

NON-HEALTHCARE PLANS AND PROGRAM REBATES, RETURNS AND OTHER DEDUCTIONS

– Charge-backs occur where our subsidiaries have arrangements with indirect customers to sell products at prices that are lower than the price charged to wholesalers. A chargeback represents the difference between the invoice price to the wholesaler and the

indirect customer's contract price. We account for vendor charge-backs by reducing revenue by an amount equal to our estimate of charge-backs attributable to a sale and they are generally settled within one to three months of incurring the liability. Provisions for estimated charge-backs are calculated using a combination of factors such as historical experience, product growth rates, payments, level of inventory in the distribution channel, the terms of individual agreements and our estimate of the claims processing time lag.

– We offer rebates to purchasing organizations and other direct and indirect customers to sustain and increase market share for our products. Since rebates are contractually agreed upon, rebates are estimated based on the terms of individual agreements, historical experience, and projected product growth rates.
– When we sell a product providing a customer the right to return a product, we record a provision for estimated sales returns based on our sales returns policy and historical rates. Other factors considered include product recalls, expected marketplace changes and the remaining shelf life of the product, and the entry of generic products. In 2011, sales returns amounted to approximately 1% of gross product sales. Especially in the Vaccines and Diagnostics Division, if there is no Novartis-specific historical return rate experience available, sales are only recorded based on evidence of product consumption or when the right of return has expired.
– We enter into distribution service agreements with major wholesalers, which provide a financial disincentive for wholesalers to purchase product quantities exceeding current customer demand. Where possible, we adjust shipping patterns for our products to maintain wholesalers' inventories level consistent with underlying patient demand;
– We offer cash discounts to customers to encourage prompt payment. Cash discounts are accrued at the time of invoicing and deducted from revenue.
– Following a decrease in the price of a product, we generally grant customers a "shelf stock adjustment" for a customer's existing inventory for the involved product. Provisions for shelf stock adjustments, which are primarily relevant within the Sandoz Division, are determined at the time of the price decline or at the point of sale if a price decline can be reasonably estimated based on inventory levels of the relevant product;
– Other sales discounts, such as consumer coupons and co-pay discount cards, are offered in some markets. These discounts are recorded at the time of sale, or when the coupon is issued and are estimated utilizing historical experience and the specific terms for each program. If a discount for a probable future transaction is offered as part of a sales transaction then an appropriate portion of revenue is deferred to cover this estimated obligation.
– We adjust provisions for revenue deductions periodically to reflect actual experience. To evaluate the adequacy of provision balances, we use internal and external estimates of the level of inventory in the distribution channel, actual claims data received and the time lag for processing rebate claims. Management also estimates the level of inventory of the relevant product held by retailers and in transit. External data sources include reports of wholesalers and third-party market data purchased by Novartis.

The following table shows the worldwide extent of our revenue deductions provisions and related payment experiences:

PROVISIONS FOR REVENUE DEDUCTIONS

	Revenue deductions provisions at January 1 USD millions	Effect of currency translation and business combinations USD millions	Payments/ utilizations USD millions	Income statement charge: Adjustments of prior years USD millions	Income statement charge: Current year USD millions	Change in provisions offset against gross trade receivables	Revenue deductions provisions at December 31 USD millions
2011							
US specific healthcare plans and program rebates	1 162		– 2 860	– 19	3 157		1 440
Non-US specific healthcare plans and program rebates	575	– 24	– 1 043	– 23	1 281		766
Non-healthcare plans and program related rebates, returns and other deductions	1 360	– 68	– 6 846	– 7	7 324	– 227	1 536
Total 2011	**3 097**	**– 92**	**– 10 749**	**– 49**	**11 762**	**– 227**	**3 742**
2010							
US specific healthcare plans and program rebates							
Non-US specific healthcare plans and program rebates							
Non-healthcare plans and program related rebates, returns and other deductions							
Total 2010							

The table below shows the gross to net sales reconciliation for our Pharmaceuticals division:

GROSS TO NET SALES RECONCILIATION

	Income statement charge: Charged through revenue deduction provisions USD millions	Income statement charge: Charged directly without being recorded in revenue deduction provisions USD millions	Total USD millions	In % of gross sales
2011				
Pharmaceuticals gross sales subject to deductions			**40 004**	**100.0**
US specific healthcare plans and program rebates	– 2 424		– 2 424	– 6.0
Non-US specific healthcare plans and program rebates	– 801	– 408	– 1 209	– 3.0
Non-healthcare plans and program related rebates, returns and other deductions	– 1 631	– 2 232	– 3 863	– 9.7
Total Pharmaceuticals gross to net sales adjustments	**– 4 856**	**– 2 640**	**– 7 496**	**– 18.7**
Pharmaceuticals net sales 2011			**32 508**	**81.3**
2010				
Pharmaceuticals gross sales subject to deductions				
US specific healthcare plans and program rebates				
Non-US specific healthcare plans and program rebates				
Non-healthcare plans and program related rebates, returns and other deductions				
Total Pharmaceuticals gross to net sales adjustments				
Pharmaceuticals net sales 2010				

ACQUISITION ACCOUNTING

The Group's consolidated financial statements reflect an acquired business from the date the acquisition has been completed. We account for acquired businesses resulting in majority ownership using the acquisition method of accounting, which requires the acquired assets and assumed liabilities to be recorded as of the acquisition date at their respective fair values. Any excess of the purchase consideration over the estimated fair values of acquired Group's share of net identified assets is recorded as goodwill in the balance sheet and denominated in the functional currency of the related acquisition. Goodwill is allocated to an appropriate cash-generating unit, which is defined as the smallest group of assets that generates independent cash inflows that support the goodwill.

In-Process Research & Development (IPR&D) is valued as part of the acquisition accounting. Payments for other separately acquired assets in development, such as those related to initial and milestone payments for licensed or acquired compounds, are capitalized as IPR&D intangible assets if they are deemed to enhance our intellectual property. This occurs even if uncertainties continue to exist as to whether the R&D projects will ultimately be successful in producing a commercial product. Estimating the fair value assigned to each class of acquired assets and assumed liabilities is based on expectations and assumptions, from the perspective of a market participant, that have been deemed reasonable by management.

Contingent considerations to former owners agreed in a business combination, e.g., in the form of milestone payments upon the achievement of certain development stages or sales targets as well as royalties, are recognized as liabilities at fair value as of the acquisition date. Any subsequent changes in amounts recorded as a liability are recognized in the consolidated income statement.

IMPAIRMENT OF LONG-LIVED INTANGIBLE AND TANGIBLE ASSETS

We review long-lived intangible and tangible assets for impairment whenever events or changes in circumstance indicate that the asset's balance sheet carrying amount may not be recoverable.

An asset, as defined, is generally considered impaired when its carrying amount exceeds its estimated recoverable amount. The recoverable amount is measuher the R&sma1 Tw T*(r)12(ecover)24(a)1(em0.0u Tc -0.068 1 0 higess-of: a1.6a2(ed ime)bsequent changes in5located to

activities. If additional payments are made to the originator company to continue to perform R&D activities, an evaluation is made as to the nature of the payments. Such additional payments will be expensed if such additional payments are deemed to be compensation for subcontracted R&D services not resulting in an additional transfer of intellectual property rights to Novartis. By contrast, such additional payments will be capitalized if these additional payments are deemed to be compensation for the transfer to Novartis of additional intellectual property developed at the risk of the originator company. Subsequent internal R&D costs in relation to IPR&D and other assets are expensed since the technical feasibility of the internal R&D activity can only be demonstrated by the receipt of marketing approval for a related product from a regulatory authority in a major market.

Costs for post-approval studies performed to support the continued registration of a marketed product are recognized as marketing expenses. Costs for activities that are required by regulatory authorities as a condition for obtaining marketing approval are charged as development expenses as they are incurred, in cases where it is anticipated that the related product will be sold over a longer period than the activities required to be performed to obtain the marketing approval. In the rare cases where costs related to the conditional approval need to be incurred over a period beyond that of the anticipated product sales, then the expected costs of these activities will be expensed over the shorter period of the anticipated product sales.

IPR&D assets are amortized in the consolidated income statement over their useful life once the related project has been successfully developed and regulatory approval for a product launch has been obtained. Other acquired technologies are amortized over their estimated useful lives.

TAXES

We prepare and file our tax returns based on an interpretation of tax laws and regulations and record estimates based on these judgments and interpretations. Our tax returns are subject to examination by the competent taxing authorities, which may result in an assessment being made requiring payments of additional tax, interest or penalties. Inherent uncertainties exist in our estimates of our tax positions. We believe that our estimated amounts for current and deferred tax assets or liabilities, including any amounts related to any uncertain tax positions, are appropriate based on currently known facts and circumstances.

NEW ACCOUNTING PRONOUNCEMENTS

Based on a Novartis analysis, the following new or amended IFRS standards will be of significance to the Group, but have not yet been adopted.

In 2009, 2010 and 2011, sections of IFRS 9 *Financial Instruments* were issued. This standard will ultimately substantially change the classification and measurement of financial instruments, hedging requirements, impairments of financial instruments and the recognition of certain fair value changes in the consolidated financial statements. Currently, only new requirements on the classification and measurement for financial assets and financial liabilities have been issued. The mandatory effective date for requirements issued as part of IFRS 9 will be on or after January 1, 2015. Early application of the requirements is permitted.

In 2011, IAS 19 revised on *Employee Benefits* was issued, for adoption by January 1, 2013. The principal impact for Novartis will be that the concepts of expected return on assets and interest expense on the defined benefit obligation as separate components of defined benefit cost will be replaced by a concept that interest will be calculated on the net of the defined benefit obligation and funded post-employment obligation assets using an interest rate reflecting market yields of high quality corporate bonds in a deep market. If this concept had been adopted by Novartis in 2011, it is estimated that operating income would have been lower by approximately USD 260 million. As required by the standard, Novartis will retrospectively adopt the standard on January 1, 2013.

Two other new standards were also issued in 2011, IFRS 10 *Consolidated Financial Statements* and IFRS 11 *Joint Arrangements* which are potentially important for Novartis. Under IFRS 10, Novartis will need to consolidate an investee based on control, i.e. when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. IFRS 11 will require that Novartis classifies joint arrangements as either joint operations, where assets, liabilities, revenues and expenses are accounted for proportionally in accordance with the agreement, or as joint ventures, which are accounted for under the equity method. These new standards become effective on January 1, 2013.

The following IFRSs and amendments are not yet effective and are not early adopted by the Group.

- IFRS 12, *Disclosures of interests in other entities*, effective for annual periods beginning on or after January 1, 2013
- IFRS 13, *Fair value measurement*, effective for annual periods beginning on or after January 1, 2013
- Amendment to IAS 1, *Presentation of items of other comprehensive income*, effective for annual periods beginning on or after July 1, 2012

Although Novartis is still completing its evaluation of these new standards, apart from where indicated, Novartis does not currently consider that the other new standards will have a significant impact on the Group's consolidated financial statements.

FACTORS AFFECTING COMPARABILITY OF YEAR-ON-YEAR RESULTS OF OPERATIONS

RECENT ACQUISITIONS AND DIVESTMENTS

The comparability of the year-on-year results of our operations for the total Group can be significantly affected by acquisitions and divestments. For more detail how these actions have affected our results, see "Significant Transactions" below.

SIGNIFICANT TRANSACTIONS

ALCON MAJORITY CONTROL IN 2010; FULL OWNERSHIP AND MERGER IN 2011

On August 25, 2010 Novartis completed the acquisition of a further 52% interest in Alcon, Inc. (Alcon) following the January 4, 2010 announcement that Novartis had exercised its call option to acquire Nestlé's remaining 52% Alcon interest for approximately USD 28.3 billion or USD 180 per share. This increased the interest in Alcon to a 77% controlling interest as Novartis had already acquired an initial 25% Alcon interest from Nestlé for USD 10.4 billion or USD 143 per share in July 2008. The overall purchase price for the 77% interest in Alcon of USD 38.7 billion included certain adjustments for Alcon dividends and interest due.

On December 14, 2010 Novartis entered into a definitive agreement to merge Alcon into Novartis in consideration for Novartis shares and a Contingent Value Amount. The acquisition of the remaining outstanding non-controlling interests in Alcon were separate transactions following the previous acquisition of majority ownership in Alcon by Novartis on August 25, 2010. On April 8, 2011 a Novartis Extraordinary General Meeting approved the merger with Alcon, Inc. creating the Alcon Division which became the fifth reported segment in Novartis' strategically diversified healthcare portfolio. The Extraordinary General Meeting also authorized the issuance of 108 million new shares.

Alcon shareholders received 2.9228 Novartis shares (which included a dividend adjustment) and USD 8.20 in cash for each share of Alcon, resulting in a total consideration of USD 168.00 per share.

Following the change in majority control of Alcon on August 25, 2010, it was required for Novartis to reassess the fair value of the initial 25% non-controlling interest in Alcon it acquired from Nestlé in 2008. As the estimated fair value of the initial non-controlling interest exceeded the recorded book value of the initial non-controlling interest, Novartis recorded a revaluation gain. After adjusting for accumulated losses recorded in the Group's consolidated statement of comprehensive income since the initial 25% interest in Alcon was acquired in July 2008, a net amount of USD 335 million was recorded as a gain under "Income from Associated Companies".

After the acquisition of majority ownership in Alcon, Inc. on August 25, 2010, Alcon contributed net sales of USD 2.4 billion and operating income of USD 323 million to the consolidated income statement in 2010.

During 2011, prior to the merger of Alcon, Inc. into Novartis AG on April 8, 4.8% of the non-controlling interests in Alcon, Inc. were acquired for USD 2.4 billion.

Completion of the acquisition of the outstanding 18.6% interest in Alcon on April 8, 2011 and subsequent merger, resulted in the issuance of Novartis shares with a fair value of USD 9.2 billion and a contingent value payment of USD 0.5 billion.

The final purchase price allocation was completed in 2011 and resulted in a fair value of net identifiable assets of USD 27.0 billion and goodwill of USD 18.0 billion. Also, the excess of the value exchanged for these 2011 transactions over the recorded value of the non-controlling interest together with merger related transaction costs resulted in a reduction in equity of USD 5.7 billion.

The accounting for these transactions is explained in more detail in note 1, 2 and 24 to the Group's consolidated financial statements.

Pharmaceuticals – Acquisition of Genoptix, Inc.

On March 7, 2011 Novartis completed the acquisition of Genoptix, Inc., a specialized laboratory providing personalized diagnostic services to community-based hematologists and oncologists. Genoptix employed approximately 500 people and became part of the Novartis Molecular Diagnostics unit within the Pharmaceuticals Division.

The acquisition in cash of 100% of the shares of Genoptix totaled USD 458 million, excluding the USD 24 million of cash acquired. The final purchase price allocation resulted in net identified assets of USD 237 million and goodwill of USD 221 million. Results of operations since the acquisition date were not material.

Vaccines and Diagnostics – Acquisition of Zhejiang Tianyuan

On March 22, 2011 Novartis completed the acquisition in cash of an 85% stake in the Chinese vaccines company, Zhejiang Tianyuan Bio-Pharmaceutical Co. Ltd. The acquisition provides Novartis with an expanded presence in the Chinese vaccines market and is expected to facilitate the introduction of additional Novartis vaccines into China. The total amount paid for the 85% interest was USD 194 million, excluding USD 39 million of cash acquired. The final purchase price allocation resulted in net identified assets of USD 131 million and goodwill of USD 82 million. Non-controlling interests have increased by USD 19 million from this transaction. Results of operations since the acquisition date were not material.

Pharmaceuticals – Divestment of *Elidel*®

On May 11, 2011 Novartis completed the divestment of *Elidel*® Cream 1% to Meda Pharma Sarl and Novartis received an upfront payment of USD 420 million and recognized a gain of USD 324 million in "Other Income".

SEGMENT REPORTING

The businesses of Novartis are divided on a worldwide basis into five reporting segments (Pharmaceuticals, Alcon, Sandoz, Vaccines and Diagnostics and Consumer Health) and Corporate activities. Following the acquisition of all of Alcon, Inc., and merger into Novartis AG on April 8, 2011 a new segment allocation was introduced. As a result, the Alcon Division includes CIBA Vision and certain Pharmaceuticals Division ophthalmology products. Falcon, the US generics business of Alcon, Inc. was transferred to the Sandoz Division. Certain residual operational costs incurred by the now disbanded Consumer Health Divisional headquarters were transferred to Corporate and Corporate R&D was transferred to the Pharmaceuticals Division. All segment results for 2010 and 2011 are presented using this new allocation. Except for Consumer Health, these segments reflect the Group's internal management structure. These segments are managed separately because they each manufacture, distribute and sell distinct products which require differing marketing strategies. In the case of Consumer Health, the segment comprises two divisions which are also managed separately, however, neither of these two divisions is material enough to the Group to be separately disclosed as a segment.

Inter-segmental sales are made at amounts considered to approximate arm's-length transactions. Currently, we principally evaluate segment performance and allocate resources based on operating income, cash flow and cash flow return on invested capital (CFROI).

The following shows an overview of the impact of the restatement on the segmentation structure. Unless otherwise stated this has been used for all years presented in this Annual Report.

Segment	Newly included	Newly excluded
Pharmaceuticals	Corporate R&D	Certain ophthalmic products
Alcon	CIBA Vision, certain ophthalmic products	Falcon
Sandoz	Falcon	
Consumer Health		CIBA Vision; disbanded Consumer Health divisional management costs
Corporate	Disbanded Consumer Health divisional management costs	Corporate R&D

A summary of the above restatements on 2010 sales, operating income and core operating income is as follows:

Segment (USD m)	Net sales	Operating income	Core operating income
Pharmaceuticals	– 252	– 327	– 323
Alcon	2 020	473	498
Sandoz	74	49	57
Consumer Health	– 1 842	– 375	– 408
Corporate		180	176
Total	0	0	0

PHARMACEUTICALS

Pharmaceuticals researches, develops, manufactures, distributes, and sells patented prescription medicines in the following therapeutic areas: Cardiovascular and Metabolism; Oncology; Neuroscience and Ophthalmics; Respiratory; Integrated Hospital Care; and additional products. Pharmaceuticals is organized into global business franchises responsible for the development and marketing of various products as well as a business unit, called Novartis Oncology, responsible for the global development and marketing of oncology products. The Novartis Oncology Business Unit is not required to be disclosed separately as a segment since it shares common long-term economic perspectives, customers, research, development, production, distribution and regulatory factors with the rest of the division.

Pharmaceuticals is the largest contributor among the segments, accounting in 2011 for USD 32.5 billion, or 56%, of net sales and for USD 8.3 billion, or 71%, of operating income (excluding Corporate Income & Expense, net).

ALCON

Alcon discovers, develops, manufactures, distributes and sells eye care products. Alcon is the global leader in eye care with product offerings in Surgical, Ophthalmic Pharmaceuticals and Vision Care. In Surgical, Alcon develops, manufactures, distributes and sells ophthalmic surgical equipment, instruments, disposable products and intraocular lenses. In Ophthalmic Pharmaceuticals, Alcon discovers, develops, manufactures, distributes and sells medicines to treat chronic and acute diseases of the eye, as well as over-the-counter medicines for the eye. In Vision Care, Alcon develops, manufactures, distributes and sells contact lenses and lens care products.

In 2011, Alcon accounted for USD 10.0 billion, or 17%, of Group net sales, and for USD 1.5 billion, or 13%, of Group operating income (excluding Corporate income and expense, net).

In addition to the restated segmentation structure, the Alcon segment is also discussed on a pro forma basis. This is necessary since the restated 2010 segmentation only includes the consolidated results of Alcon, Inc. from the date of acquisition of majority control on August 25, 2010. In order to provide a meaningful description of the results of this segment in 2011 compared to

2010, the pro forma results of Alcon, Inc. from January 1, 2010 to August 25, 2010 have been included. The pro forma results of the Alcon segment therefore have been prepared assuming that the acquisition of Alcon, Inc. had occurred as of January 1, 2010 and that the purchase price allocation had been performed as of this date. As a result, the pro forma results include the full year charge for additional amortization of the acquired intangible assets and the impact of other revaluations of assets and liabilities. Exceptional items included in the results for 2010 resulting from the change of control on August 25, 2010 such as change of control and other exceptional costs as well as the impact of revaluing the inventory and charging this to the post August 25, 2010 consolidated income statement have also been excluded. Also excluded is the impact of any divestments in 2010 and 2011 required by regulators to approve the merger.

The additional impact on the 2010 and 2011 restated Alcon segment results from incorporating the pro forma adjustments can be summarized as follows:

(USD m)	Net sales	Operating income	Core operating income
2010			
Alcon restated			
Pro forma adjustments			
Alcon pro forma			
2011			
Alcon restated	9 958	1 472	3 492
Pro forma adjustments	– 9	– 11	– 2
Alcon pro forma	9 949	1 461	3 490

SANDOZ

Sandoz is a leading global generic pharmaceuticals company that develops, manufactures, distributes and sells prescription medicines, as well as pharmaceutical and biotechnological active substances, which are not protected by valid and enforceable third-party patents. Sandoz has activities in Retail Generics, Anti-Infectives, Biopharmaceuticals and Oncology Injectables. In Retail Generics, Sandoz develops, manufactures and markets active ingredients and finished dosage forms of pharmaceuticals, as well as supplying active ingredients to third parties. In Anti-Infectives, Sandoz develops and manufactures active pharmaceutical ingredients and intermediates – mainly antibiotics – for internal use by Retail Generics and for sale to third-party customers. In Biopharmaceuticals, Sandoz develops manufactures and markets protein- or other biotechnology-based products (known as biosimilars or follow-on biologics) and sells biotech manufacturing services to other companies. In Oncology Injectables, Sandoz develops, manufactures and markets cytotoxic products for the hospital market.

In 2011, Sandoz accounted for USD 9.5 billion, or 16%, of net sales and for USD 1.4 billion, or 12% of operating income (excluding Corporate Income & Expense, net).

VACCINES AND DIAGNOSTICS

Vaccines and Diagnostics researches, develops, manufactures, distributes and sells preventive vaccines and diagnostic tools. Novartis Vaccines is a leading global developer and manufacturer of human vaccines.

Novartis Diagnostics is a blood testing and molecular diagnostics business dedicated to preventing the spread of infectious diseases through novel blood-screening tools that protect the world's blood supply.

In 2011, Vaccines and Diagnostics accounted for USD 2.0 billion, or 3%, of net sales and an operating loss of USD 249 million, or 2%, of operating income (excluding Corporate Income & Expense, net).

CONSUMER HEALTH

Consumer Health now consists of two divisions: OTC (over-the-counter medicines) and Animal Health. Each has its own research, development, manufacturing, distribution and selling capabilities. However, neither is material enough to the Group to be separately disclosed as a segment. OTC offers readily available consumer medicine and Animal Health provides veterinary products for farm and companion animals.

In 2011, Consumer Health accounted for USD 4.6 billion, or 8%, of net sales and for USD 727 million, or 6% of operating income (excluding Corporate Income & Expense, net).

CORPORATE

Income and expenses relating to Corporate include the costs of our headquarters and corporate coordination functions in major countries. In addition, Corporate includes certain items of income and expense that are not attributable to specific divisions, including global IT infrastructure remediation.

EFFECTS OF CURRENCY FLUCTUATIONS

We transact our business in many currencies other than the US dollar, our reporting currency.

The following provides an overview of net sales and expenses for 2011 and 2010 for currencies most important to the Group:

Currency		2011 %
US dollar (USD)	Net sales	36
	Operating expenses	38
Euro (EUR)	Net sales	27
	Operating expenses	25
Swiss franc (CHF)	Net sales	2
	Operating expenses	14
Japanese yen (JPY)	Net sales	9
	Operating expenses	4
Other currencies	Net sales	26
	Operating expenses	19

We prepare our consolidated financial statements in US dollars. As a result, fluctuations in the exchange rates between the US dollar and other currencies can have a significant effect on both the Group's results of operations as well as on the reported value of our assets, liabilities, revenue and expenses as measured in US dollars. This in turn may significantly affect reported earnings (both positively and negatively) and the comparability of period-to-period results of operations.

For purposes of our consolidated balance sheets, we translate assets and liabilities denominated in other currencies into US dollars at the prevailing market exchange rates as of the relevant balance sheet date. As a result, even if the amounts or values of these items remain unchanged in the respective local currency, changes in exchange rates have an impact on the amounts or values of these items in our consolidated financial statements. For purposes of the Group's consolidated income and cash flow statements, revenue, expense and cash flow items in local currencies are translated into US dollars at average exchange rates prevailing during the relevant period.

We seek to manage currency exposure by engaging in hedging transactions where management deems appropriate. For 2011, we entered into various contracts that change in value with movements in foreign exchange rates in order to preserve the value of assets, commitments and expected transactions. We also use forward contracts and foreign currency options to hedge expected net revenues in foreign currencies. For more information on how these transactions affect our consolidated financial statements and on how foreign exchange rate exposure is managed, see notes 1, 5 and 16 to the Group's consolidated financial statements.

The average value of the US dollar in 2011 decreased against the EUR, CHF and JPY. The following table sets forth the foreign exchange rates of the US dollar against these currencies, used for foreign currency translation when preparing the Group's consolidated financial statements:

USD per unit	2011	Change in %	2011	Change in %
EUR	1.392	5%	1.294	–2%
CHF	1.130	18%	1.064	0%
JPY (100)	1.255	10%	1.289	5%

The following table provides a summary of the currency impact on key Group figures due to their conversion into USD, the Group's reporting currency, of the financial data from entities reporting in non-US dollars. Constant currency (cc) calculations apply the exchange rates of the prior year to the current year financial data for entities reporting in non-US dollars.

CURRENCY IMPACT ON KEY FIGURES

	Change in constant currencies % 2011	Change in USD % 2011	Percentage point currency impact 2011
Net sales	12	16	4
Operating income	1	–5	–6
Net income	–2	–7	–5
Core operating income	16	14	–2
Core net income	15	12	–3

For additional information on the effects of currency fluctuations, see note 16 to the Group's consolidated financial statements.

RESULTS OF OPERATIONS

KEY FIGURES

	Year ended Dec 31, 2011 USD millions	Change in USD %	Change in constant currencies %
Net sales	58 566	16	12
Other revenues	809	–14	–15
Cost of Goods Sold	–18 983	31	25
Gross profit	40 392	9	7
Marketing & Sales	–15 079	13	9
Research & Development	–9 583	6	–2
General & Administration	–2 970	20	12
Other income	1 354	10	–4
Other expense	–3 116	63	48
Operating income	10 998	–5	1
Income from associated companies	528	–34	–34
Interest expense	–751	9	5
Other financial income and expense	–2	–103	–140
Income before taxes	10 773	–8	–2
Taxes	–1 528	–12	–6
Group net income	9 245	–7	–2
Attributable to:			
Shareholders of Novartis AG	*9 113*	*–7*	*–1*
Non-controlling interests	*132*	*–25*	*–25*
Basic earnings per share	3.83	–11	–5

CORE KEY FIGURES

	Year ended Dec 31, 2011 USD millions	Change in USD %	Change in constant currencies %
Core gross profit	43 839	14	11
Marketing & Sales	–15 077	13	9
Research & Development	–9 239	14	7
General & Administration	–2 957	19	11
Other income	443	–9	–43
Other expense	–1 100	–2	–19
Core operating income	15 909	14	16
Core net income	13 490	12	15
Core basic earnings per share	5.57	8	11

The Group's core results – including core operating income, core net income and core earnings per share – exclude the amortization of intangible assets, impairment charges, expenses relating to the integration of acquisitions as well as other items that are, or are expected to accumulate within the year to be, over a USD 25 million threshold that management deems exceptional.

A detailed summary of the reconciliation of reported to core results is provided starting on page 179.

OVERVIEW – RESULTS OF OPERATIONS

Net sales rose 16% (+12% cc) to USD 58.6 billion in 2011, with a positive currency impact of 4% arising from the weakness of the US dollar against most major currencies during much of 2011. Recently launched products sales grew 38% (in USD, excluding the A(H1N1) pandemic flu vaccine) over 2010 to USD 14.4 billion. These products contributed 25% of Group net sales, up from 19% in 2010.

Operating income was down 5% (+1% cc) to USD 11.0 billion. The weakness of the US dollar, combined with the strong Swiss franc, resulted in a negative currency impact of 6 percentage points. Cost of Goods Sold rose by 31% (25% cc) to USD 19.0 billion in 2011, increasing by 3.8 percentage points to 32.4% of net sales. This led to a reduction in the gross margin by 4.2% to 69.0%. Marketing & Sales rose 13% (9% cc) to USD 15.1 billion, improving 0.6 percentage points to 25.7% of net sales, as productivity improvements and changes in the portfolio mix were partly offset by investments in new launch products. Research & Development expenses increased by 6% (–2% cc) in 2011 to USD 9.6 billion. This included USD 341 million in impairments of intangible assets. General & Administration expenses increased 20% (12% cc) to USD 3.0 billion. Other income was up 10% (–4% cc) to USD 1.4 billion and largely consists of gains from product disposals, legal settlements and certain items of net periodic pension cost. Other expense was up 63% (48% cc) to USD 3.1 billion and includes impairment of financial assets as well as property plant and equipment, litigation settlement costs, restructuring and related charges and acquisition related integration expenses.

Core operating income, which excludes exceptional items and amortization of intangible assets, was up 14% (16% cc) to USD 15.9 billion. Core operating income margin in constant currencies increased by 1.1 percentage points. However, this improvement was more than offset by a negative currency impact of 1.6 percentage points, resulting in a net decrease in core operating income margin of 0.5 percentage points to 27.2% of net sales. Total net exceptional income and expense adjusted in core results in the various line items in 2011 amounted to USD 1.9 billion expense compared to USD 1.3 billion in the prior year. It comprised charges of USD 2.9 billion (2010: USD 2.1 billion) partly offset by exceptional income of USD 1.0 billion (2010: USD 732 million). Exceptional charges included: *Tekturna/Rasilez* (USD 903 million); USD 348 million related to the discontinuation of the PRT128 (elinogrel), SMC021 (oral calcitonin), AGO178 (agomelatine), and PTK796 (omadacy-

cline) development programs; a charge of USD 115 million related to the temporary suspension of production at one of our US Consumer Health sites; other intangible asset impairment charges of USD 71 million principally relating to development projects; financial asset impairment charges of USD 192 million; integration charges of USD 250 million (mainly for Alcon); and restructuring and related costs of USD 492 million. Exceptional income includes divestment proceeds (USD 480 million) and a USD 106 million reduction of a contingent consideration obligation in Sandoz. In 2011, amortization of intangible assets amounted to USD 3.0 billion compared to USD 1.1 billion in 2010 as a result of a full year of incorporating Alcon.

Net income decreased 7% (–2% cc) to USD 9.2 billion, more than the decline in operating income as a result of lower associated company income, higher financing costs following the Alcon acquisition, partly offset by a lower tax rate (14.2% compared to 14.8%). EPS declined 11% (–5% cc), more than the decline in net income, mainly as a result of the increase in issued shares following the Alcon merger, partially offset by a lower impact from non-controlling minority interests.

Core net income grew 12% (+15% cc) to USD 13.5 billion broadly in line with core operating income. Core EPS was up by 8% (+11% cc): a lower rate than net income as a result of a higher number of outstanding shares in 2011.

The average number of shares outstanding in 2011 rose 4% to 2 382 million from 2 286 million in the year ago, while a total of 2 407 million shares were outstanding at December 31, 2011.

Free cash flow reached USD 12.5 billion (2010: USD 12.3 billion), an increase of 1% over the previous year. Free cash flow in 2010 included substantial cash flows from sales of A(H1N1) amounting to USD 1.8 billion.

NET SALES

	Year ended Dec 31, 2011 USD millions	[1] Change in USD %	Change in constant currencies %
Pharmaceuticals	32 508	7	4
Alcon	9 958	124	118
Sandoz	9 473	10	7
Vaccines and Diagnostics	1 996	– 32	– 34
Consumer Health	4 631	6	3
Net sales	58 566	16	12

[1] Restated to reflect new segment allocation introduced during 2011 as explained in detail on page 159

Pharmaceuticals net sales grew 7% (+4% cc) to USD 32.5 billion, and Alcon net sales of USD 10.0 billion rose 10% (+7% cc) on a pro forma basis. Sandoz net sales also grew 10% (+7% cc) to USD 9.5 billion. Vaccines and Diagnostics net sales were down 32% (–34% cc) to USD 2.0 billion, mainly due to USD 1.3 billion of A(H1N1) pandemic flu vaccine sales in 2010. Net sales of the two Consumer Health businesses together grew 6% (+3% cc) to USD 4.6 billion.

PHARMACEUTICALS

Net sales expanded 7% (+4% cc) to USD 32.5 billion in 2011 driven by 9 percentage points of increased volume, partly offset by a negative pricing impact of 1 percentage point and the combined impact of generic entries and product divestments of an additional 4 percentage points. Recently launched products contributed USD 9.2 billion of net sales, growing 35% in constant currencies over the previous year. These products now represent 28% of division sales compared to 22% in 2010.

Europe remained the largest region (USD 11.6 billion, +2% cc) for Pharmaceuticals, particularly benefiting from recently launched products, which generated 35% of net sales, more than offsetting health care cost-containment measures and generic erosion. The US (USD 10.0 billion, 0% cc) contributed 31% of net sales for the division. Japan's performance (USD 3.9 billion, +7% cc) improved versus the prior year due to new launches. Latin America and Canada (USD 3.0 billion, +10% cc) achieved strong growth rates. The top six emerging markets (USD 3.2 billion, +7% cc) were led by double-digit growth from China and India.

TOP 20 PHARMACEUTICALS DIVISION PRODUCT NET SALES – 2011

Brands		United States USD millions	% change in constant currencies	Rest of world USD millions	% change in constant currencies	Total USD millions	% change in USD	% change in constant currencies
Diovan/Co-Diovan	Hypertension	2 333	–7	3 332	–11	5 665	–6	–9
Gleevec/Glivec	Chronic myeloid leukemia	1 459	14	3 200	2	4 659	9	5
Lucentis	Age-related macular degeneration			2 050	26	2 050	34	26
Zometa	Cancer complications	642	–11	845	0	1 487	–2	–5
Sandostatin	Acromegaly	574	12	869	7	1 443	12	9
Exforge	Hypertension	325	14	884	36	1 209	34	30
Exelon/Exelon Patch	Alzheimer's disease	375	–1	692	7	1 067	6	4
Femara	Breast cancer	219	–66	692	–11	911	–34	–37
Neoral/Sandimmun	Transplantation	71	–13	832	–1	903	4	–2
Exjade	Iron chelator	259	–2	591	13	850	12	8
Top ten products total		**6 257**	**–7**	**13 987**	**3**	**20 244**	**3**	**0**
Voltaren **(excl. OTC)**	Inflammation/pain	4	0	790	1	794	0	2
Tasigna	Chronic myeloid leukemia	255	90	461	66	716	79	74
Galvus	Diabetes			677	66	677	73	66
Comtan/Stalevo	Parkinson's disease	214	–7	400	3	614	2	–1
Reclast/Aclasta	Osteoporosis	386	–2	227	18	613	6	5
Tekturna/Rasilez	Hypertension	216	4	341	41	557	27	24
Ritalin/Focalin	Attention Deficit/Hyperactive Disorder	398	17	152	14	550	19	17
Myfortic	Transplantation	200	23	318	11	518	17	15
Gilenya	Relapsing Multiple Sclerosis	383	nm	111	nm	494	nm	nm
Xolair	Asthma	15	–38	463	35	478	30	29
Top 20 products total		**8 328**	**2**	**17 927**	**8**	**26 255**	**9**	**6**
Rest of portfolio		1 645	–9	4 608	–1	6 253	0	–4
Total Division sales		**9 973**	**0**	**22 535**	**6**	**32 508**	**7**	**4**

nm - not meaningful

PHARMACEUTICALS DIVISION PRODUCT HIGHLIGHTS – SELECTED LEADING PRODUCTS

Net sales growth data below refer to 2011 worldwide performance. Growth rates are not provided for some recently launched products since they are not meaningful.

Diovan **Group** (–6% to USD 5.7 billion, –9% cc) worldwide sales declined due to loss of exclusivity in the EU. *Diovan* Group remains the top-selling anti-hypertensive medication worldwide, with 13.27% of the global hypertension market.

Exforge **Group** (+34% to USD 1.2 billion, +30% cc), showed strong worldwide growth fueled by continued prescription demand in the EU, US and other key regions, as well as ongoing *Exforge HCT* launches in Europe, Asia and Latin America. *Exforge*, a single-pill combination of *Diovan* and the calcium channel blocker amlodipine, has delivered excellent growth globally and is now available in over 80 countries. *Exforge HCT*, *Exforge* with a diuretic (hydrochlorothiazide) in a single pill, is now available for patients in over 40 countries with additional launches expected in 2012.

Tekturna/Rasilez (+27% to USD 557 million, +24% cc), the first in a class of medicines known as direct renin inhibitors to treat high blood pressure, has been growing consistently since its launch in 2007. However, in late December, following the seventh interim review of data from the ALTITUDE study with *Tekturna/Rasilez*, Novartis announced that the trial was halted on the recommendation of the independent Data Monitoring Committee (DMC) overseeing the study. The DMC concluded that patients were unlikely to benefit from treatment on top of standard anti-hypertensive medicines, and identified higher adverse events in patients receiving Tek*turna/Rasilez* in addition to standard of care as part of the trial. Novartis has written to healthcare professionals worldwide recommending that hypertensive patients with diabetes should not be treated with *Tekturna/Rasilez*, or combination products containing aliskiren (the active ingredient in *Tekturna/Rasilez*), if they are also receiving an angiotensin-converting enzyme (ACE) inhibitor or angiotensin receptor blocker (ARB). As an additional precautionary measure, Novartis has ceased promotion of *Tekturna/Rasilez*-based products for use in combination with an ACE inhibitor or ARB.

In 2011, single-pill combinations *Rasilamlo*, a dual combination of aliskiren and amlodipine, and *Rasitrio*, a triple combination of aliskiren, amlodipine and hydrochlorothiazide, were approved in the EU. These single-pill combinations were also launched in the US in 2011 under the brand names *Tekamlo* and *Amturnide*, respectively.

Galvus/Eucreas (+73% to USD 677 million, +66% cc), which includes oral treatments with vildagliptin for type 2 diabetes, has shown strong growth in Japan and many European, Latin American and Asian Pacific markets since launch in 2007. The single-pill combination *Eucreas/GalvusMet* (vildagliptin and metformin) accounted for the majority of sales, with the expanded use of *Galvus* in elderly patients over 75 years old in the EU also fueling growth in 2011. Additional EU approvals for use in moderate or severe renally impaired type 2 diabetes patients are expected to drive growth in 2012. Vildagliptin is now approved in more than 90 countries with an additional launch expected in China in 2012.

Gleevec/Glivec (+9% to USD 4.7 billion, +5% cc), a targeted therapy for some forms of chronic myeloid leukemia (CML) and gastrointestinal stromal tumors (GIST), maintained solid growth based on its leadership position in treating these cancers. New clinical data showing significant survival benefits for adult patients with resected KIT+ GIST who received adjuvant (post-surgery) treatment with *Gleevec/Glivec* (imatinib) for three years compared to one year following surgery served as the basis for worldwide regulatory filings to update the label. *Gleevec/Glivec* was approved in 2008 for use in certain adjuvant (post-surgery) KIT+ GIST patients and is now approved in more than 60 countries for this indication.

Tasigna (+79% to USD 716 million, +74% cc), has shown rapid growth as a next-generation targeted therapy for newly diagnosed Ph+ CML patients following approvals in more than 50 markets globally including the US, EU, Japan and Switzerland, with additional submissions pending worldwide. *Tasigna* market share continues to rise in Ph+ CML in the second-line indication with approvals in over 95 countries.

Zometa (–2% to USD 1.5 billion, –5% cc) is an intravenous bisphosphonate therapy for patients with certain types of cancer that has spread to the bones. Zoledronic acid, the active ingredient in *Zometa* (4 mg), is also available under the trade names *Reclast/Aclasta* (5 mg) for use in non-oncology indications with different dosing. *Zometa* is facing new competition from denosumab, a product of Amgen.

Femara (–34% to USD 911 million, –37% cc), a treatment for early stage and advanced breast cancer in postmenopausal women, experienced a decline in sales due to multiple generic entries in the US, Europe and other key markets.

Sandostatin (+12% to USD 1.4 billion, +9% cc) benefited from the increasing use of *Sandostatin LAR* in treating symptoms of patients with neuroendocrine tumors as well as approvals in 25 countries for the delay of tumor progression in patients with midgut carcinoid tumors. It is currently under review in more than 20 additional countries for this indication.

Exjade (+12% to USD 850 million, +8% cc) continued to expand with strong growth based on new patients and expanded access led by Asia and Europe. *Exjade* is currently approved in more than 100 countries as the only once-daily oral therapy for transfusional iron overload. Filings for a potential new indication in the treatment of non-transfusion-dependent thalassemia were submitted in the US and EU.

Afinitor/Votubia (+82% to USD 443 million, +77% cc) is an oral inhibitor of the mTOR pathway used across multiple diseases. Afin*itor* continues to achieve strong growth in key markets as the only approved treatment for patients with advanced renal cell carcinoma following VEGF-targeted therapy. *Afinitor* expanded its indications with approvals in the US, EU and Japan for the treatment of advanced pancreatic neuroendocrine tumors. Everolimus, the active ingredient in *Afinitor*, is also approved in the US as *Afinitor* and in the EU as *Votubia* for the treatment of subependymal giant cell astryocytomas associated with tuberous sclerosis complex (TSC). A Phase III study of everolimus in patients with non-cancerous kidney tumors, or angiomyolipomas, associated with TSC formed the basis of regulatory filings currently underway for this potential indication. In addition, results of another Phase III study, which showed *Afinitor* plus exemestane met the primary endpoint of progression-free survival versus exemestane alone in postmenopausal women with ER+HER2- advanced breast cancer, are supporting worldwide regulatory filings for this potential indication. Everolimus is also available under the trade names *Zortress/Certican* for use in other non-oncology indications and is exclusively licensed to Abbott and sublicensed to Boston Scientific for use in drug-eluting stents.

Lucentis (+34% to USD 2.0 billion, +26% cc) is a biotechnology eye therapy now approved in more than 100 countries for the treatment of wet age-related macular degeneration, and in more than 50 countries for the treatment of visual impairment due to diabetic macular edema. *Lucentis* was approved in June 2011 in Europe for visual impairment due to macular edema secondary to branch- and central-retinal vein occlusion, and is now approved for this indication in more than 50 countries, including China. Genentech/Roche holds the US rights to this medicine.

***Exelon/Exelon* Patch** (+6% to USD 1.1 billion, +4% cc) is a therapy for mild to moderate forms of Alzheimer's disease dementia as well as dementia linked with Parkinson's disease. The majority of sales are for *Exelon* Patch, the novel skin patch launched in 2007 which is now available in more than 80 countries worldwide for Alzheimer's disease dementia, including more than 20 countries where it is also approved for dementia associated with Parkinson's disease.

Extavia (+24% to USD 154 million, +19% cc), available in the US and more than 35 other countries for relapsing forms of multiple sclerosis (MS), marked the entry of Novartis into the field of MS. *Extavia* is the Novartis-patented version of Betaferon®/Betaseron®.

Gilenya (USD 494 million) is approved in more than 55 countries and showed continued rapid growth as a once-daily, oral disease-modifying treatment for relapsing remitting and/or relapsing forms of MS in adult patients. *Gilenya* was approved in the EU in March 2011 as a disease modifying therapy in patients with highly active relapsing-remitting multiple sclerosis (RRMS) despite treatment with beta interferon, or in patients with rapidly evolving severe RRMS. Novartis also received approval for *Gilenya* in September 2011 in Japan for the prevention of relapse and delay of progression of physical disability in adults with MS. It is licensed from Mitsubishi Tanabe Pharma Corporation.

Xolair (+30% to USD 478 million, +29% cc, ex-US), a biotechnology drug approved for severe persistent allergic asthma in Europe and moderate to severe persistent allergic asthma in the US, gained blockbuster status when annual global sales (including US sales recorded by Genentech/Roche) reached USD 1 billion in November 2011. *Xolair* is now approved in 90 countries and has shown strong growth during 2011 in Europe, major Latin American markets and Japan. A Phase III trial is progressing to support registration in China. Launches are continuing across Europe for *Xolair* Liquid, a new formulation in pre-filled syringes that enables easier administration than the original lyophilized formulation. Phase III studies are also being conducted in an additional potential indication, chronic idiopathic urticaria. Novartis co-promotes *Xolair* with Genentech/Roche in the US and shares a portion of operating income, but does not record any US sales. Novartis has the sole rights to market *Xolair* outside the US.

Onbrez Breezhaler/Arcapta Neohaler (USD 103 million) has shown strong sales growth since its approval in the EU in November 2009 as a once-daily long-acting $beta_2$-agonist (LABA) for the maintenance bronchodilator treatment of airflow obstruction in adult patients with chronic obstructive pulmonary disease (COPD).

OPHTHALMIC PHARMACEUTICALS

Global net sales of Ophthalmic Pharmaceuticals products increased 12% (+10% cc) to USD 3.9 billion in 2011. Glaucoma product sales rose 13% (+10% cc), with growth driven by non-US combination products *DuoTrav* and *Azarga*, with a combined growth of 41% (+34% cc). Infection/inflammation product sales advanced 15% (+14% cc) led by strong growth of *Nevanac* ophthalmic suspension, as well as solid performance of *Durezol* ophthalmic suspension. Allergy, otic, and nasal products showed solid growth, led by the *Patanol/Pataday* franchise. Dry eye products *Systane* and *Systane* Balance were the key contributors to growth in that product segment.

VISION CARE

Global net sales of Vision Care products rose 5% (+1% cc) in 2011 to USD 2.4 billion. Contact lens growth was driven by the continued strong performance of *Air Optix*, which leads the marketplace in the multifocal segment and achieved 18% (cc) growth over the previous year, and by strong *Dailies* growth in the US. Sales of contact lenses were impacted by the discontinuation of the Specialty contact lens business as well as slower market growth in European countries. Contact lens solutions sales were led by strong growth of the *Clear Care* hydrogen peroxide solution, offset by weakness in the category for multi-purpose product sales.

SANDOZ

Sandoz achieved strong sales growth in 2011 (+10% to USD 9.5 billion, +7% cc) versus prior year driven by significant growth in US retail generics and biosimilars (+22% cc), with sales of over USD 1 billion for enoxaparin. Strong performances in Canada (+13% cc), Western Europe (+13% cc), Latin America (+12% cc), Asia (+12% cc) and Central and Eastern Europe (+6% cc) also contributed to growth in 2011. Germany retail generics and biosimilars declined (–13% cc) in a market that is estimated to have contracted 17% in net terms due to the impact of statutory health insurance tenders and new lower reference prices. Biosimilars grew 37% in constant currencies to USD 261 million globally. Sales volume expanded 14 percentage points due to new product launches, and Falcon (transferred from Alcon) contributed 2 additional percentage points of growth, more than compensating price erosion of 9 percentage points.

VACCINES AND DIAGNOSTICS

Net sales declined 32% to USD 2.0 billion in 2011 (–34% cc) compared to USD 2.9 billion in 2010. The primary driver of the net sales variance against the prior year was USD 1.3 billion of A(H1N1) pandemic flu vaccine sales in 2010 not repeated in 2011.

Excluding the impact of A(H1N1) pandemic flu vaccines sales in 2010, net sales growth was 22% in constant currencies, driven by growth across all strategic franchises, with a particularly strong contribution from our meningococcal disease franchise.

The growth of our meningococcal disease franchise was underpinned by *Menveo*, which continues to gain market share both in the US and worldwide, with net sales of USD 142 million in 2011.

CONSUMER HEALTH

Consumer Health (comprising OTC and Animal Health) delivered combined 2011 net sales of USD 4.6 billion producing growth of 6% (+3% cc).

OTC delivered low-single-digit growth driven by emerging markets and priority brands. In nine out of the top ten countries for OTC, volume growth outpaced the market. Cough and cold brands, including *Theraflu*, grew strongly behind sustained investment and a stronger season in several markets compared to 2010. *Voltaren* continued to grow through the use of innovative commercial models and a focus on marketing fundamentals, while *Prevacid24HR* benefitted from normalized stock movements compared to 2010. In the US, *Excedrin* sales declined in the fourth quarter due to the temporary suspension of operations and voluntary product recall at OTC's Lincoln, Nebraska, USA site. Expired distribution contracts and divested brands also negatively impacted net sales growth versus the prior year.

Animal Health contributed mid-single-digit net sales growth over the previous year, driven by Germany, Japan, Australia and emerging markets. *CliK* and *Vetrazin* retained their leadership positions in the sheep market in Australia and the UK. *Milbemax* delivered double-digit growth as the number one cat and dog dewormer in Europe, while *Onsior* gained market share across key European markets and Japan. In the swine business, *Denagard* continued to drive strong double-digit growth led by the US. Total US sales were flat despite the negative impact of a competitor entry in the heartworm and flea categories.

OPERATING INCOME BY SEGMENTS

	Year ended Dec 31, 2011 USD millions	% of net sales	[1]	Change in USD %	Change in constant currencies %
Pharmaceuticals	8 296	25.5		– 2	4
Alcon	1 472	14.8		85	67
Sandoz	1 422	15.0		8	10
Vaccines and Diagnostics	– 249	– 12.5		– 141	– 131
Consumer Health	727	15.7		– 7	4
Corporate income & expenses, net	– 670				
Operating income	10 998	18.8		– 5	1

[1] Restated to reflect new segment allocation introduced during 2011 as explained in detail on page 159

CORE OPERATING INCOME BY SEGMENTS

	Year ended Dec 31, 2011 USD millions	% of net sales	[1] Change in USD %	Change in constant currencies %
Pharmaceuticals	10 040	30.9	5	8
Alcon	3 492	35.1	159	146
Sandoz	1 921	20.3	10	11
Vaccines and Diagnostics	135	6.8	– 87	– 85
Consumer Health	873	18.9	3	12
Corporate income & expenses, net	– 552			
Core operating income	15 909	27.2	14	16

[1] Restated to reflect new segment allocation introduced during 2011 as explained in detail on page 159

PHARMACEUTICALS

Operating income decreased 2% (+4% cc) in 2011 to USD 8.3 billion. Exceptional items including amortization amounted to a net USD 1.7 billion expense compared to USD 1.1 billion expense in 2010. Exceptional items include *Tekturna/Rasilez* charges of USD 903 million, restructuring charges of USD 420 million and other intangible asset impairments of USD 302 million (mainly AGO178, PTK796, PRT128 and SMC021). These were partly offset by higher prior-year impairment charges, and divestment income from *Elidel*® (USD 324 million) and from ophthalmic pharmaceutical products related to the Alcon acquisition (USD 81 million).

Core operating income in 2011 grew 5% (+8% cc) to USD 10.0 billion. In constant currencies, core operating income margin increased by 1.4 percentage points due to continuing productivity efforts. However, this improvement was more than offset by a negative currency impact of 2.1 percentage points, resulting in a net decrease in core operating income margin of 0.7 percentage points to 30.9% of net sales. The underlying gross margin decreased by 0.6 percentage points (cc) mainly driven by increased royalties. Functional costs – which include General & Administration, Marketing & Sales and R&D expenses – improved by 2.0 percentage points, driven by productivity gains in Marketing & Sales and R&D despite significant investments in new product launches. Other Income & Expense, net, remained flat in constant currencies.

ALCON

In 2011, Alcon operating income increased 85% to USD 1.5 billion on a restated basis. Since however the 2010 base only includes Alcon, Inc. from August 25, 2010, as indicated above, a comparison on a 2010 pro forma basis is more meaningful.

Operating income in 2011 of USD 1.5 billion rose 24% (+14% cc) on a pro forma basis. Operating income was impacted by the inclusion of exceptional income from a litigation settlement (USD 183 million), amortization of intangible assets (USD 1.9 billion), integration costs (USD 221 million), and the impact of manufacturing optimization (USD 57 million).

Core operating income in 2011 of USD 3.5 billion increased by 13% (+9% cc) on a pro forma basis. Core operating income margin in constant currencies increased by 0.7 percentage points on a pro forma basis. In addition, there was a positive currency impact of 0.1 percentage points, resulting in a net increase in core operating income margin of 0.8 percentage points to 35.1% of net sales.

SANDOZ

Operating income grew 8% (+10% cc) over the prior year to USD 1.4 billion. The operating income margin improved by 0.5 percentage points in constant currencies, more than offset by a negative currency impact of 0.9 percentage points, resulting in a net decrease of 0.4 percentage points to 15.0% of net sales. The constant currency margin improvement was the result of productivity improvements, the addition of the Falcon business and income from reduction of a contingent consideration obligation, partly offset by charges and provisions for legal cases in the US (USD 204 million) as well as price erosion.

In 2011, core operating income rose 10% (+11% cc) to USD 1.9 billion, as declining prices were more than offset by additional sales volume, new product launches and productivity improvements in all areas. Core operating income margin in constant currencies increased by 0.8 percentage points to 21.2% of net sales. Currency had a negative impact, resulting in a 20.3% core operating income margin.

VACCINES AND DIAGNOSTICS

Operating loss was USD 249 million for 2011 compared to an operating income of USD 612 million in 2010, due in large part to the operating income associated with A(H1N1) pandemic flu vaccine sales from the prior year not repeated in 2011.

Excluding the impact of A(H1N1), profitability improved, despite continued investment in our pipeline and meningococcal disease franchise, driven by solid underlying sales growth. 2011 included impairments of USD 143 million related to financial and intangible assets compared to USD 98 million in 2010; 2010 also included charges related to a legal settlement of USD 45 million and restructuring charges of USD 52 million.

Core operating income for the year was USD 135 million compared to USD 1.1 billion for 2010. Excluding the impact of A(H1N1), core operating income also improved over 2010.

CONSUMER HEALTH

Operating income for 2011 decreased 7% to USD 727 million (but increased 4% cc), with operating income margin in constant currencies increasing by 0.2 percentage points, more than offset by a negative currency impact of 2.3 percentage points, resulting in an operating income margin of 15.7% of net sales.

Core operating income in 2011 increased by 3% (+12% cc) to USD 873 million. Core operating income excludes the USD 115 mil-

lion exceptional charge related to the product recall. Core operating income margin in constant currencies increased by 1.8 percentage points. This result demonstrates strong operating leverage with core operating income growing significantly ahead of net sales. USD 73 million of the product recall exceptional charge relates to sales returns. As no corresponding adjustment was made at the net sales level, it had a beneficial impact of 0.4 percentage points on the core operating income margin. Currency negatively impacted core operating income margin by 2.3 percentage points, resulting in a net core operating income margin decrease of 0.5 percentage points to 18.9% of net sales.

Gross margin improved slightly by 0.1 percentage points (cc) driven by productivity gains that were partially offset by product mix. Marketing & Sales expenses decreased by 0.7 percentage points (cc) versus prior year driven by efficiency improvements in OTC partially offset by increased investment in the Animal Health business. R&D expenses decreased by 0.1 percentage points (cc) from productivity measures that more then offset continued investment in innovation. General & Administrative expenses decreased by 0.2 percentage points (cc) due to strong cost control. Other Income and Expense, net, improved by 0.3 percentage points (cc) largely driven by income from smaller product divestments.

CORPORATE INCOME & EXPENSE, NET

Corporate income & expense, net, includes the costs of Group headquarters. These net expenses of USD 670 million in 2011 were 48% higher than in 2010 primarily due to an exceptional pension curtailment gain of USD 265 million in the prior year.

NON-OPERATING INCOME AND EXPENSE

	Year ended Dec 31, 2011 USD millions	Change in USD %	Change in constant currencies %
Operating income	10 998	– 5	1
Income from associated companies	528	– 34	– 34
Interest expense	– 751	9	5
Other financial income and expense	– 2	– 103	– 140
Income before taxes	10 773	– 8	– 2
Taxes	– 1 528	– 12	– 6
Group net income	9 245	– 7	– 2
Attributable to:			
Shareholders of Novartis AG	*9 113*	*– 7*	*– 1*
Non-controlling interests	*132*	*– 25*	*– 25*
Basic EPS (USD)	3.83	– 11	– 5

CORE NON-OPERATING INCOME AND EXPENSE

	Year ended Dec 31, 2011 USD millions	Change in USD %	Change in constant currencies %
Core operating income	15 909	14	16
Income from associated companies	779	– 25	– 28
Interest expense	– 751	9	5
Other financial income and expense	– 2	– 103	– 140
Core income before taxes	15 935	11	13
Taxes	– 2 445	2	5
Core net income	13 490	12	15
Attributable to:			
Shareholders of Novartis AG	*13 273*	*13*	*16*
Non-controlling interests	*217*	*– 17*	*– 17*
Core basic EPS (USD)	5.57	8	11

INCOME FROM ASSOCIATED COMPANIES

Associated companies are accounted for using the equity method generally when Novartis holds between 20% and 50% of the voting shares of these companies, or where Novartis has otherwise significant influence over them. Income from associated companies is mainly derived from the Group's investments in Roche Holding AG and, prior to August 25, 2010, Alcon.

The income from associated companies fell from USD 804 million in 2010 to USD 528 million in 2011, as since August 25, 2010 Alcon, Inc. is fully consolidated and no longer accounted for as an associated company.

The following is a summary of the individual components included in the income from associated companies:

	2011 USD millions
Share of estimated Roche reported net income	702
Restructuring impact (2011 includes USD 41 million from 2010; 2010 includes USD 43 million from 2009)	– 41
Amortization of intangible assets	– 162
Net income effect from Roche	499
Share of Alcon net income	
Catch-up for actual Alcon previous year net income	
Revaluation of initial 25% interest to fair value	
Recycling of losses accumulated in comprehensive income from July 7, 2008 to August 25, 2010	
Amortization of intangible assets	
Net income effect from Alcon (in 2010 up to August 25, 2010)	
Net income from other associated companies	29
Income from associated companies	528

The Group's 33.3% interest in Roche's voting shares, which represents a 6.3% interest in Roche's total equity, generated income of USD 499 million in 2011, up from USD 380 million in 2010. The 2011 contribution reflects an estimated USD 702 million share of Roche's net income in 2011. This contribution, however, was reduced by USD 162 million for the amortization of intangible assets arising from the allocation of the purchase price paid by Novartis for this investment to Roche's intangible assets and an exceptional charge of USD 41 million taken in 2011 as part of Roche's restructuring charges.

The 2010 result from Alcon includes the net income up to August 25, 2010 of USD 385 million and a positive prior-year adjustment of USD 2 million which were reduced by USD 289 million for the amortization of intangible assets.

Adjusting for the exceptional items in both years, core income from associated companies decreased 25% to USD 779 million.

A survey of analyst estimates is used to estimate the Group's share of net income in Roche. Any differences between these estimates and actual results will be adjusted in the 2012 consolidated financial statements.

INTEREST EXPENSE AND OTHER FINANCIAL INCOME/EXPENSE

In 2011, interest expense increased by 9% from USD 692 million to USD 751 million. Other financial income/expense was a net expense of USD 2 million, down from a net income of USD 64 million in the prior year mainly due to lower earnings from investments as a result of the decreased average liquidity. The currency result remained stable.

TAXES

Tax expenses in 2011 were USD 1.5 billion, a 12% (6% cc) decrease from 2010. The tax rate (taxes as a percentage of income before taxes) decreased to 14.2% in 2011 from 14.8% in 2010 mainly due to the favorable impact of the Alcon, Inc. merger and as a result the ability to undertake a related tax structure reorganization. For the same reason the core tax rate (taxes as percentage of core income before taxes) decreased to 15.3% in 2011 from 16.6% in 2010. The effective tax rate is different to the expected tax rate due to various adjustments made to the IFRS results to arrive at taxable income. For further information on the main elements contributing to the difference, see the core tables in the Appendix starting on page 179 and note 6 to the Group's consolidated financial statements.

CONDENSED CONSOLIDATED BALANCE SHEETS

	Dec 31, 2011 USD millions	Change USD millions
Assets		
Property, plant & equipment	15 627	– 213
Goodwill	29 943	251
Intangible assets other than goodwill	31 969	– 3 262
Financial and other non-current assets	15 873	3
Total non-current assets	**93 412**	**– 3 221**
Inventories	5 930	– 163
Trade receivables	10 323	450
Other current assets	2 756	171
Cash, short-term deposits and marketable securities	5 075	– 3 059
Total current assets	**24 084**	**– 2 601**
Total assets	**117 496**	**– 5 822**
Equity and liabilities		
Total equity	**65 940**	**– 3 829**
Financial debts	13 855	– 505
Other non-current liabilities	14 553	22
Total non-current liabilities	**28 408**	**– 483**
Trade payables	4 989	201
Financial debts and derivatives	6 374	– 2 253
Other current liabilities	11 785	542
Total current liabilities	**23 148**	**– 1 510**
Total liabilities	**51 556**	**– 1 993**
Total equity and liabilities	**117 496**	**– 5 822**

BALANCE SHEET

The total assets at December 31, 2011 amounted to USD 117.5 billion and were USD 5.8 billion lower than the level at the beginning of the year. Total non-current assets amounted to USD 93.4 billion compared to USD 96.6 billion at the beginning of the year, and included goodwill and intangible assets, which decreased to USD 61.9 billion from USD 64.9 billion at the beginning of the year. Current assets also decreased to USD 24.1 billion from USD 26.7 billion mainly due to a reduction in marketable securities, which fell by USD 3.1 billion as a result of the transaction with Alcon minority shareholders and a decrease in inventories of USD 0.2 billion while trade receivables increased by USD 0.5 billion.

Trade receivable balances include sales to government-supported healthcare systems. We continue to monitor sovereign debt issues and economic conditions in Greece, Italy, Spain, Portugal and other countries in Europe and evaluate accounts receivable in these countries for potential collection risks. Deteriorating credit and economic conditions and other factors in these countries have resulted in, and may continue to result in an increase in the average length of time that it takes to collect these accounts receivable and may require us to re-evaluate the collectability of these receivables in future periods.

The following table provides an overview of our aging analysis as of December 31, 2011 and 2010:

	2011 USD millions
Not overdue	8 967
Past due for not more than one month	498
Past due for more than one month but less than three months	295
Past due for more than three months but less than six months	249
Past due for more than six months but less than one year	228
Past due for more than one year	305
Provisions for doubtful trade receivables	– 219
Total trade receivables, net	**10 323**

Financial debt including derivatives decreased by USD 2.8 billion to USD 20.2 billion at December 31, 2011 despite the funding of acquisitions and share repurchases. The long-term financial debt of USD 13.8 billion comprises bonds and Euro Medium Term Notes totaling USD 12.7 billion and other long-term financial loans of USD 1.1 billion. The short-term financial debt of USD 6.4 billion comprises commercial paper of USD 2.2 billion and other short-term borrowings totaling USD 4.2 billion.

The Group's equity fell by USD 3.8 billion to USD 65.9 billion at December 31, 2011 compared to December 31, 2010. Total comprehensive income amounted to USD 7.3 billion, principally due to net income for 2011 (USD 9.2 billion), offset by net actuarial losses from defined benefit plans (USD 1.4 billion) and negative currency translation movements (USD 0.6 billion). This was more than offset by dividends (USD 5.4 billion), the net effect of the purchase of treasury shares (USD 3.5 billion) coupled with the acquisition of the remaining USD 2.9 billion non-controlling interest in Alcon, Inc. and an increase from equity-based compensation (USD 0.8 billion).

The acquisition of the remaining interests in Alcon, Inc. was achieved in two key steps. Prior to April 8, 2011, 4.8% of Alcon, Inc. was acquired which resulted in a reduction of consolidated equity by USD 2.4 billion. On April 8, 2011, the remaining outstanding non-controlling interests were acquired by an exchange of Novartis shares with a value of USD 9.2 billion plus a contingent value payment of USD 0.5 billion. Including acquisition related costs charged to equity of USD 0.1 billion, this resulted in total consolidated equity reductions of USD 12.2 billion which more than offset the amount of USD 6.5 billion non-controlling interests Novartis obtained through this transaction, leading to a net reduction in consolidated equity of USD 5.7 billion. Non-controlling interests in total reduced by USD 6.6 billion, mainly due to the transactions described above.

The Group's debt/equity ratio improved to 0.31:1 at December 31, 2011, compared to 0.33:1 at the end of 2010 mainly as the reduction in equity was more than offset by a reduction in short term financial debts.

LIQUIDITY, CASH FLOW AND CAPITAL RESOURCES

The following table sets forth certain information about the Group's cash flow and net debt.

	2011 USD millions	Change USD millions
Cash flows from operating activities	14 309	242
Cash flows used in investing activities	– 792	14 964
Cash flows used in / from financing activities	– 15 024	– 19 140
Currency translation effect on cash and cash equivalents	– 103	– 101
Net change in cash and cash equivalents	**– 1 610**	**– 4 035**
Change in marketable securities	– 1 449	10 291
Change in current and non-current financial debts	2 758	11 757
Change in net (debt) / liquidity	**– 301**	**18 013**
Net (debt) / liquidity at January 1	– 14 853	– 18 314
Net debt at December 31	**– 15 154**	**– 301**

Net debt consists of:

	2011 USD millions		Change USD millions
Current financial debts and derivative financial instruments	– 6 374	– 8 627	2 253
Non-current financial debts	– 13 855	– 14 360	505
Total financial debt	**– 20 229**		**2 758**
Less liquidity:			
Cash and cash equivalents	3 709		– 1 610
Marketable securities and derivative financial instruments	1 366		– 1 449
Total liquidity	**5 075**		**– 3 059**
Net debt at December 31	**– 15 154**		**– 301**

In 2011 the cash flow from operating activities was USD 14.3 billion, a 2% increase from USD 14.1 billion in 2010 which included USD 1.8 billion of cash collections for A (H1N1) pandemic flu vaccines.

The strong increase in operating income after adjustments for non-cash items was partially mitigated by working capital requirements to fund business expansion.

Cash outflows for investing activities were USD 0.8 billion compared to USD 15.8 billion in the prior year period. Outflows for investments in property, plant and equipment (USD 2.2 billion) and intangible and financial assets (USD 0.4 billion) as well as acquisition of businesses (USD 0.6 billion), mainly Genoptix Inc., were partly compensated by net inflows from the sale of marketable securities (USD 1.6 billion) and proceeds from the sales of various assets (USD 0.8 billion, mainly *Elidel*® marketing rights).

In 2010, outflows for investments in property, plant and equipment (USD 1.7 billion) and in intangible and financial assets (USD 0.7 billion) as well as acquisition of businesses (USD 26.7 billion), mainly Alcon, were partially funded by the sale of marketable secu-

rities, net (USD 12.6 billion) and proceeds from the sales of various assets (USD 0.7 billion).

Net cash used for financing activities was USD 15.0 billion in 2011. It was comprised of outflows of USD 5.4 billion for the dividend payment, of a net USD 3.5 billion for treasury share repurchases, USD 3.2 billion for the acquisition of the Alcon non-controlling interests and net USD 2.8 billion for the repayment of financial debts and USD 0.1 billion other financing items. In 2010 the financing activities resulted in a net cash inflow of USD 4.1 billion on account of additional debt raised for the increased Alcon investment.

Overall liquidity of USD 5.1 billion consists of USD 3.7 billion of cash and cash equivalents and of USD 1.4 billion marketable securities and derivative financial instruments. It decreased by USD 3.0 billion from the prior year level of USD 8.1 billion which included cash and cash equivalents of USD 5.3 billion and marketable securities and financial derivatives of USD 2.8 billion.

The total financial debt was USD 20.2 billion, down by USD 2.8 billion. Group net debt increased to USD 15.2 billion at the end of 2011 from USD 14.9 billion at the end of 2010. This represents a net increase of USD 0.3 billion since December 31, 2010. The peak Novartis net debt amount of USD 22.7 billion was reached at the beginning of the second quarter of 2011. This has been repaid to the extent of USD 7.5 billion by the year end. The long-term credit rating for the company continues to be double-A (Moody's Aa2; Standard & Poor's AA-; Fitch AA).

Net debt/liquidity constitutes a non-IFRS financial measure, which means that it should not be interpreted as a measure determined under IFRS. Net debt/liquidity is presented as additional information as it is a useful indicator of the Group's ability to meet financial commitments and to invest in new strategic opportunities, including strengthening its balance sheet.

We continuously track our liquidity position and asset/liability profile. This involves modeling cash flow maturity profiles based on both historical experiences and contractual expectations to project our liquidity requirements. We seek to preserve prudent liquidity and funding capabilities.

We are not aware of significant demands to change our level of liquidity needed to support normal business activity. We intend to use part of our free cash flow to reduce our financial debt. We make use of various borrowing facilities provided by several financial institutions. We also successfully issued various bonds in 2010 and 2011. In addition, we raised funds through our commercial paper program. We have no commitments from repurchase or securities lending transactions. The principal reason for the increase in average current financial debt in 2011 compared to 2010 is the increase in commercial paper during 2011, which was used for general corporate purposes of the Novartis Group, as well as for financing purposes in connection with the acquisition of the remaining Alcon, Inc. non-controlling interests in 2011.

An overview of the movements in our current financial debt and related interest rates is set forth below:

	December 31 USD millions	Average interest rate at year end % [1]	Average balance during the year USD millions	Average interest rate during the year % [1]	Maximum balance during the year USD millions [2]
2011					
Interest bearing accounts of associates	1 357	1.36	1 463	1.25	1 626
Other bank and financial debt	2 053	3.38	3 784	1.83	7 749
Commercial paper	2 156	0.55	5 597	0.21	8 673
Current portion of non-current financial debt	778	na	479	na	911
Fair value of derivative financial instruments	30	na	97	na	184
Total current financial debt	**6 374**		**11 420**		**19 143**
2010					
Interest bearing accounts of associates					
Other bank and financial debt					
Commercial paper					
Current portion of non-current financial debt					
Fair value of derivative financial instruments					
Total current financial debt					

[1] 2010 interest is calculated based on the average balances for a quarter and 2011 interest is calculated based on the average balances for a month
[2] For 2010 maximum amount at end of any quarter in each category and for 2011 maximum amount at end of any month in each category
na – not applicable or available

Interest bearing accounts of associates relate to employee deposits in CHF from the compensation of associates employed by Swiss entities (actual interest rate: 1.25%). Other bank and financial debt refer to usual lending and overdraft facilities.

The maturity schedule of our net debt is as follows:

December 31, 2011	Due or due within one month USD millions	Due later than one month but less than three months USD millions	Due later than three months but less than one year USD millions	Due later than one year but less than five years USD millions	Due after five years USD millions	Total USD millions
Current assets						
Marketable securities			36	638	562	1 236
Derivative financial instruments and accrued interest on derivative financial instruments	61	15	54			130
Cash and cash equivalents	3 709					3 709
Total current financial assets	**3 770**	**15**	**90**	**638**	**562**	**5 075**
Non-current liabilities						
Financial debts				9 874	3 981	13 855
Total non-current financial debt				**9 874**	**3 981**	**13 855**
Current liabilities						
Financial debts	4 039	1 100	1 205			6 344
Derivative financial instruments	7	7	16			30
Total current financial debt	**4 046**	**1 107**	**1 221**			**6 374**
Net debt	**– 276**	**– 1 092**	**– 1 131**	**– 9 236**	**– 3 419**	**– 15 154**

Current assets

Marketable securities

Derivative financial instruments and accrued interest on derivative financial instruments

Cash and cash equivalents

Total current assets

Non-current liabilities

Financial debts

Total non-current liabilities

Current liabilities

Financial debts

Derivative financial instruments

Total current liabilities

Net debt

The following table provides a breakdown of liquid funds and financial debt by currency:

LIQUID FUNDS AND FINANCIAL DEBT BY CURRENCY
(as of December 31)

	Liquid funds in % 2011	Financial debt in % 2011
USD	60	56
EUR	2	13
CHF	33	15
JPY		14
Other	5	2
	100	100

FREE CASH FLOW

Novartis defines free cash flow as cash flow from operating activities less purchase or sale of property, plant & equipment, intangible, non-current and financial assets. Cash effects realized in connection with the acquisition or divestment of subsidiaries, associated companies and non-controlling interests are excluded from free cash flow. The following is a summary of the Group's free cash flow:

	2011 USD millions	Change USD millions
Cash flows from operating activities	**14 309**	**242**
Purchase of property, plant & equipment	– 2 167	– 489
Purchase of intangible assets	– 220	334
Purchase of financial assets	– 139	– 15
Purchase of non-current non-financial assets	– 48	– 33
Proceeds from sales of property, plant & equipment	61	25
Proceeds from sales of intangible assets	643	98
Proceeds from sales of financial assets	59	– 7
Proceeds from sales of non-current non-financial assets	5	2
Group free cash flow	**12 503**	**157**

Free cash flow for 2011 was USD 12.5 billion, which represents an increase of 1% or USD 0.2 billion compared to the prior-year. Main contributors were Pharmaceuticals with USD 10.8 billion followed by Alcon with USD 3.5 billion while other divisions contributed in total USD 2.1 billion. Corporate had a free cash outflow of USD 3.9 billion mainly on account of interest and tax payments.

Free cash flow of USD 12.5 billion was deployed for dividend payments of USD 5.4 billion and share repurchases of USD 5.9 billion (including USD 2.4 billion repurchased indirectly via Alcon, Inc. to reduce the dilutive impact of the subsequent merger of Alcon, Inc. into Novartis AG). In total, dividends and share repurchases utilized 90% of the Group's 2011 free cash flow.

Free cash flow is presented as additional information because Novartis considers it is a useful indicator of the Group's ability to operate without relying on additional borrowing or the use of existing cash. Free cash flow is a measure of the net cash generated that is available for debt repayment and investment in strategic opportunities. The Group uses free cash flow as a performance measure when making internal comparisons of the results of divisions. Free cash flow constitutes a non-IFRS financial measure, which means that it should not be interpreted as a measure determined under IFRS. Free cash flow is not intended to be a substitute measure for cash flow from operating activities (as determined under IFRS).

CONTRACTUAL OBLIGATIONS

The following table summarizes the Group's contractual obligations and other commercial commitments as well as the effect these obligations and commitments are expected to have on the Group's liquidity and cash flow in future periods:

		Payments due by period			
	Total USD millions				
Non-current financial debt	14 633	778	4 818	5 056	3 981
Operating leases	3 036	355	445	233	2 003
Unfunded pensions and other post-retirement obligations	1 808	85	173	186	1 364
Research & Development					
– Unconditional commitments	343	105	126	81	31
– Potential milestone commitments	2 653	282	665	560	1 146
Purchase commitments					
– Property, plant & equipment	583	493	75	13	2
Total contractual cash obligations	23 056	**2 098**	**6 302**	**6 129**	**8 527**

The Group intends to fund the R&D and purchase commitments with internally generated resources.

SUMMARY OF EQUITY MOVEMENTS

	Number of shares (in millions)		Issued share capital and reserves attributable to Novartis AG shareholders	
	2011	Change	2011 USD millions	Change USD millions
Balance at beginning of year	2 289	15	63 196	5 809
Shares issued in connection with the merger with Alcon	108	108	6 009	6 009
Treasury shares exchanged in connection with the merger with Alcon	57	57	3 154	3 154
Excess of the purchase price for acquiring non-controlling interest compared to the recorded amounts and other impacts of change of ownership in consolidated entities			– 5 664	– 5 494
Share buy-backs:				
Shares acquired to be held in Group Treasury	– 21	– 21	– 1 131	– 1 113
Shares acquired to be cancelled	– 39	– 39	– 2 360	– 2 360
Other treasury shares movements	13	– 2	837	– 122
Dividends			– 5 368	– 882
Net income of the year attributable to shareholders of Novartis AG			9 113	– 681
Other comprehensive income attributable to shareholders of Novartis AG			– 1 942	– 1 672
Balance at end of year	2 407	118	65 844	2 648

A total of 165 million Novartis shares with a fair value of USD 9.2 billion were exchanged on April 8, 2011 to obtain the outstanding non-controlling interest in Alcon, Inc. These shares consisted of 108 million newly issued shares and 57 million treasury shares.

In 2011 a total of 60 million shares, net were purchased for USD 3.5 billion. Out of these, 39 million shares were acquired under the 2nd line of the SIX Swiss Exchange repurchase program with the intention to be cancelled and 21 million shares were repurchased on the 1st trading line of the SIX Swiss Exchange with the intention of being retained in Group Treasury. 13 million shares were transferred to associates as part of the equity-settled compensation or sold (2010: 15 million shares) resulting in a total net reduction of 9.2 million treasury shares (2010: 15.1 million shares).

EARNINGS BEFORE INTEREST, TAX, DEPRECIATION AND AMORTIZATION

The Group defines the non-IFRS measure of earnings before interest, tax, depreciation and amortization (EBITDA) as operating income excluding depreciation of property, plant & equipment (including any related impairment charges), amortization of intangible assets (including any related impairment charges), income from associated companies, interest expense, other financial income/expense, other expense and taxes.

	2011 USD millions	Change USD millions
Operating income	10 998	– 528
Depreciation of property, plant & equipment	1 728	365
Amortization of intangible assets	3 028	1 893
Impairments of property, plant & equipment and intangible assets	1 032	111
Group EBITDA	16 786	1 841

The following table provides an overview of EBITDA by segment:

	2011 USD millions	% of net sales
Pharmaceuticals	10 544	32.4
Alcon	3 731	37.5
Sandoz	2 134	22.5
Vaccines and Diagnostics	107	5.4
Consumer Health	852	18.4
Corporate and other	– 582	
Group EBITDA	16 786	28.7

[1] Restated to reflect new segment allocation introduced during 2011 as explained in detail on page 159

As indicated above, EBITDA is an additional non-IFRS measure. Compared to our definition of "Core" which is also a non-IFRS measure, EBITDA only adjusts for the impact of the significant non-cash items contained in operating income relating to depreciation, amortization and impairment charges but does not take into account any other exceptional items.

ENTERPRISE VALUE

Enterprise value is a non-IFRS measure representing the total amount that shareholders and debt holders have invested in Novartis, less the Group's liquidity.

	Dec 31, 2011 USD millions	Change USD millions
Market capitalization	137 511	3 780
Non-controlling interests	96	– 6 477
Financial debts	20 229	– 2 758
Liquidity	– 5 075	3 059
Enterprise value	152 761	– 2 396
Enterprise value/EBITDA	9	

NOVARTIS ECONOMIC VALUE ADDED

Novartis utilizes its own definition for measuring Novartis Economic Value Added (NVA), a non-IFRS measure, which is utilized for determining payouts under the Long-Term Performance Plan. The following table shows NVA for 2011 and 2010 utilizing the Novartis definition.

	Year ended Dec 31, 2011 USD millions	Change in USD %
Operating income	10 998	– 5
Income from associated companies	528	– 34
Operating interest	– 284	– 12
Operating tax	– 2 296	6
Capital charge	– 7 397	35
Novartis Economic Value Added	1 549	– 64

Operating interest is the internal charge on average working capital based on the short-term borrowing rates of the entity owning them.

Operating tax is the internal tax charge for each entity applying the applicable tax rate to the profit before tax of each entity unadjusted for tax-disallowed items or tax loss carryforwards.

The capital charge is the notional interest charge on the Group's average non-current assets based on an internally calculated weighted average cost of capital for the Group.

NET NOVARTIS ADDED VALUE

Net Novartis Added Value (NNAV) is a non-IFRS measure, which describes, among other items, the percentage of Group sales used either directly or individually for payments to suppliers, associates, public authorities, financial institutions or our shareholders.

A total of 46% of the 2011 revenue from net sales was used to purchase goods and services from suppliers. Of the total of USD 26.6 billion of NNAV, 56% was paid either directly or indirectly to associates, 14% was retained in the business for future expansion and 9% was paid to public authorities and financial institutions. Income attributed to non-controlling interests and dividends paid to shareholders of Novartis AG represented 21% of the NNAV.

ORIGIN OF NET NOVARTIS ADDED VALUE

	2011 USD millions	2011 % of net sales
Net sales	58 566	100
Other revenues, change in inventory and own manufactured items	763	1.3
	59 329	101.3
Services bought from third parties:		
Material costs and other operating expenses	– 26 756	– 45.7
Gross added value	32 573	55.6
Depreciation, amortization and impairments	– 5 980	– 10.2
Financial income	– 2	0.0
Net Novartis Added Value	26 591	45.4

INTERNAL CONTROL OVER FINANCIAL REPORTING

The Group's management has assessed the effectiveness of internal control over financial reporting. The Group's independent statutory auditor also issued an opinion on the effectiveness of internal control over financial reporting concluding that the Group maintained, in all material respects, effective internal control over financial reporting as of December 31, 2011.

APPENDIX

CORE RESULTS AS DEFINED BY NOVARTIS

The Group's core results – including core operating income, core net income and core earnings per share – exclude the amortization of intangible assets, impairment charges, expenses relating to the integration of acquisitions as well as other items that are, or are

2011 AND 2010[1] RECONCILIATION OF SEGMENT OPERATING INCOME TO CORE OPERATING INCOME

	Pharmaceuticals	Alcon
	2011 USD millions	2011 USD millions
Operating income	8 296	1 472
Amortization of intangible assets	423	1 928
Impairments		
Intangible assets	552	20
Property, plant & equipment - manufacturing sites[3]	12	5
Other property, plant & equipment	391	
Financial assets	30	4
Total impairment charges	985	29
Acquisition-related items		
- Gains	– 81	– 21
- Expenses		233
Total acquisition related items, net	– 81	212
Exceptional items		
Exceptional divestment gains	– 334	
Swiss restructuring expenses[3]	249	
Restructuring expenses - non-Swiss manufacturing sites[3]	90	52
Other restructuring expenses	81	
Legal-related items		
- Income	– 100	– 229
- Expense	80	45
Swiss pension curtailment gain		
Other exceptional income		– 17
Other exceptional expense	351	
Total exceptional items	417	– 149
Total adjustments	1 744	2 020
Core operating income	10 040	3 492
Core return on net sales	30.9%	35.1%

[1] Restated to reflect new segment allocation introduced during 2011 as explained in detail on page 159
[2] Consolidated results of Alcon, Inc., only included for the period from acquiring control on August 25, 2010 to December 31, 2010. Ophthalmic activities transferred from Pharmaceuticals and CIBA Vision transferred from Consumer Health included for the full year.
[3] Related to the Group-wide rationalization of manufacturing sites (Swiss portion amounts to approximately USD 100 million)

Sandoz	Vaccines and Diagnostics	Consumer Health	Corporate	Total
2011 USD millions	2011 USD millions	2011 USD millions	2011 USD millions	2011 USD millions
1 422	– 249	727	– 670	10 998
383	231	59	4	3 028	
25	8	14		619
				17
1	2	2		396
	135		23	192
26	145	16	23	1 224
				– 102
	5		12	250
	5		12	148
		– 44		– 378
		5		254
3	3	4		152
– 11		– 1		69
				– 329
204				329
– 106			– 85	– 208
		107	164	622
90	3	71	79	511
499	384	146	118	4 911
1 921	135	873	– 552	15 909
20.3%	6.8%	18.9%		27.2%

ALCON SEGMENT RECONCILIATION FROM 2010 RESTATED TO PRO FORMA DATA

On August 25, 2010 Novartis acquired a majority interest in Alcon, Inc. and its results have been included in the consolidated IFRS results of the Novartis Group and the Alcon segment since then (see note 2 to our consolidated financial statements for further information).

Novartis believes that the presentation of pro forma information will assist investors in their understanding of the combined companies' operating performance by setting a base for comparison with the 2011 consolidated results of Alcon. Without these pro forma results, the Alcon 2010 restated results through August 25, 2010 would consist only of the results from CIBA Vision and those Pharmaceuticals ophthalmics products which were transferred to Alcon. As a result, it is considered that a comparison between the 2011 Alcon results and the 2010 restated results would not be meaningful.

Therefore Novartis prepared pro forma information assuming the Alcon acquisition was completed on January 1, 2010. The pro forma information does not purport to present what the actual results of operations would have been had the transaction actually occurred on the date indicated.

The pro forma information includes the full 2010 consolidated income statement data for Alcon, Inc. from January 1, 2010 and adjusts for the impact of divestments required by regulators to approve the Alcon acquisition as well as for exceptional costs related to the acquisition of majority ownership of Alcon.

(in USD millions)
Net sales to third parties
Sales to other segments
Net sales of segments
Other revenues
Cost of Goods Sold
Gross profit
Marketing & Sales
Research & Development
General & Administration
Other income
Other expense
Operating income
as % of net sales
Core adjustments
Cost of Goods Sold
Research & Development
General & Administration
Other expense
Core Operating income
as % of net sales

[1] This assumes that the acquisition of Alcon, Inc. had occured on January 1, 2010. It therefore also reflects USD 1.4 billion of additional amortization of intangible assets arising from the purchase price allocation and excludes USD 145 million of change of control and acquisition related costs.

SUMMARY OF QUARTERLY FINANCIAL DATA FOR 2011 AND 2010

USD millions unless indicated otherwise	Q1	Q2	Q3	Q4	2011
Net sales	14 027	14 915	14 843	14 781	58 566
Other revenues	195	208	191	215	809
Cost of Goods Sold	– 4 458	– 4 619	– 4 788	– 5 118	– 18 983
Gross profit	9 764	10 504	10 246	9 878	40 392
Marketing & Sales	– 3 524	– 3 904	– 3 652	– 3 999	– 15 079
Research & Development	– 2 188	– 2 397	– 2 475	– 2 523	– 9 583
General & Administration	– 694	– 738	– 734	– 804	– 2 970
Other income	549	502	213	90	1 354
Other expense	– 499	– 645	– 647	– 1 325	– 3 116
Operating income	3 408	3 322	2 951	1 317	10 998
Income from associated companies	117	130	151	130	528
Interest expense	– 189	– 190	– 198	– 174	– 751
Other financial income and expense	22	– 16	4	– 12	– 2
Income before taxes	3 358	3 246	2 908	1 261	10 773
Taxes	– 537	– 520	– 420	– 51	– 1 528
Group net income	2 821	2 726	2 488	1 210	9 245
Attributable to:					
Shareholders of Novartis AG	*2 770*	*2 704*	*2 464*	*1 175*	*9 113*
Non-controlling interests	*51*	*22*	*24*	*35*	*132*
Basic earnings per share (USD)	*1.21*	*1.13*	*1.02*	*0.49*	*3.83*
Net sales by segment [1]					
Pharmaceuticals	7 698	8 338	8 159	8 313	32 508
Alcon	2 416	2 625	2 492	2 425	9 958
Sandoz	2 373	2 466	2 340	2 294	9 473
Vaccines and Diagnostics	371	299	655	671	1 996
Consumer Health	1 169	1 187	1 197	1 078	4 631
Group net sales	14 027	14 915	14 843	14 781	58 566
Operating income by segment [1]					
Pharmaceuticals	2 461	2 791	2 219	825	8 296
Alcon	524	371	341	236	1 472
Sandoz	412	283	333	394	1 422
Vaccines and Diagnostics	– 101	– 214	24	42	– 249
Consumer Health	265	225	210	27	727
Corporate income & expense, net	– 153	– 134	– 176	– 207	– 670
Group operating income	3 408	3 322	2 951	1 317	10 998
Core operating income	4 012	4 235	4 112	3 550	15 909
Core net income	3 376	3 564	3 539	3 011	13 490
Core basic earnings per share	*1.41*	*1.48*	*1.45*	*1.23*	*5.57*

[1] Restated to reflect new segment allocation introduced during 2011 as explained in detail on page 159

SUMMARY OF GROUP FINANCIAL DATA 2007–2011

USD millions unless indicated otherwise		2011
Net sales to third parties from continuing operations		**58 566**
Change relative to preceding year	%	15.7
Pharmaceuticals net sales		32 508
Change relative to preceding year	%	7.3
Alcon net sales		9 958
Change relative to preceding year	%	nm
Sandoz net sales		9 473
Change relative to preceding year	%	10.3
Vaccines and Diagnostics net sales		1 996
Change relative to preceding year	%	–31.6
Consumer Health net sales from continuing operations		4 631
Change relative to preceding year	%	6.2
Net sales from discontinued operations[3]		
Operating income from continuing operations		**10 998**
Change relative to preceding year	%	–4.6
As a % of net sales	%	18.8
As a % of average equity	%	16.2
As a % of average net operating assets	%	13.3
Operating income from discontinued operations[3]		
Net income from continuing operations		**9 245**
Change relative to preceding year	%	–7.3
As a % of net sales	%	15.8
Net income from discontinued operations[3]		
Total Group net income		**9 245**
As a % of average equity	%	13.6
Dividends of Novartis AG[4]		**5 762**
As % of net income from continuing operations[5]	%	63.2
Cash flows from operating activities[6]		**14 309**
Change relative to preceding year	%	1.7
As a % of net sales	%	24.4
Free cash flow[6]		**12 503**
Change relative to preceding year	%	1.3
As a % of net sales	%	21.3
Purchase of property, plant & equipment[6]		**2 167**
Change relative to preceding year	%	29.1
As a % of net sales	%	3.7
Depreciation of property, plant & equipment[6]		**1 728**
As a % of net sales	%	3.0
Core Research & Development[6]		**9 239**
As a % of net sales	%	15.8
Core Pharmaceuticals Division Research & Development		**6 860**
As a % of Pharmaceuticals Division net sales	%	21.1
Total assets		**117 496**
Liquidity		5 075
Equity		65 940
Debt/equity ratio		0.31:1
Current ratio		1.04:1
Net operating assets[6]		**81 094**
Change relative to preceding year	%	–4.2
As a % of net sales	%	138
Personnel costs[6]		**14 913**
As a % of net sales	%	25.5
Full-time equivalent associates at year-end[6]		**123 686**
Net sales per full-time equivalent associate (average)[6]	USD	481 818

[1] Restated to reflect new segment allocation introduced during 2011 as explained in detail on page 159
[2] 2007 and 2008 restated only for the transfer of CIBA Vision from Consumer Health to Alcon
[3] Discontinued Consumer Health operations (Gerber, Medical Nutrition and Nutrition & Santé).
[4] 2011: Proposed dividend for approval at the Annual General Meeting in February 2012. In all years, figure reflects only amounts paid to third party shareholders of Novartis AG.
[5] Based on net income from continuing operations attributable to the shareholders of Novartis AG
[6] Only continuing operations.
nm - not meaningful

NOVARTIS SHARE DEVELOPMENTS IN 2011

– Swiss-listed Novartis shares fall 2% to CHF 53.70
– American Depositary Shares (ADS) fall 3% to USD 57.17

Novartis shares finished at CHF 53.70, a decrease of 2% from the 2010 year-end closing price of CHF 54.95. The Novartis American Depositary Shares (ADS) decreased by 3% to USD 57.17 from USD 58.95 in 2010. The Swiss Market Index (SMI) in comparison fell at a 7.8% pace in 2011, whereas the world pharmaceutical index (MSCI) grew by 9.0% in the year. Over a longer-term period, Novartis has consistently delivered a solid performance, providing a 8.7% compounded annual total shareholder return between January 1, 1996, and December 31, 2011, clearly exceeding the compounded returns of 7.3% of its large pharmaceutical peers or the returns of 7.5% of the world pharmaceutical index (MSCI).

On April 8, 2011, 165 million shares were issued in connection with the merger with Alcon, composed of 108 million newly issued shares and 57 million treasury shares. This represented an increase in the shares outstanding of 7.2% since December 31, 2010.

The market capitalization of Novartis amounted to USD 138 billion as of December 31, 2011, compared to USD 134 billion as of December 31, 2010.

SHARE REPURCHASE PROGRAMS

In 2011, Novartis has carried out the share repurchases committed to at the time of the Alcon merger announcement. These share repurchases amounted to USD 5.3 billion including the purchases of USD 2.4 billion of Alcon shares, a contingent value payment of USD 0.5 billion and repurchases of USD 2.4 billion of Novartis shares (39.4 million shares). All of these Novartis shares were repurchased on the second trading line during the first six months of 2011. In addition, in the second half of 2011, Novartis repurchased USD 1.1 billion (20.4 million shares) of own shares on the first trading line. These shares will be kept as treasury shares to mostly cover future employee participation programs.

No shares were cancelled in 2011 as none had been repurchased in the 12 months to December 2010.

Novartis will propose to shareholders at the Annual General Meeting in February 2012 to cancel all shares repurchased on the second trading line during 2011. If approved, a total of 39.4 million shares, which corresponds to 1.4% of the registered Novartis share capital, will be cancelled, and the share capital will be reduced accordingly.

CONTINUOUSLY RISING DIVIDEND SINCE 1996

The Board of Directors proposes a 2% increase in the dividend payment for 2011 to CHF 2.25 per share (2010: CHF 2.20) for approval at the Annual General Meeting on February 23, 2012. This represents the 15th consecutive increase in the dividend paid per share since the creation of Novartis in December 1996. If the 2011 dividend proposal is approved by shareholders, dividends paid out on the outstanding shares will amount to approximately USD 5.8 billion (2010: USD 5.4 billion), resulting in a payout ratio of 63% of net income attributable to Novartis shareholders (2010: 55%). Based on the 2011 year-end share price of CHF 53.70, the dividend yield will be 4.2% (2010: 4.0%). The dividend payment date has been set for March 1, 2012. With the exception of 146.3 million treasury shares, all shares issued are dividend-bearing.

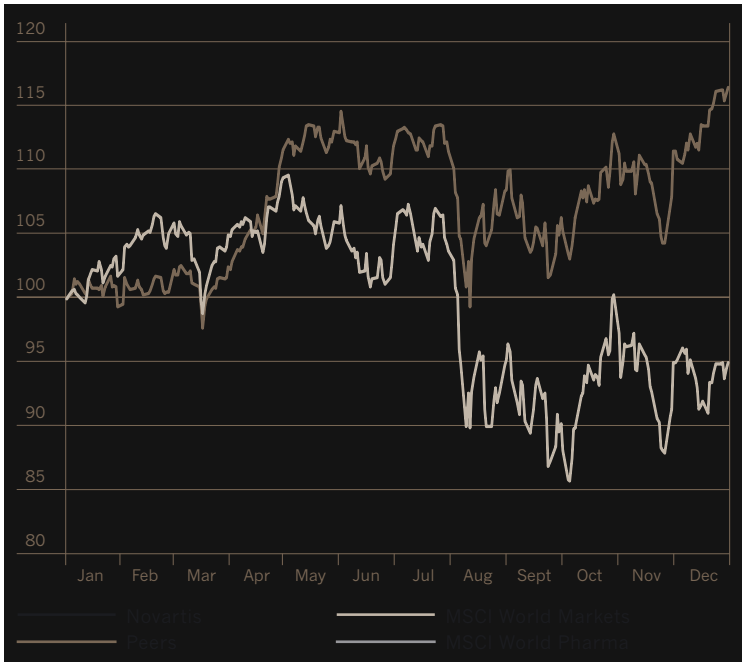
DIRECT SHARE PURCHASE PLANS

Novartis has been offering US investors since 2001 an ADS Direct Share Purchase Plan that provides investors an easy and inexpensive way of directly purchasing Novartis shares and of reinvesting dividends. This plan holds Novartis ADSs that are listed on the New York Stock Exchange under the trading symbol NVS. At the end of 2011, the ADS Direct Plan had 1 122 participants.

Starting in September 2004, Novartis began offering a Direct Share Purchase Program to investors residing in Switzerland, Liechtenstein, France and the United Kingdom, which was the first of its kind in Europe. This plan offers an easy and inexpensive way for investors to directly purchase Novartis registered shares and for them to be held at no cost in a deposit account with SIX SAG AG. At the end of 2011, a total of 9 403 shareholders were enrolled in this program.

INFORMATION ON NOVARTIS SHARES

Further information can be found on the Internet at http://www.novartis.com/investors.


120
115
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Jan
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Mar
Apr
May
Jun
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Aug
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Nov
Dec
Novartis
Peers
MSCI World Markets
MSCI World Pharma

TRADING

Novartis shares are listed in Switzerland and traded on the SIX Swiss Exchange, while American Depositary Shares (ADSs) are listed on the New York Stock Exchange.

SYMBOLS

	SIX Swiss Exchange (Reuters/Bloomberg)	NYSE (Reuters/ Bloomberg)
Shares	NOVN.VX/NOVN VX	
ADSs		NVS

WIDELY DISPERSED SHAREHOLDINGS

Novartis shares are widely held. As of December 31, 2011, Novartis had approximately 165 000 shareholders (2010: 160 000) listed in its share register, representing 75% of issued shares. Based on the Novartis AG share register and excluding treasury shares, approximately 43% (2010: 45%) of the shares registered by name were held in Switzerland and 45% were held in the US (2010: 42%). Approximately 12% of the shares registered in the share register were held by individual investors, while 88% were held by legal entities, nominees and fiduciaries.

CONSOLIDATED INCOME STATEMENTS

(For the years ended December 31, 2011 and 2010)

	Note	2011 USD millions
Net sales	3	58 566
Other revenues		809
Cost of Goods Sold		–18 983
Gross profit		**40 392**
Marketing & Sales		–15 079
Research & Development		–9 583
General & Administration		–2 970
Other income		1 354
Other expense		–3 116
Operating income	3	**10 998**
Income from associated companies	4	528
Interest expense	5	–751
Other financial income and expense	5	–2
Income before taxes		**10 773**
Taxes	6	–1 528
Net income		**9 245**
Attributable to:		
Shareholders of Novartis AG		*9 113*
Non-controlling interests		*132*
Basic earnings per share (USD)	7	3.83
Diluted earnings per share (USD)	7	3.78

The accompanying notes form an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(For the years ended December 31, 2011 and 2010)

	Note	2011 USD millions
Net income		**9 245**
Fair value adjustments on financial instruments, net of taxes	8.1	21
Actuarial losses from defined benefit plans, net of taxes	8.2	– 1 421
Novartis share of other items recorded in comprehensive income recognized by associated companies, net of taxes	8.3	1
Currency translation effects		– 559
Total comprehensive income		**7 287**
Attributable to:		
Shareholders of Novartis AG		*7 171*
Non-controlling interests		*116*

The accompanying notes form an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(For the years ended December 31, 2011 and 2010)

	Note	Share capital USD millions	Treasury shares USD millions	Share premium USD millions	Retained earnings USD millions	Total value adjustments USD millions	Total reserves USD millions	Non-controlling interests USD millions	Total equity USD millions
Total equity at January 1, 2010									
Net income									
Other comprehensive income									
Total comprehensive income									
Dividends									
Sale of treasury shares, net									
Equity-based compensation									
Impact of change of ownership of Alcon, Inc.									
Excess of consideration exchanged for acquiring non-controlling interest compared to the recorded amounts									
Changes in non-controlling interests									
Total of other equity movements									
Total equity at December 31, 2010									
Net income					9 113		9 113	132	9 245
Other comprehensive income	8				1	– 1 943	– 1 942	– 16	– 1 958
Total comprehensive income					**9 114**	**– 1 943**	**7 171**	**116**	**7 287**
Dividends	9.1				– 5 368		– 5 368		– 5 368
Purchase of treasury shares, net	9.2		– 31		– 3 429		– 3 429		– 3 460
Equity-based compensation	9.3		4		802		802		806
Excess of consideration exchanged for acquiring non-controlling interest compared to the recorded amounts	9.5				– 5 664		– 5 664		– 5 664
Changes in non-controlling interests	9.6							– 6 593	– 6 593
Fair value of Novartis shares used to acquire outstanding non-controlling interests in Alcon, Inc.	9.7	59	31		9 073		9 073		9 163
Total of other equity movements		**59**	**4**		**– 4 586**		**– 4 586**	**– 6 593**	**– 11 116**
Total equity at December 31, 2011		**1 016**	**– 121**	**198**	**65 602**	**– 851**	**64 949**	**96**	**65 940**

The accompanying notes form an integral part of the consolidated financial statements.

CONSOLIDATED BALANCE SHEETS
(At December 31, 2011 and 2010)

	Note	2011 USD millions
Assets		
Non-current assets		
Property, plant & equipment	10	15 627
Goodwill	11	29 943
Intangible assets other than goodwill	11	31 969
Investments in associated companies	4	8 622
Deferred tax assets	12	5 857
Financial assets	13	976
Other non-current non-financial assets		418
Total non-current assets		**93 412**
Current assets		
Inventories	14	5 930
Trade receivables	15	10 323
Marketable securities and derivative financial instruments	16	1 366
Cash and cash equivalents	16	3 709
Other current assets	17	2 756
Total current assets		**24 084**
Total assets		**117 496**
Equity and liabilities		
Equity		
Share capital	18	1 016
Treasury shares	18	– 121
Reserves		64 949
Issued share capital and reserves attributable to Novartis AG shareholders		**65 844**
Non-controlling interests		96
Total equity		**65 940**
Liabilities		
Non-current liabilities		
Financial debts	19	13 855
Deferred tax liabilities	12	6 761
Provisions and other non-current liabilities	20	7 792
Total non-current liabilities		**28 408**
Current liabilities		
Trade payables		4 989
Financial debts and derivative financial instruments	21	6 374
Current income tax liabilities		1 706
Provisions and other current liabilities	22	10 079
Total current liabilities		**23 148**
Total liabilities		**51 556**
Total equity and liabilities		**117 496**

The accompanying notes form an integral part of the consolidated financial statements.

CONSOLIDATED CASH FLOW STATEMENTS
(For the years ended December 31, 2011 and 2010)

	Note	2011 USD millions
Net income		**9 245**
Reversal of non-cash items	23.1	9 300
Dividends from associated companies		403
Dividends received from marketable securities		1
Interest received		66
Interest paid		– 640
Other financial payments		– 47
Taxes paid		– 2 435
Cash flows before working capital and provision changes		**15 893**
Restructuring payments and other cash payments from provisions		– 1 471
Change in net current assets and other operating cash flow items	23.2	– 113
Cash flows from operating activities		**14 309**
Purchase of property, plant & equipment		– 2 167
Proceeds from sales of property, plant & equipment		61
Purchase of intangible assets		– 220
Proceeds from sales of intangible assets		643
Purchase of financial assets		– 139
Proceeds from sales of financial assets		59
Purchase of non-current non-financial assets		– 48
Proceeds from sales of non-current non-financial assets		5
Acquisitions of interests in associated companies		– 12
Acquisitions and divestments of businesses	23.3	– 569
Purchase of marketable securities		– 1 750
Proceeds from sales of marketable securities		3 345
Cash flows used in investing activities		**– 792**
Acquisition of treasury shares		– 3 628
Disposal of treasury shares		159
Increase in non-current financial debts		281
Repayment of non-current financial debts		– 28
Change in current financial debts		– 3 054
Proceeds from issuance of share capital to third parties		4
Acquisition of Alcon non-controlling interests		– 3 187
Dividends paid to non-controlling interests and other financing cash flows		– 203
Dividends paid to shareholders of Novartis AG		– 5 368
Cash flows used in / from financing activities		**– 15 024**
Net effect of currency translation on cash and cash equivalents		– 103
Net change in cash and cash equivalents		**– 1 610**
Cash and cash equivalents at January 1		5 319
Cash and cash equivalents at December 31		**3 709**

The accompanying notes form an integral part of the consolidated financial statements.

1. ACCOUNTING POLICIES

The Novartis Group (Group or Novartis) consolidated financial statements comply with the International Financial Reporting Standards (IFRS) as published by the International Accounting Standards Board (IASB). They are prepared in accordance with the historical cost convention except for items that are required to be accounted for at fair value.

The preparation of financial statements requires management to make estimates and other judgments that affect the reported amounts of assets and liabilities as well as the accounting and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual outcomes could differ from those estimates.

SCOPE OF CONSOLIDATION

The consolidated financial statements include all companies that Novartis AG, Basel, Switzerland directly or indirectly controls (generally more than 50% of voting interest). Special purpose entities, irrespective of their legal structure, are consolidated in instances where the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from their activities.

Investments in associated companies (generally defined as investments in companies in which Novartis holds between 20% and 50% of voting shares or over which it otherwise has significant influence) and joint ventures are accounted for using the equity method. In these situations, the Group records its share of the estimated associated company's net income and equity. The share of results attributed to Novartis from these associated companies is included in the income statement line "Income from associated companies" and is calculated after the deduction of related taxes and non-controlling interests included in the financial results of the associated company.

PRINCIPLES OF CONSOLIDATION

The Group's financial year end is December 31, and the annual closing date of the individual financial statements incorporated into the Group's consolidated financial statements is December 31.

The acquisition method of accounting is used to account for business combinations by the Group in transactions where Novartis takes control of another entity. The cost of an acquisition is measured as the fair value of the transferred assets as well as incurred or assumed liabilities at the date of acquisition. The fair value of any contingent consideration potentially due to former owners of the acquired business is included in the cost of the acquisition. Transaction costs for acquisitions are expensed as incurred. Identifiable acquired assets as well as assumed liabilities and contingent liabilities obtained in a business combination are measured initially at their fair values as of the acquisition date, irrespective of the extent of any non-controlling interest. The excess of the consideration transferred to obtain a controlling interest and the fair value of any previous non-controlling interest in the acquiree, over the fair value of the Group's share of net identifiable assets in a business combination, is recorded as goodwill in the balance sheet and is denominated in the functional currency of the related acquisition. The excess of the cost of acquiring an additional interest in an entity already controlled by the Group over the identifiable net assets related to that non-controlling interest is recorded in consolidated equity. Any difference between the proceeds received from reducing the interest in a controlled entity compared to the share of the related net assets is recorded in consolidated equity. For an acquisition of an entity in stages, any revaluation of an initial non-controlling interest in an entity required as a result of obtaining control is recorded in the consolidated income statement. Novartis has elected to value any remaining outstanding non-controlling interest in a controlled subsidiary only at its proportionate share of the fair value of the net identified assets. Companies acquired or disposed of during the year are included in the consolidated financial statements from the date of acquisition or until the date of disposal.

Intercompany income and expenses, including unrealized profits from internal Novartis transactions and intercompany receivables and payables, are eliminated.

FOREIGN CURRENCIES

The consolidated financial statements of Novartis are presented in US dollars (USD). The functional currency of certain Swiss and foreign finance companies used for preparing the consolidated financial statements is USD instead of the respective local currencies. This reflects the fact that the cash flows and transactions of these entities are primarily denominated in USD. Generally, the respective local currency is used as the functional currency for other entities. In the respective entity financial statements, monetary assets and liabilities denominated in foreign currencies are translated at the prevailing exchange rate at the balance sheet date. Transactions are recorded using the approximate exchange rate at the time of the transaction. All resulting foreign exchange transaction gains and losses are recognized in the entity's income statement.

Income, expense and cash flows of the consolidated entities have been translated into USD using the average of monthly exchange rates during the year. Balance sheets are translated using year-end exchange rates. Translation differences arising from movements in exchange rates used to translate equity and long-term intercompany financing transactions relating to net investments in a foreign entity, retained earnings and other equity components and net income for the year are allocated directly to the cumulative

translation effects included in the fair value adjustments in the consolidated statement of comprehensive income. Translation gains and losses accumulated in the consolidated statement of comprehensive income are included in the income statement when the foreign operation is completely or partially liquidated or is sold.

IMPAIRMENT OF LONG-LIVED INTANGIBLE AND TANGIBLE ASSETS

Novartis reviews long-lived intangible and tangible assets for impairment whenever events or changes in circumstance indicate that the asset's balance sheet carrying amount may not be recoverable.

An asset, as defined, is generally considered impaired when its carrying amount exceeds its estimated recoverable amount. The recoverable amount is measured as the higher of: a) an asset or related cash-generating unit's fair value less costs to sell and b) its value in use. Fair value reflects the Group's estimates of assumptions that market participants would use when pricing the asset. In contrast the value in use concept reflects the Group's estimates based on its expected use of the asset, including the effects of factors that may be specific to the Group and not applicable to entities in general. Value in use, and fair value, are measured principally on the basis of discounted cash flow analysis using management's best estimate of the range of economic conditions that are expected to exist over the remaining useful life of the asset. Also value in use measurements specifically exclude consideration of any estimated future net cash flows that might be expected to arise from future restructuring or from improving or enhancing the asset's performance.

The net present values involve highly sensitive estimates and assumptions including consideration of factors such as the following:
– the amount and timing of projected future cash flows;
– the selected discount and tax rate;
– the outcome of Research & Development (R&D) activities (compound efficacy, results of clinical trials, etc.);
– the amount and timing of projected costs to develop In-Process Research & Development (IPR&D) projects into commercially viable products;
– the probability of obtaining regulatory approval;
– long-term sales forecasts for periods of up to 25 years;
– sales erosion rates after the end of patent protection and timing of the entry of generic competition; and
– the behavior of competitors (launch of competing products, marketing initiatives, etc.).

Factors that could result in shortened useful lives or impairments include:
– entry into the market of generic or alternative products;
– lower than expected sales for acquired products or for sales associated with patents and trademarks;
– lower than anticipated future sales resulting from acquired IPR&D;
– the closing of facilities; and
– changes in the planned use of property, plant & equipment.

Goodwill and the Alcon brand name have an indefinite useful life and impairment testing is done at least annually. Any impairment charge is recorded in the consolidated income statement under "Other expense". Novartis considers that the Alcon brand name has an indefinite life as Alcon has a history of strong revenue and cash flow performance, and Novartis has the intent and ability to support the brand with marketplace spending for the foreseeable future. IPR&D is also assessed for impairment at least on an annual basis, with any impairment charge recorded in the consolidated income statement under "Research & Development". Once a project included in IPR&D has been successfully developed and is available for use, it is amortized over its useful life in the consolidated income statement under "Cost of Goods Sold", where related impairment charges, if any, are also recorded.

Novartis has adopted a uniform method for assessing goodwill and indefinite-life intangible assets for impairment and any other intangible asset indicated as being possibly impaired. Generally, for intangible assets Novartis uses cash flow projections for the whole useful life of these assets, and for goodwill and the Alcon brand name, Novartis utilizes cash flow projections for a five-year period based on management forecasts, with a terminal value based on sales projections usually in line with or lower than inflation rates for later periods. Probability-weighted scenarios are typically used.

Discount rates used in these scenarios are based on the Group's weighted average cost of capital as an approximation of the weighted average cost of capital of a comparable market participant, which are adjusted for specific country and currency risks associated with cash flow projections.

Due to the above factors, actual cash flows and values could vary significantly from forecasted future cash flows and related values derived using discounting techniques.

PROPERTY, PLANT & EQUIPMENT

Land is recorded at acquisition cost less accumulated impairment, if any. Prepayments for long-term leasehold land agreements are amortized over the life of the lease.

Other items of property, plant & equipment are recorded at acquisition cost or production cost and are depreciated on a straight-line basis to the consolidated income statement over the following estimated useful lives:

Buildings	20 to 40 years
Other property, plant & equipment:	
– Machinery and equipment	7 to 20 years
– Furniture and vehicles	5 to 10 years
– Computer hardware	3 to 7 years

Additional costs that enhance the future economic benefit of property, plant & equipment are capitalized. Government grants for construction activities and equipment are deducted from the carrying value of the assets. Borrowing costs associated with the construction of new property, plant and equipment projects are capitalized. Property, plant & equipment is reviewed for impairment whenever events

or changes in circumstances indicate that the balance sheet carrying amount may not be recoverable.

Property, plant & equipment that are financed by leases giving Novartis substantially all risks and rewards of ownership are capitalized at the lower of the fair value of the leased asset or the present value of minimum lease payments at the inception of the lease. These are depreciated in the same manner as other assets over the shorter of the lease term or their useful life. Leases in which a significant portion of the ownership risks and rewards are retained by the lessor are classified as operating leases. These are charged to the consolidated income statement over the life of the lease, generally, on a straight-line basis.

INTANGIBLE ASSETS

GOODWILL

The excess of the consideration transferred to obtain a controlling interest and the fair value of any previous non-controlling interest in the acquiree, over the fair value of the Group's share of net identifiable assets in a business combination, is recorded as goodwill in the balance sheet and is denominated in the functional currency of the related acquisition. Goodwill is allocated to an appropriate cash-generating unit which is defined as the smallest group of assets that generates independent cash inflows that support the goodwill. All goodwill is tested for impairment at least annually. In addition, goodwill is evaluated for impairment at each reporting date for each cash-generating unit with any resulting goodwill impairment charge recorded under "Other Expense" in the consolidated income statement.

Goodwill is tested for possible impairment annually and whenever events or changes in circumstances indicate the value may not be fully recoverable. If the initial accounting for goodwill in the reporting period is only provisional, it is not tested for impairment unless an impairment indicator exists, and not included in the calculation of the net book values at risk from changes in the amount of discounted cash flows. An impairment is recognized when the consolidated balance sheet carrying amount is higher than the greater of "fair value less costs to sell" and "value in use."

OTHER INTANGIBLE ASSETS

All identifiable intangible assets acquired in a business combination are recognized at their fair value. Furthermore, all acquired Research & Development assets, including upfront and milestone payments on licensed or acquired compounds, which are deemed to enhance the intellectual property of Novartis, are capitalized at cost as intangible assets, when it is probable that future economic benefits will arise, even though uncertainties exist as to whether the R&D projects will be ultimately successful in producing a commercial product.

All Novartis intangible assets are allocated to cash-generating units. IPR&D and the Alcon brand name are the only classes of separately identified intangible assets that are not amortized. Both are tested for impairment on an annual basis or when facts and circumstances warrant an impairment test. Any impairment charge is recorded in the consolidated income statement under "Research & Development" for IPR&D and under "Other Expense" for the Alcon brand name. Once a project included in IPR&D has been successfully developed and is available for use, it is amortized over its useful life in the consolidated income statement under "Cost of Goods Sold," where any related impairment charges are also recorded. The Alcon brand name is considered to have an indefinite life as Alcon has a history of strong revenue and cash flow performance, and we have the intent and ability to support the brand with marketplace spending for the foreseeable future.

Internally developed computer software is capitalized and once available for use amortized over its estimated useful life.

All other intangible assets are amortized over their estimated useful lives once they are available for use and tested for impairment whenever facts and circumstances indicate that their carrying value may not be recoverable. The useful lives assigned to acquired intangible assets are based on the period over which they are expected to generate economic benefits, commencing in the year in which they first generate sales or are used in development. Acquired intangible assets are amortized on a straight-line basis over the following periods:

Trademarks	Over their estimated economic or legal life with a maximum of 20 years
Currently marketed products and marketing know-how	5 to 25 years
Technology	10 to 30 years
Software	3 to 5 years
Others	3 to 5 years

DEFINED BENEFIT PENSION PLANS, OTHER POST-EMPLOYMENT BENEFITS AND OTHER NON-CURRENT BENEFITS OF ASSOCIATES

DEFINED BENEFIT PENSION PLANS

The liability in respect of defined benefit pension plans is the defined benefit obligation calculated annually by independent actuaries using the projected unit credit method. The defined benefit obligation is measured as the present value of the estimated future payments required to settle the obligation that is attributable to the service of associates in the current and prior periods. The service cost for such pension plans is included in the personnel expenses of the various functions where the associates are employed, while the expected return on assets and interest expense are recognized as "Other income" or "Other expense". Plan assets are recorded at their fair value. Unvested past service costs arising from amendments to pension plans are charged or credited on a straight-line basis to income over the associates' remaining vesting period. Vested past service costs, including such costs for retired associates are immediately recognized in the consolidated income statement. Gains or losses arising from plan curtailments or settlements are accounted for at the time they occur. Any net pension asset is limited to the present value of future economic benefits available to the Group in the form of refunds from the plan or expected reductions in future contributions to the plan.

The effects of changes in actuarial assumptions and experience adjustments on the value of plan assets and liabilities of defined benefit plans are immediately recognized in the consolidated balance sheet with a corresponding movement in the consolidated statement of comprehensive income.

OTHER POST-EMPLOYMENT BENEFITS

Certain subsidiaries provide healthcare and insurance benefits for a portion of their retired associates and their eligible dependents. The cost of these benefits is actuarially determined and accrued over the service lives of the related associates. Service costs are included in the personnel expenses of the various functions where the associates are located, while the expected return on assets and interest expense are recognized as "Other income" or "Other expense". The related obligation is recognized in non-current liabilities.

OTHER NON-CURRENT BENEFITS OF ASSOCIATES

Other non-current benefits of associates represent amounts due to associates under deferred compensation arrangements available in certain jurisdictions in which the Group conducts its operations. Benefit costs are recognized on an accrual basis in the personnel expenses of the various functions where the associates are located. The related obligation is recognized in other non-current liabilities.

EQUITY-BASED COMPENSATION

The fair value of Novartis shares, restricted shares, restricted share units (RSU) and American Depositary Shares (ADS) and related options granted to associates as compensation is recognized as an expense over the related vesting or service period adjusted to reflect actual and expected vesting levels. The charge for equity-based compensation is included in the personnel expenses which are allocated to functional costs and credited to equity for equity-settled amounts or to other current liabilities for cash-settled amounts. An option's fair value at grant date is calculated using the trinomial valuation method. Accurately measuring the value of share options is difficult and requires an estimate of factors used in the valuation model. These key factors involve uncertain future events, such as expected dividend yield and expected share price volatility. Expected volatilities are based on those implied from listed warrants on Novartis shares, and – to the extent that equivalent options are not available – a future extrapolation based on historical volatility. Novartis shares, restricted shares, RSUs and ADSs are valued using the market value on the grant date.

REVENUE RECOGNITION

Revenue is recognized when there is persuasive evidence that a sales arrangement exists, title and risks and rewards for the products are transferred to the customer, the price is determinable and collectability is reasonably assured. Where contracts contain customer acceptance provisions, sales are recognized upon the satisfaction of acceptance criteria. Revenue is recognized for products that are stockpiled at the request of the customer once the products have been inspected and accepted by the customer and there is no right of return or replenishment on product expiry, and cost of storage will be paid by the customer on normal commercial terms. Provisions for rebates and discounts granted to government agencies, wholesalers, retail pharmacies, managed care and other customers are recorded as a reduction of revenue at the time the related revenues are recorded or when the incentives are offered. They are calculated on the basis of historical experience and the specific terms in the individual agreements. Provisions for refunds granted to healthcare providers under innovative pay for performance agreements are recorded as a reduction of revenue at the time the related revenues are recorded. They are calculated on the basis of historical experience and clinical data for the product as well as the specific terms in the individual agreements. In cases where historical experience and clinical data are not sufficient for a reliable estimation of the outcome, revenue recognition is deferred until such history is available.

Cash discounts are offered to customers to encourage prompt payment and are recorded as revenue deductions. Wholesaler shelf-inventory adjustments are granted to customers based on the existing inventory of a product at the time of decreases in the invoice or contract price of a product or at the point of sale if a price decline is reasonably estimable. Where there is an historical experience of Novartis agreeing to customer returns or Novartis can

otherwise reasonably estimate expected future returns, Novartis records a provision for estimated sales returns. In doing so it applies the estimated rate of return, determined based on historical experience of customer returns or considering any other relevant factors, to the amounts invoiced also considering the amount of returned products to be destroyed versus products that can be placed back in inventory for resale. Where shipments are made on a re-sale or return basis, without sufficient historical experience for estimating sales returns, revenue is only recorded when there is evidence of consumption or when the right of return has expired. Provisions for revenue deductions are adjusted to actual amounts as rebates, discounts and returns are processed.

RESEARCH & DEVELOPMENT

Internal Research & Development (R&D) costs are fully charged to the consolidated income statement in the period in which they are incurred. The Group considers that regulatory and other uncertainties inherent in the development of new products preclude the capitalization of internal development expenses as an intangible asset until marketing approval from a regulatory authority is obtained in a major market such as for the US, the EU, Switzerland or Japan.

Payments made to third parties in compensation for subcontracted R&D that is deemed not to enhance the intellectual property of Novartis such as contract research and development organizations are expensed as internal R&D expenses in the period in which they are incurred. Such payments are only capitalized if they meet the criteria for recognition of an internally generated intangible asset, usually when marketing approval has been achieved from a regulatory authority in a major market.

Payments made to third parties in order to in-license or acquire intellectual property rights, compounds and products (In-Process Research & Development assets, "IPR&D"), including initial upfront and subsequent milestone payments, are capitalized as are payments for other assets, such as technologies to be used in R&D activities. If additional payments are made to the originator company to continue to perform R&D activities, an evaluation is made as to the nature of the payments. Such additional payments will be expensed if such additional payments are deemed to be compensation for subcontracted R&D services not resulting in an additional transfer of intellectual property rights to Novartis. By contrast, such additional payments will be capitalized if these additional payments are deemed to be compensation for the transfer to Novartis of additional intellectual property developed at the risk of the originator company. Subsequent internal R&D costs in relation to IPR&D and other assets are expensed since the technical feasibility of the internal R&D activity can only be demonstrated by the receipt of marketing approval for a related product from a regulatory authority in a major market.

Costs for post-approval studies performed to support the continued registration of a marketed product are recognized as marketing expenses. Costs for activities that are required by regulatory authorities as a condition for obtaining marketing approval are charged as development expenses as they are incurred in cases where it is anticipated that the related product will be sold over a longer period than the activities required to be performed to obtain the marketing approval. In the rare cases where costs related to the conditional approval need to be incurred over a period beyond that of the anticipated product sales, then the expected costs of these activities will be expensed over the shorter period of the anticipated product sales. As a result, all activities necessary as a condition to maintain a received approval, whether conditional or not, are expensed in the consolidated income statement.

IPR&D assets are amortized in the consolidated income statement over their useful life once the related project has been successfully developed and regulatory approval for a product launch has been obtained. Other acquired technologies included in intangible assets are amortized in the consolidated income statement over their estimated useful lives.

Laboratory buildings and equipment included in property, plant & equipment are depreciated in the consolidated income statement over their estimated useful lives.

GOVERNMENT GRANTS

Grants from the government are recognized at their fair value where there is a reasonable assurance that the grant will be received and the Group will comply with all attached conditions.

Government grants are deferred and recognized in the consolidated income statement over the period necessary to match them with the related costs which they are intended to compensate.

Government grants relating to property, plant and equipment are deducted from the carrying value of assets and released to the consolidated income statement on a straight-line basis over the expected lives of the related assets.

Government grants related to income are deducted in reporting the related expense.

PROVISIONS

Novartis records provisions when it is judged probable that a liability has been incurred and the amount can be reliably estimated. These provisions are adjusted periodically as assessments change or additional information becomes available.

Cost of future expenditures do not usually reflect any insurance or other claims or recoveries, as Novartis only recognizes insurance or other recoveries at such time the amount is reliably estimable and collection is virtually certain.

PRODUCT LIABILITIES

Provisions are made for present product liability obligations resulting from past sales including related legal and other fees and expenses. The provision is actuarially determined taking into consideration such factors as past experience, amount and number of claims reported and estimates of claims incurred but not yet reported. Individually significant cases are provided for when probable and reliably estimable.

LEGAL LIABILITIES

Provisions are made for anticipated settlement costs where a reliable estimate can be made of the probable outcome of legal or other disputes against the Group. In addition, provisions are made for legal and other fees and expenses arising from claims affecting Novartis.

ENVIRONMENTAL LIABILITIES

Novartis is exposed to environmental liabilities relating to its past operations, principally in respect to remediation costs. Provisions for remediation costs are made when expenditure on remedial work is probable and the cost can be reliably estimated. These remediation costs are calculated as the present value of expected cash outflows including anticipated inflation, discounted at a rate based on the market yields for high quality corporate bonds. The increase in provisions due to the passage of time and the effect of changes in the discount rates are included in Interest Expense.

CONTINGENT CONSIDERATION IN A BUSINESS COMBINATION

Contingent consideration potentially due to former owners as part of the consideration paid for a business combination is recognized as a liability at fair value as of the acquisition date. Any subsequent change in the fair value of the contingent consideration liability is recognized in the consolidated income statement.

RESTRUCTURING CHARGES

Restructuring charges are accrued against operating income in the period in which management has committed to a plan and has raised the valid expectation of the plan's implementation by those affected and the amount can be reliably estimated. The Group recognizes the costs for terminating the employment contracts of associates when it is demonstrably committed to either terminating employment according to a detailed formal plan without possibility of withdrawal or when it is committed to providing termination benefits as a result of an offer made to encourage voluntary redundancy.

Charges to increase restructuring provisions are included in "Other expense" in the consolidated income statement. Corresponding releases are recorded in "Other income".

DIVIDENDS

Dividends are recorded in the Group's consolidated financial statements in the period in which they are approved by the Group's shareholders.

TREASURY SHARES

Treasury shares are deducted from consolidated equity at their nominal value of CHF 0.50 per share. Differences between this amount and the amount paid for acquiring, or received for disposing of, treasury shares are recorded in consolidated retained earnings.

REPORTING SEGMENTS

Reporting segments are presented in a manner consistent with the internal reporting to the chief operating decision maker. The chief operating decision maker, who is responsible for allocating resources and assessing the performance of the reporting segments, has been identified as being the Executive Committee.

STATUS OF ADOPTION OF SIGNIFICANT NEW OR AMENDED IFRS STANDARDS OR INTERPRETATIONS

The following new or amended IFRS standards will, based on a Novartis analysis, be of significance to the Group, but have not yet been adopted.

In 2009, 2010 and 2011, IFRS 9 *Financial Instruments* was issued which will substantially change the classification and measurement of financial instruments, hedging requirements and the recognition of certain fair value changes in the consolidated financial statements. Currently, only new requirements on the classification and measurement for financial assets and financial liabilities have been issued. The mandatory effective date for requirements issued as part of IFRS 9 will be on or after January 1, 2015. Early application of the requirements is permitted.

In 2011, IAS 19 revised on *Employee Benefits* was issued, for adoption by January 1, 2013. The principal impact for Novartis will be that the concepts of expected return on plan assets and interest expense on the defined benefit obligation as separate components of defined benefit cost will be replaced by a concept that interest will be calculated on the net of the defined benefit obligation and funded post-employment obligation assets generally using an interest rate reflecting market yields of high quality corporate bonds in deep markets. If this concept had been adopted by Novartis in 2011, it is estimated that operating income would have been lower by approximately USD 260 million. Novartis will retrospectively adopt the standard on January 1, 2013.

Two other new standards were also issued in 2011, IFRS 10 *Consolidated Financial Statements* and IFRS 11 *Joint Arrangements* which are potentially important for Novartis. Under IFRS 10, Novartis will need to consolidate an investee based on control, i.e. when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. IFRS 11 will require that Novartis classifies joint arrangements as either joint operations,

where assets, liabilities, revenues and expenses are accounted for proportionally in accordance with the agreement, or as joint ventures, which are accounted for under the equity method. These new standards become effective on January 1, 2013.

The following IFRSs and amendments are not yet effective and are not early adopted by the Group:

– IFRS 12, *Disclosures of interests in other entities*, effective for annual periods beginning on or after January 1, 2013
– IFRS 13, *Fair value measurement*, effective for annual periods beginning on or after January 1, 2013
– Amendment to IAS 1, *Presentation of items of other comprehensive income*, effective for annual periods beginning on or after July 1, 2012

Although Novartis is still completing its evaluation of these new standards, apart from where indicated, Novartis does not currently consider that the other new standards will have a significant impact.

2. SIGNIFICANT TRANSACTIONS, BUSINESS COMBINATIONS AND DIVESTMENTS

The following acquisitions, business combinations or other significant transactions occurred during 2011 and 2010. See notes 3 and 24 for further details of the impact of these transactions on the consolidated financial statements.

ALCON MAJORITY CONTROL IN 2010; FULL OWNERSHIP AND MERGER IN 2011

On August 25, 2010 Novartis completed the acquisition of a further 52% interest in Alcon, Inc. (Alcon) following on from the January 4, 2010 announcement that Novartis had exercised its call option to acquire Nestlé's remaining 52% Alcon interest for approximately USD 28.3 billion or USD 180 per share. The overall purchase price of USD 38.7 billion included certain adjustments for Alcon dividends and interest due. This increased the interest in Alcon to a 77% controlling interest as Novartis had already acquired an initial 25% Alcon interest from Nestlé for USD 10.4 billion or USD 143 per share in July 2008.

On December 14, 2010 Novartis entered into a definitive agreement to merge Alcon into Novartis in consideration for Novartis shares and a Contingent Value Amount. The acquisition of the remaining outstanding non-controlling interests in Alcon were separate transactions following the previous acquisition of majority ownership in Alcon by Novartis in 2010.

On April 8, 2011 a Novartis Extraordinary General Meeting approved the merger with Alcon, Inc. leading to the creation of the Alcon Division which became the fifth reported segment in Novartis' strategically diversified healthcare portfolio. The Extraordinary General Meeting also authorized the issuance of 108 million new shares. Alcon shareholders received 2.9228 Novartis shares (which included a dividend adjustment) and USD 8.20 in cash for each share of Alcon, resulting in a total consideration of USD 168.00 per share.

For business combinations achieved in stages, IFRS requires that any previously held interest of an acquirer in an acquiree is adjusted to its fair value through the consolidated income statement as of the acquisition date. The agreement that Novartis entered into with Nestlé in 2008 specified an average price of up to USD 168 per share for all of the approximately 77% interest in Alcon held by Nestlé, including USD 143 per share for the initial 25% interest acquired by Novartis in 2008, and a maximum of USD 181 per share for the remaining 52%, including a premium for the change of majority ownership.

Novartis reassessed the fair value of the initial 25% non-controlling interest in Alcon it acquired from Nestlé in 2008. In 2010, Novartis recognized a revaluation gain of USD 378 million on its initial 25% equity-method investment in Alcon upon acquiring a 52% controlling interest in the second-stage purchase from Nestlé on August 25, 2010. This gain was based on Novartis concluding that the fair value of that interest had a corresponding per-share value of USD 139. On this date the quoted marked price of Alcon on the NYSE was USD 160. Novartis measured this revaluation gain based on the estimated current fair value of its investment in Alcon, with the assistance of outside specialist investment bank advisors. This valuation demonstrated that, as at August 25, 2010, the quoted price for Alcon was affected by an anticipated premium on Novartis' eventual purchase of the 23% not owned at that time. Novartis concluded that this "premium" should not be included in the valuation of the previously held equity interest.

This gain was reduced by USD 43 million of accumulated losses recorded in the consolidated statement of comprehensive income of Novartis since the July 2008 acquisition date of the initial interest. These accumulated losses were recorded under the equity accounting method, which requires such accumulated losses to be recycled into the consolidated income statement at the time of

acquiring majority ownership. The net amount of USD 335 million was recorded as a gain under "Income from Associated Companies".

At December 31, 2010 Novartis recorded the outstanding non-controlling interests in Alcon at their proportionate share of identifiable net assets which amounted to USD 6.3 billion. After the acquisition of majority ownership in Alcon, Inc. on August 25, 2010, Alcon contributed in 2010 net sales of USD 2.4 billion and operating income of USD 323 million to the 2010 consolidated income statement.

During 2011, prior to the merger of Alcon, Inc. into Novartis AG on April 8, 4.8% of the non-controlling interests in Alcon, Inc. were acquired for USD 2.4 billion. Completion of the acquisition of the outstanding 18.6% on April 8, 2011 and subsequent merger, resulted in the issuance of Novartis shares with a fair value of USD 9.2 billion and a contingent value payment of USD 0.5 billion.

The final purchase price allocation was completed in 2011 and resulted in a fair value of net identifiable assets of USD 27.0 billion and goodwill of USD 18.0 billion. The excess of the value exchanged for the non-controlling interests in 2011 over the recorded value of the non-controlling interest together with merger related transaction costs resulted in a reduction in equity of USD 5.7 billion.

Pharmaceuticals – Acquisition of Genoptix, Inc.

On March 7, 2011 Novartis completed the acquisition of Genoptix, Inc., a specialized laboratory providing personalized diagnostic services to community-based hematologists and oncologists. Genoptix employed approximately 500 people and became part of the Novartis Molecular Diagnostics unit within the Pharmaceuticals Division.

The acquisition in cash of 100% of the shares of Genoptix totaled USD 458 million, excluding the USD 24 million of cash acquired. The final purchase price allocation resulted in net identified assets of USD 237 million and goodwill of USD 221 million. Results of operations since the acquisition date were not material.

Vaccines and Diagnostics – Acquisition of Zhejiang Tianyuan

On March 22, 2011 Novartis completed the acquisition in cash of an 85% stake in the Chinese vaccines company, Zhejiang Tianyuan Bio-Pharmaceutical Co. Ltd. The acquisition provides Novartis with an expanded presence in the Chinese vaccines market and is expected to facilitate the introduction of additional Novartis vaccines into China. The total amount paid for the 85% interest was USD 194 million, excluding USD 39 million of cash acquired. The final purchase price allocation resulted in net identified assets of USD 131 million and goodwill of USD 82 million. Non-controlling interests have increased by USD 19 million from this transaction. Results of operations since the acquisition date were not material.

Pharmaceuticals – Divestment of *Elidel*®

On May 11, 2011 Novartis completed the divestment of *Elidel*® Cream 1% to Meda Pharma Sarl and Novartis received an upfront payment of USD 420 million and recognized a gain of USD 324 million in "Other Income".

OTHER SIGNIFICANT TRANSACTIONS IN 2010

Pharmaceuticals – Acquisition of Corthera

On February 3, 2010 Novartis completed the 100% acquisition (announced on December 23, 2009) of the privately held US-based Corthera Inc., gaining worldwide rights to relaxin for the treatment of acute decompensated heart failure and assumed full responsibility for development and commercialization for a total purchase consideration of USD 327 million. This amount consists of an initial cash payment of USD 120 million and USD 207 million of deferred contingent consideration. The deferred contingent consideration is the net present value of the additional milestone payments due to Corthera's previous shareholders which they are eligible to receive contingent upon the achievement of specified development and commercialization milestones. The final purchase price allocation resulted in net identified assets of USD 309 million and goodwill of USD 18 million. Results of operations since the acquisition date were not material.

Corporate – Issuance of bond in US dollars

On March 9, 2010 Novartis issued a three-tranche bond totaling USD 5.0 billion registered with the US Securities and Exchange Commission as part of a shelf registration statement filed by Novartis in 2008. A 1.9% three-year tranche totaling USD 2.0 billion, a 2.9% five-year tranche totaling USD 2.0 billion and a 4.4% 10-year tranche totaling USD 1.0 billion were issued by the Group's US entity, Novartis Capital Corp. All tranches are unconditionally guaranteed by Novartis AG.

Corporate – Change of pension plan in Switzerland

On April 23, 2010 the Board of Trustees of the Novartis Swiss Pension Fund agreed to amend the conditions and insured benefits of the current Swiss pension plan with effect from January 1, 2011. These amendments do not have an impact on existing pensions in payment or on plan members born before January 1, 1956. Under the previous rules, benefits from the plan are primarily linked to the level of salary in the years prior to retirement while under the new rules benefits are also partially linked to the level of contributions made by the members during their active service period up to their retirement. This has led to changes in the amounts that need to be included in the Group's consolidated financial statements prepared using IFRS in respect of the Swiss Pension Fund.

As part of this change, Novartis, supported by the Swiss Pension Fund, will make transitional payments, which vary according to the member's age and years of service. As a result, it is estimated that additional payments will be made over a ten-year period of up to approximately USD 481 million (CHF 453 million) depending on whether or not all current members affected by the change remain in the plan over this ten-year period.

2. SIGNIFICANT TRANSACTIONS, BUSINESS COMBINATIONS AND DIVESTMENTS (CONTINUED)

The accounting consequence of this change in the Swiss pension plan rules results in the Group's consolidated financial statements prepared under IFRS reflecting a net pre-tax curtailment gain of USD 265 million (CHF 283 million) in 2010. This calculation only takes into account the discounted value of transition payments of USD 202 million (CHF 219 million) attributed to already completed years of service of the affected plan members as calculated in accordance with IFRS requirements. It does not take into account any amount for transitional payments related to their future years of service.

Sandoz – Acquisition of Oriel Therapeutics

On June 1, 2010 Sandoz completed the 100% acquisition of the privately held US-based Oriel Therapeutics Inc., to broaden its portfolio of projects in the field of respiratory drugs for a total purchase consideration of USD 332 million. This amount consists of an initial cash payment of USD 74 million and USD 258 million of deferred contingent consideration. Oriel's previous shareholders are eligible to receive milestone payments, which are contingent upon the company achieving future development steps, regulatory approvals and market launches, and sales royalties. The total USD 258 million of deferred contingent consideration represents the net present value of expected milestone and royalty payments. The final purchase price allocation, including the valuation of the contingent payment elements of the purchase price, resulted in net identified assets of USD 281 million and goodwill of USD 51 million. Results of operations since the acquisition date were not material. During 2011, USD 106 million of contingent consideration has been released to the consolidated income statement as it is remote that the related contingent event will occur.

Pharmaceuticals – Divestment of *Enablex*®

On October 18, 2010 Novartis finalized the sale of the US rights for *Enablex*® (darifenacin) to Warner Chilcott Plc for USD 400 million and recognized a gain of USD 392 million.

3. SEGMENTATION OF KEY FIGURES 2011 AND 2010

REPORTING SEGMENTS

The businesses of Novartis are divided operationally on a worldwide basis into five reporting segments: Pharmaceuticals, Alcon, Sandoz, Vaccines and Diagnostics and Consumer Health and Corporate activities. Following the full acquisition of Alcon, Inc., on April 8, 2011 a new divisional segment allocation was introduced. As a result, the Alcon Division includes CIBA Vision and certain Pharmaceuticals Division ophthalmology products. Falcon, the US generics business of Alcon, Inc. was transferred to the Sandoz Division. Certain residual operational costs incurred for the Consumer Health Division headquarters were transferred to Corporate and Corporate R&D was transferred to the Pharmaceuticals Division. All segment results for 2010 and 2011 use this new allocation. Except for Consumer Health, these segments reflect the Group's internal management structures. These segments are managed separately, including the two divisions of the Consumer Health segment, because they manufacture, distribute, and sell distinct products which require differing marketing strategies. In the case of Consumer Health, the segment comprises two divisions which are also managed separately, however, neither of these two divisions is material enough to the Group to be disclosed separately as a segment. The reported segments are as follows:

Pharmaceuticals researches, develops, manufactures, distributes and sells patented prescription medicines in the following therapeutic areas: Cardiovascular and Metabolism; Oncology; Neuroscience and Ophthalmics; Respiratory; Integrated Hospital Care; and additional products. Pharmaceuticals is organized into global business franchises responsible for the development and marketing of various products, as well as a business unit, called Novartis Oncology, responsible for the global development and marketing of oncology products. The Novartis Oncology Business Unit is not required to be disclosed separately as a segment since it shares common long-term economic perspectives, customers, research, development, production, distribution and regulatory factors with the rest of the division.

Alcon discovers, develops, manufactures, distributes and sells eye care products. Alcon is the global leader in eye care with product offerings in Surgical, Ophthalmic Pharmaceuticals and Vision Care. In Surgical, Alcon develops, manufactures, distributes and sells ophthalmic surgical equipment, instruments, disposable products and intraocular lenses. In Ophthalmic Pharmaceuticals, Alcon discovers, develops, manufactures, distributes and sells medicines to treat chronic and acute diseases of the eye, as well as over-the-counter medicines for the eye. In Vision Care, Alcon develops, manufactures, distributes and sells contact lenses and lens care products.

Sandoz develops, manufactures, distributes and sells prescription medicines, as well as pharmaceutical and biotechnological active substances, which are not protected by valid and enforceable third-party patents. Sandoz has activities in Retail Generics, Anti-Infectives, Biopharmaceuticals & Oncology Injectables. In Retail Generics, Sandoz develops, manufactures, distributes and markets active ingredients and finished dosage forms of pharmaceuticals, as well as supplying active ingredients to third parties. In Anti-Infectives, Sandoz develops and manufactures, distributes and sells active pharmaceutical ingredients and intermediates – mainly antibiotics – for internal use by Retail Generics and for sale to third-party customers. In Biopharmaceuticals, Sandoz develops, manufactures, distributes and markets protein- or other biotechnology-based products (known as biosimilars or follow-on biologics) and sells biotech manufacturing services to other companies. In Oncology Injectables, Sandoz develops, manufacturers, and markets cytotoxic products for the hospital market.

Vaccines and Diagnostics consists of two activities: Vaccines and Diagnostics. Vaccines researches, develops, manufactures, distributes and sells human vaccines worldwide. Diagnostics researches, develops, distributes and sells blood testing and molecular diagnostics products.

Consumer Health now consists of two divisions: OTC (over-the-counter medicines) and Animal Health. OTC offers readily available consumer medicine. Animal Health provides veterinary products for farm and companion animals.

The following shows an overview of the impact of the restatement on the segmentation structure. Unless otherwise stated this has been used for all years presented in this Annual Report.

Segment	Newly included	Newly excluded
Pharmaceuticals	Corporate R&D	Certain ophthalmic products
Alcon	CIBA Vision, certain ophthalmic products	Falcon
Sandoz	Falcon	
Consumer Health		CIBA Vision; disbanded Consumer Health divisional management costs
Corporate	Disbanded Consumer Health divisional management costs	Corporate R&D

A summary of the above restatements on 2010 net sales and operating income is as follows:

Segment (USD m)	Net sales	Operating income
Pharmaceuticals	– 252	– 327
Alcon	2 020	473
Sandoz	74	49
Consumer Health	– 1 842	– 375
Corporate		180
Total	**0**	**0**

Inter-segmental sales are made at amounts which are considered to approximate arm's length transactions. Where practicable, the same accounting policies are applied by the Group and the segments. Currently, the Executive Committee principally evaluates segmental performance and allocates resources among the segments based on their operating income, cash flow and cash flow return on invested capital (CFROI).

Segment net operating assets consist primarily of property, plant & equipment, intangible assets, inventories and trade and other operating receivables less operating liabilities.

CORPORATE

Income and expenses relating to Corporate include the costs of the Group headquarters and those of corporate coordination functions in major countries. In addition, Corporate includes other items of income and expense which are not attributable to specific segments such as certain expenses related to post-employment benefits, environmental liabilities, charitable activities, donations and sponsorships. Usually, no allocation of Corporate items is made to the segments. Corporate assets and liabilities principally consist of net liquidity (cash and cash equivalents, marketable securities less financial debts), investments in associated companies and current and deferred taxes and non-segmental specific environmental and post-employment benefit liabilities.

3. SEGMENTATION[1] OF KEY FIGURES 2011 AND 2010 (CONTINUED)

	Pharmaceuticals	Alcon
(In USD millions)	2011	2011
Net sales to third parties	32 508	9 958
Sales to other segments	244	22
Net sales of segments	32 752	9 980
Other revenues	453	43
Cost of Goods Sold	– 6 573	– 4 566
Gross profit	26 632	5 457
Marketing & Sales	– 8 929	– 2 537
Research & Development	– 7 232	– 892
General & Administration	– 1 047	– 509
Other income	697	262
Other expense	– 1 825	– 309
Operating income	8 296	1 472
Income from associated companies	– 3	
Interest expense		
Other financial income and expense		
Income before taxes		
Taxes		
Group net income		
Attributable to:		
Shareholders of Novartis AG		
Non-controlling interests		
Included in net income are:		
Interest income		
Depreciation of property, plant & equipment	– 870	– 306
Amortization of intangible assets	– 423	– 1 928
Impairment charges on property, plant & equipment	– 403	– 5
Impairment charges on intangible assets	– 552	– 20
Impairment charges on financial assets	– 30	– 4
Additions to restructuring provisions	– 265	– 74
Equity-based compensation of Novartis and Alcon equity plans	– 648	– 113
Total assets	24 111	46 065
Total liabilities	– 10 415	– 2 273
Total equity	13 696	43 792
Net debt		
Net operating assets	13 696	43 792
Included in total assets and total liabilities are:		
Total property, plant & equipment	8 071	2 056
Additions to property, plant & equipment[3]	1 041	354
Total goodwill and intangible assets	6 244	40 542
Additions to goodwill and intangible assets[3]	219	80
Total investment in associated companies	3	18
Additions to investment in associated companies	5	3
Cash, marketable securities and derivative financial instruments		
Financial debts and derivative financial instruments		
Current income tax and deferred tax liabilities		

[1] All 2010 segment information has been restated to reflect new segment allocation introduced during 2011 as explained in detail on page 159
[2] Consolidated results of Alcon, Inc., only included for the period from acquiring control on August 25, 2010 to December 31, 2010.
[3] Excluding impact of business combinations

Sandoz	Vaccines and Diagnostics	Consumer Health	Corporate (including eliminations)	Total Group	
2011	2011	2011	2011	2011	
9 473	1 996	4 631		58 566	
319	73	15	– 673		
9 792	2 069	4 646	– 673	58 566	
9	295	24	– 15	809	
– 5 445	– 1 410	– 1 735	746	– 18 983	
4 356	954	2 935	58	40 392	
– 1 591	– 363	– 1 674	15	– 15 079	
– 640	– 523	– 296		– 9 583	
– 369	– 150	– 291	– 604	– 2 970	
88	18	91	198	1 354	
– 422	– 185	– 38	– 337	– 3 116	
1 422	– 249	727	– 670	10 998	
4	2		525	528	
				– 751	
				– 2	
				10 773	
				– 1 528	
				9 245	9 969
				9 113	
				132	
				62	
– 303	– 115	– 50	– 84	– 1 728	
– 383	– 231	– 59	– 4	– 3 028	
– 1	– 2	– 2		– 413	
– 25	– 8	– 14		– 619	
	– 135		– 23	– 192	
		– 7		– 346	
– 33	– 38	– 61	– 122	– 1 015	
17 965	5 764	2 684	20 907	117 496	
– 2 742	– 697	– 960	– 34 469	– 51 556	
15 223	5 067	1 724	– 13 562	65 940	
			15 154	15 154	
15 223	5 067	1 724	1 592	81 094	
2 824	1 535	431	710	15 627	
335	192	74	190	2 186	
11 356	2 883	867	20	61 912	
24	6	4	3	336	
18	4		8 579	8 622	
			24	32	
			5 075	5 075	
			20 229	20 229	
			8 467	8 467	

3. SEGMENTATION OF KEY FIGURES 2011 AND 2010 (CONTINUED)

The following countries accounted for more than 5% of at least one of the respective Group totals for the years ended December 31, 2011 and 2010:

Country	Net sales[1]		Total of selected non-current assets[2]	
USD millions	2011	%	2011	%
Switzerland	726	1	38 827	45
United States	19 225	33	30 061	35
Germany	4 362	7	4 214	5
Japan	5 281	9	204	
France	2 848	5	299	
Other	26 124	45	12 556	15
Group	**58 566**	**100**	**86 161**	**100**
Europe	21 507	37	51 101	59
Americas	24 705	42	33 211	39
Asia / Africa / Australasia	12 354	21	1 849	2
Group	**58 566**	**100**	**86 161**	**100**

[1] Net sales from operations by location of third party customer.
[2] Total of property, plant and equipment, goodwill, intangible assets and investment in associated companies

The Group's largest customer accounts for approximately 9% of net sales, and the second and third largest customer account for 7% each of net sales (2010: 8%, 8% and 7% respectively). No other customer accounts for 2% or more of net sales, in both years.

The highest amounts of trade receivables outstanding were for these three customers. They amounted to 10%, 6% and 6%, respectively, of the Group's trade receivables at December 31, 2011 (2010: 9%, 5% and 6% respectively).

PHARMACEUTICALS DIVISION THERAPEUTIC AREA NET SALES

Therapeutic areas

	2011 USD millions	Change USD %
Cardiovascular and Metabolism		
Hypertension medicines		
Diovan	5 665	–6
Exforge	1 209	34
Subtotal Valsartan Group	6 874	–1
Tekturna/Rasilez	557	27
Subtotal Hypertension	**7 431**	**0**
Galvus	677	73
Total strategic franchise products	**8 108**	**4**
Established medicines	1 027	–25
Total Cardiovascular and Metabolism products	**9 135**	**0**
Oncology		
Gleevec/Glivec	4 659	9
Tasigna	716	79
Subtotal Bcr-Abl franchise	5 375	15
Zometa	1 487	–2
Sandostatin	1 443	12
Femara	911	–34
Exjade	850	12
Afinitor	443	82
Other	163	–10
Total Oncology products	**10 672**	**6**
Neuroscience and Ophthalmics		
Lucentis	2 050	34
Exelon/Exelon Patch	1 067	6
Comtan/Stalevo	614	2
Gilenya	494	nm
Extavia	154	24
Other (including *Fanapt*)	159	–16
Total strategic franchise products	**4 538**	**31**
Established medicines	547	–4
Total Neuroscience and Ophthalmics products	**5 085**	**26**

Therapeutic areas

	2011 USD millions	Change USD %
Respiratory		
Xolair	478	30
TOBI	296	6
Onbrez Breezhaler	103	nm
Total strategic franchise products	**877**	**29**
Established medicines	172	–1
Total Respiratory products	**1 049**	**23**
Integrated Hospital Care (IHC)*		
Neoral/Sandimmun	903	4
Myfortic	518	17
Zortress/Certican	187	30
Ilaris	48	85
Other	363	24
Total strategic franchise products	**2 019**	**14**
Established medicines	1 453	–1
Total IHC products	**3 472**	**7**
Additional products		
Voltaren (excl. OTC)	794	0
Ritalin/Focalin	550	19
Tegretol	364	3
Foradil	312	–12
Trileptal	263	4
Everolimus stent drug	256	7
Other	556	4
Total additional products	**3 095**	**4**
Total strategic franchise products	**26 214**	**10**
Total established medicines and additional products	6 294	–4
Total Division net sales	**32 508**	**7**

* includes Transplantation
nm – not meaningful

The product portfolio of other segments is widely spread and none of the products or product ranges exceed 5% of the net sales of the Group in 2011 and 2010.

4. ASSOCIATED COMPANIES

Novartis has the following significant investments in associated companies which are accounted for using the equity method:

	Balance sheet value	Net income statement effect
	2011 USD millions	2011 USD millions
Roche Holding AG, Switzerland	8 362	499
Alcon Inc., Switzerland		
Others	260	29
Total	8 622	528

The results of the Group's associated companies are adjusted to be in accordance with IFRS as applied by Novartis in cases where IFRS is not already used.

Since up-to-date financial data are not available when Novartis produces its consolidated financial results, a survey of analyst estimates is used to estimate the Group's share of net income in Roche Holding. Any differences between these estimates and actual results are adjusted in the Group's 2012 consolidated financial statements when available.

The following table shows summarized financial information of Roche for the year ended December 31, 2010 since 2011 data is not yet available:

	Asset billions	Liabilities billions	Revenue billions	Net income billions
Roche (CHF)	61.0	49.4	49.2	8.9

ROCHE HOLDING AG

The Group's holding in Roche voting shares was 33.3% at December 31, 2011 and 2010. This investment represents approximately 6.3% of Roche's total outstanding voting and non-voting equity instruments. The purchase price allocation was performed on the basis of publicly available information at the time of acquisition.

The December 31, 2011 balance sheet value allocation is as follows:

	USD millions
Novartis share of Roche's estimated net assets	2 828
Novartis share of re-appraised intangible assets	1 882
Implicit Novartis goodwill	3 030
Current value of share in net identifiable assets and goodwill	**7 740**
Accumulated equity accounting adjustments and translation effects less dividends received	622
December 31, 2011 balance sheet value	**8 362**

The identified intangible assets principally relate to the value of currently marketed products and are amortized on a straight-line basis over their estimated average useful life of 20 years.

The income statement effects from applying Novartis accounting principles for this investment in 2011 and 2010 are as follows:

	2011 USD millions
Novartis share of Roche's estimated current-year consolidated net income	702
Prior-year adjustment	– 41
Amortization of fair value adjustments relating to intangible assets, net of taxes of USD 47 million (2010: USD 41 million)	– 162
Net income effect	**499**

The publicly quoted market value of the Novartis interest in Roche (Reuters symbol: RO.S) at December 31, 2011, was USD 9.5 billion

The following table summarizes these value adjustments and currency translation effects attributable to Novartis shareholders:

	Fair value adjustments to marketable securities USD millions	Fair value adjustments of deferred cash flow hedges USD millions	Actuarial losses from defined benefit plans USD millions	Revaluation of previously held equity interests USD millions	Cumulative currency translation effects USD millions	Total value adjustments USD millions
Value adjustments at January 1, 2010						
Fair value adjustments on financial instruments						
Net actuarial losses from defined benefit plans						
Currency translation effects						
Total value adjustments in 2010						
Value adjustments at December 31, 2010						
Fair value adjustments on financial instruments	– 21	41				20
Net actuarial losses from defined benefit plans			– 1 429			– 1 429
Currency translation effects					– 534	– 534
Total value adjustments in 2011	**– 21**	**41**	**– 1 429**		**– 534**	**– 1 943**
Value adjustments at December 31, 2011	**137**	**– 141**	**– 4 667**	**685**	**3 135**	**– 851**

8.1) The 2011 and 2010 changes in the fair value of financial instruments:

	Fair value adjustments to marketable securities USD millions	Fair value adjustments of deferred cash flow hedges USD millions	Total USD millions
Fair value adjustments at January 1, 2011	**157**	**– 182**	**– 25**
Changes in fair value:			
– Available-for-sale marketable securities	– 32		– 32
– Available-for-sale financial investments	– 141		– 141
– Associated companies' movements in comprehensive income	– 8		– 8
Realized net gains transferred to the consolidated income statement:			–
– Marketable securities sold	– 13		– 13
– Other financial assets sold	– 13		– 13
Amortized net losses on cash flow hedges transferred to the consolidated income statement		44	44
Impaired marketable securities and other financial assets transferred to the consolidated income statement	192		192
Deferred tax on above items	– 5	– 3	– 8
Fair value adjustments during the year	**– 20**	**41**	**21**
Attributable to:			
Shareholders of Novartis AG	*– 21*	*41*	*20*
Non-controlling interests	*1*		*1*
Fair value adjustments at December 31, 2011	**137**	**– 141**	**– 4**

8. CHANGES IN CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (CONTINUED)

	Fair value adjustments to marketable securities USD millions	Fair value adjustments of deferred cash flow hedges USD millions	Total USD millions
Fair value adjustments at January 1, 2010	**231**	**– 223**	**8**
Changes in fair value:			
– Available-for-sale marketable securities	19		19
– Available-for-sale financial investments	– 226		– 226
– Associated companies' movements in comprehensive income	– 5		– 5
Realized net gains transferred to the consolidated income statement:			
– Marketable securities sold	– 39		– 39
– Other financial assets sold	– 15		– 15
Amortized net losses on cash flow hedges transferred to the consolidated income statement		44	44
Impaired marketable securities and other financial assets transferred to the consolidated income statement	164		164
Deferred tax on above items	28	– 3	25
Fair value adjustments during the year	**– 74**	**41**	**– 33**
Attributable to:			
Shareholders of Novartis AG	*– 73*	*41*	*– 32*
Non-controlling interests	*– 1*		*– 1*
Fair value adjustments at December 31, 2010	**157**	**– 182**	**– 25**

8.2) Actuarial losses from defined benefit plans arise from:

	2011 USD millions	
Defined benefit pension plans before tax	– 1 876	
Other post-employment benefit plans before tax	– 55	
Taxation on above items	510	
Total after tax	**– 1 421**	
Attributable to:		
Shareholders of Novartis AG	*– 1 429*	*– 678*
Non-controlling interests	*8*	*– 7*

8.3) The Group has investments in associated companies, principally Roche Holding AG. The Group's share in movements in these companies' other comprehensive income are recognized directly in the respective categories of the Novartis consolidated statement of comprehensive income, net of tax. The currency translation effects and fair value adjustments of associated companies are included in the corresponding Group amounts. All other movements in these companies' statements of comprehensive income are recognized directly in the consolidated statement of comprehensive income under "Novartis share of other items recorded in comprehensive income recognized by associated companies, net of taxes". These amounted to income of USD 1 million (2010: loss of USD 94 million. The loss includes a gain of USD 43 million arising from the recycling to the consolidated income statement the net losses accumulated in the consolidated statement of comprehensive income during the time Alcon, Inc. was accounted for as an associated company from July 2008 to August 2010).

9. CHANGES IN CONSOLIDATED EQUITY

9.1) At the 2011 Annual General meeting, a dividend of CHF 2.20 per share was approved that amounted to USD 5.4 billion, and was paid in 2011 (2010: CHF 2.10 per share dividend payment that amounted to USD 4.5 billion). The amount available for distribution as a dividend to shareholders is based on the available distributable retained earnings of Novartis AG determined in accordance with the legal provisions of the Swiss Code of Obligation.

9.2) In 2011 a total of 54.7 million shares net were purchased for USD 3.5 billion (2010: sale of 8.4 million for USD 342 million), out of which 39.4 million shares were acquired under the share repurchase program.

9.3) Equity-settled share-based compensation is expensed in the consolidated income statement in accordance with the vesting or service period of the share-based compensation plans. In 2011 7.2 million shares (2010: 6.7 million shares) were transferred to associates as part of equity-based compensation. The value for the shares and options expensed in 2011, including associated tax, amounted to USD 806 million (2010: USD 599 million) and is credited to consolidated equity.

9.4) In 2010 a reduction in consolidated equity attributable to Novartis of USD 74 million arose from a dilution of the Novartis interest in Alcon, Inc. since obtaining majority control on August 25, 2010. This was due to an increase in Alcon's outstanding shares, principally due to the issuance of new shares and the use of Alcon treasury shares to satisfy conversion of Alcon's equity-based instruments held by associates.

9.5) As required by IAS 27 the excess of the consideration exchanged by Novartis to acquire the additional non-controlling interests in Alcon, Inc. over the value of the related outstanding non-controlling interests of Alcon, Inc. is recognized against consolidated equity. In 2011 this led to a USD 5.7 billion reduction in equity (2010: USD 96 million, mainly due to the acquisition of additional shares in Alcon, Inc.). Also deducted are USD 59 million of merger related transaction costs.

9.6) Changes in non-controlling interests are mainly due to the acquisition of the remaining non-controlling interests in Alcon, Inc. leading to a reduction of USD 6.6 billion (2010: increase of USD 6.3 billion due to full consolidation of Alcon, Inc. from August 25, 2010).

9.7) A total of 164.7 million Novartis shares with a fair value of USD 9.2 billion were exchanged on April 8, 2011 to obtain the outstanding non-controlling interest in Alcon, Inc. These shares consisted of 108 million newly issued shares and 56.7 million treasury shares.

10. PROPERTY, PLANT & EQUIPMENT MOVEMENTS

	Land USD millions	Buildings USD millions	Construction in progress USD millions	Machinery & other equipment USD millions	Total USD millions
2011					
Cost					
January 1	**827**	**10 674**	**2 327**	**15 129**	**28 957**
Acquisition and divestment of consolidated business	12	20		9	41
Reclassifications[1]		888	– 1 688	800	
Additions	2	105	1 616	463	2 186
Disposals and derecognitions[2]	– 3	– 148	– 21	– 638	– 810
Currency translation effects	– 7	– 110	– 70	– 252	– 439
December 31	**831**	**11 429**	**2 164**	**15 511**	**29 935**
Accumulated depreciation					
January 1	**– 19**	**– 4 318**	**– 6**	**– 8 774**	**– 13 117**
Depreciation on divested consolidated business		3		6	9
Reclassifications[1]		– 3		3	
Depreciation charge	– 3	– 438		– 1 287	– 1 728
Depreciation on disposals and derecognitions[2]		117		575	692
Impairment charge		– 55	– 4	– 354	– 413
Currency translation effects		48		201	249
December 31	**– 22**	**– 4 646**	**– 10**	**– 9 630**	**– 14 308**
Net book value at December 31	**809**	**6 783**	**2 154**	**5 881**	**15 627**
Insured value at December 31					**34 483**
Net book value of property, plant & equipment under finance lease contracts					**4**
Commitments for purchases of property, plant & equipment					**583**

[1] Reclassifications between various asset categories due to completion of plant and other equipment under construction.
[2] Derecognition of tangible assets which are no longer used and are not considered to have a significant disposal value or other alternative use.

The Group was awarded government grants in the United States for the construction of a manufacturing facility to produce flu vaccines. The contracts included a maximum of USD 294 million cost reimbursement for construction activities and equipment, of which USD 223 million was received by December 31, 2011 (2010: USD 185 million). These grants were deducted in arriving at the carrying value of the assets since the receipt of the respective government grant is reasonably assured. There are no onerous contracts or unfulfilled conditions in connection with this grant.

Borrowing costs on new additions to property, plant and equipment have been capitalized and amounted to USD 1 million in 2011 (2010: USD 1 million).

The impairment charge for property, plant and equipment in 2011 amounted to USD 413 million (2010: USD 10 million).

2010

Cost

January 1

Impact of business combinations

Reclassifications [1]

Additions

Disposals and derecognitions [2]

Currency translation effects

December 31

Accumulated depreciation

January 1

Reclassifications [1]

Depreciation charge

Depreciation on disposals and derecognitions [2]

Impairment charge

Currency translation effects

December 31

Net book value at December 31

Insured value at December 31

Net book value of property, plant & equipment under finance lease contracts

Commitments for purchases of property, plant & equipment

[1] Reclassifications between various asset categories due to completion of plant and other equipment under construction.
[2] Derecognition of tangible assets which are no longer used and are not considered to have a significant disposal value or other alternative use.

11. GOODWILL AND INTANGIBLE ASSET MOVEMENTS

	Goodwill USD millions	Acquired research & development USD millions	Alcon brand name USD millions	Technologies USD millions	Currently marketed products USD millions	Marketing know-how USD millions	Other intangible assets USD millions	Total of intangible assets other than goodwill USD millions
2011								
Cost								
January 1	**30 261**	**4 627**	**2 980**	**6 699**	**22 740**	**5 960**	**1 135**	**44 141**
Impact of business combinations	303	7		3	101		1	112
Reclassifications[1]		– 255			260		– 5	
Additions[2]	69	122			43		102	267
Disposals and derecognitions[3]	– 48	– 1 420			– 19		– 4	– 1 443
Currency translation effects	– 134	10		– 21	– 85		– 7	– 103
December 31	**30 451**	**3 091**	**2 980**	**6 681**	**23 040**	**5 960**	**1 222**	**42 974**
Accumulated amortization								
January 1	**– 569**	**– 1 565**		**– 370**	**– 6 254**		**– 721**	**– 8 910**
Amortization charge				– 589	– 2 090	– 238	– 111	– 3 028
Amortization on disposals and derecognitions[3]	48	1 420			19		4	1 443
Impairment charge		– 338			– 287		– 2	– 627
Reversal of impairment charge					8			8
Currency translation effects	13	22		9	69		9	109
December 31	**– 508**	**– 461**		**– 950**	**– 8 535**	**– 238**	**– 821**	**– 11 005**
Net book value at December 31	**29 943**	**2 630**	**2 980**	**5 731**	**14 505**	**5 722**	**401**	**31 969**

[1] Reclassifications between various asset categories as a result of product launches of acquired In-Process Research & Development.
[2] Additions to goodwill relates to finalization of Alcon, Inc., acquisition accounting
[3] Derecognitions of intangible assets which are no longer used or being developed and are not considered to have a significant disposal value or other alternative use.

2010

Cost

January 1

Impact of business combinations

Reclassifications [1]

Additions

Disposals and derecognitions [2]

Currency translation effects

December 31

Accumulated amortization

January 1

Reclassifications [1]

Amortization charge

Amortization on disposals and derecognitions [2]

Impairment charge

Reversal of impairment charge

Currency translation effects

December 31

Net book value at December 31

[1] Reclassifications between various asset categories as a result of product launches of acquired In-Process Research & Development.

[2] Derecognitions of intangible assets which are no longer used or being developed and are not considered to have a significant disposal value or other alternative use.

SEGMENTATION OF GOODWILL AND INTANGIBLE ASSETS

The net book values at December 31, 2011 of goodwill and intangible assets are allocated to the Group's segments as summarized below:

	Goodwill USD millions	Acquired research & development USD millions	Alcon brand name USD millions	Technologies USD millions	Currently marketed products USD millions	Marketing know-how USD millions	Other intangible assets USD millions	Total of intangible assets other than goodwill USD millions
Pharmaceuticals	3 077	1 309		2	1 639		217	3 167
Alcon	17 740	598	2 980	4 836	8 639	5 722	27	22 802
Sandoz	7 697	592		678	2 378		11	3 659
Vaccines and Diagnostics	1 197	128		215	1 210		133	1 686
Consumer Health	226				639		2	641
Corporate	6	3					11	14
Total	**29 943**	**2 630**	**2 980**	**5 731**	**14 505**	**5 722**	**401**	**31 969**
Potential impairment charge, if any, if discounted cash flows fell by 5%		3			5			
Potential impairment charge, if any, if discounted cash flows fell by 10%		7			21			

11. GOODWILL AND INTANGIBLE ASSET MOVEMENTS (CONTINUED)

The recoverable amount of a cash-generating unit and related goodwill is based on the higher of "fair value less costs to sell" or "value in use". The following assumptions are used in the calculations:

	Pharmaceuticals %	Alcon %	Sandoz %	Vaccines and Diagnostics %	Consumer Health %
Sales growth rate assumptions after forecast period	0.4	3	0 to 2	0.5	0 to 2
Discount rate (post-tax)	7	7	7	7	7

In 2011, intangible asset impairment charges of USD 627 million were recorded. USD 552 million of these arose in the Pharmaceuticals Division, principally due to the expected reduction in demand for *Tekturna/Rasilez* (aliskiren) and discontinuation of PRT128 (elinogrel), SMC021 (oral calcitonin), PTK796 and AGO178 (agomelatine) development programs. USD 75 million of impairment charges arose in all other Divisions.

In 2010, Novartis recorded impairment charges totaling USD 1.0 billion. These relate to impairment charges of USD 356 million for *Mycograb*, USD 250 million for PTZ601, USD 228 million for albinterferon alfa-2b and USD 120 million for ASA404 as Novartis decided to discontinue the related development projects. Additionally, USD 40 million were recorded for various other impairment charges in the Pharmaceuticals Division. Novartis also recorded various impairment charges of USD 24 million in Sandoz and Consumer Health.

Reversal of prior year impairment charges amounted to USD 8 million (2010: USD 107 million).

12. DEFERRED TAX ASSETS AND LIABILITIES

	Property, plant & equipment USD millions	Intangible assets USD millions	Pensions and other benefit obligations of associates USD millions	Inventories USD millions	Tax loss carryforwards USD millions	Other assets, provisions and accruals USD millions	Valuation allowance USD millions	Total USD millions
Gross deferred tax assets at January 1, 2011	**131**	**251**	**1 086**	**1 792**	**241**	**2 007**	**– 19**	**5 489**
Gross deferred tax liabilities at January 1, 2011	**– 951**	**– 5 689**	**– 409**	**– 253**	**– 10**	**– 626**		**– 7 938**
Net deferred tax balance at January 1, 2011	**– 820**	**– 5 438**	**677**	**1 539**	**231**	**1 381**	**– 19**	**– 2 449**
At January 1, 2011	**– 820**	**– 5 438**	**677**	**1 539**	**231**	**1 381**	**– 19**	**– 2 449**
(Charged)/credited to income	68	350	28	418	– 28	322	– 16	1 142
(Charged)/credited to equity						22		22
(Charged)/credited to comprehensive income			510			– 32		478
Impact of business combinations						– 9		– 9
Other movements	– 38	154	– 12	– 162	– 15	– 18	3	– 88
Net deferred tax balance at December 31, 2011	**– 790**	**– 4 934**	**1 203**	**1 795**	**188**	**1 666**	**– 32**	**– 904**
Gross deferred tax assets at December 31, 2011	**157**	**234**	**1 576**	**2 020**	**201**	**2 221**	**– 32**	**6 377**
Gross deferred tax liabilities at December 31, 2011	**– 947**	**– 5 168**	**– 373**	**– 225**	**– 13**	**– 555**		**– 7 281**
Net deferred tax balance at December 31, 2011	**– 790**	**– 4 934**	**1 203**	**1 795**	**188**	**1 666**	**– 32**	**– 904**
Deferred tax assets and liabilities after offsetting amounts of USD 520 millions recorded in companies within the same tax jurisdiction								
Deferred tax assets at December 31, 2011								**5 857**
Deferred tax liabilities at December 31, 2011								**– 6 761**
Net deferred tax balance at December 31, 2011								**– 904**

Gross deferred tax assets at January 1, 2010	
Gross deferred tax liabilities at January 1, 2010	
Net deferred tax balance at January 1, 2010	
At January 1, 2010	
(Charged)/credited to income	
(Charged)/credited to equity	
(Charged)/credited to comprehensive income	
Impact of business combinations	
Other movements	
Net deferred tax balance at December 31, 2010	
Gross deferred tax assets at December 31, 2010	
Gross deferred tax liabilities at December 31, 2010	
Net deferred tax balance at December 31, 2010	
Deferred tax assets and liabilities after offsetting amounts of USD 249 millions recorded in companies within the same tax jurisdiction	
Deferred tax assets at December 31, 2010	**5 240**
Deferred tax liabilities at December 31, 2010	**– 7 689**
Net deferred tax balance at December 31, 2010	**– 2 449**

12. DEFERRED TAX ASSETS AND LIABILITIES (CONTINUED)

A reversal of valuation allowance could occur when circumstances make the realization of deferred taxes probable. This would result in a decrease in the Group's effective tax rate.

Deferred tax assets of USD 2.3 billion (2010: USD 2.3 billion) and deferred tax liabilities of USD 6.5 billion (2010: USD 7.1 billion) are expected to have an impact on current taxes payable after more than twelve months.

At December 31, 2011, unremitted earnings of USD 51 billion (2010: USD 45 billion) have been retained by subsidiary companies for reinvestment. No provision is made for income taxes that would be payable upon the distribution of these earnings. If these earnings were remitted, an income tax charge could result based on the tax statutes currently in effect.

	2011 USD millions
Temporary differences on which no deferred tax has been provided as they are permanent in nature related to:	
– Investments in subsidiaries	4 782
– Goodwill from acquisitions	– 25 089

The gross value of tax-loss carry-forwards that have, or have not, been capitalized as deferred tax assets, with their expiry dates is as follows:

	Not capitalized USD millions	Capitalized USD millions	2011 total USD millions
One year	81	2	83
Two years	171	4	175
Three years	175	38	213
Four years	72	29	101
Five years	63	100	163
More than five years	419	443	862
Total	**981**	**616**	**1 597**

One year	
Two years	
Three years	
Four years	
Five years	
More than five years	
Total	

Deferred tax assets related to taxable losses of relevant Group entities are recognized to the extent it is considered probable that future taxable profits will be available against which such losses can be utilized in the foreseeable future.

In 2011, USD 155 million (2010: USD 11 million) of tax-loss carry-forwards expired.

13. FINANCIAL ASSETS

	2011 USD millions
Financial investments, long-term loans and other investments	938
Loans to associated companies	
Prepaid post-employment benefit plans	38
Total financial assets	**976**

Available-for-sale financial investments at December 31, 2011, totaling USD 604 million (2010: USD 712 million) are valued at fair value, while long-term loans and other investments of USD 334 million (2010: USD 145 million) are valued at amortized cost or at cost.

In 2011, impairments on available-for-sale financial investments amounted to USD 189 million (2010: USD 160 million). In 2011 no reversal of impairments occurred (2010: USD 2 million). These amounts were recorded in the consolidated income statement under “Other expense” or “Other income”, respectively.

14. INVENTORIES

	2011 USD millions
Raw material, consumables	930
Finished products	5 000
Total inventories	**5 930**

The following summarizes movements in inventory write-downs deducted from inventory categories. Reversals of inventory provisions mainly result from the reassessment of inventory values manufactured prior to regulatory approval but for which approval was subsequently received:

	2011 USD millions
January 1	**– 879**
Impact of business combinations	
Inventory write-downs charged to the consolidated income statement	– 1 554
Utilization of inventory provisions	921
Reversal of inventory provisions	738
Currency translation effects	33
December 31	**– 741**

15. TRADE RECEIVABLES

	2011 USD millions
Total gross trade receivables	10 542
Provisions for doubtful trade receivables	– 219
Total trade receivables, net	**10 323**

The following table summarizes the movement in the provision for doubtful trade receivables:

	2011 USD millions
January 1	**– 221**
Impact of business combinations	– 9
Provisions for doubtful trade receivables charged to the consolidated income statement	– 116
Utilization or reversal of provisions for doubtful trade receivables	121
Currency translation effects	6
December 31	**– 219**

The following sets forth details of the age of trade receivables that are not overdue as specified in the payment terms and conditions established with Novartis customers as well as an analysis of overdue amounts and related provisions for doubtful trade receivables:

	2011 USD millions
Not overdue	8 967
Past due for not more than one month	498
Past due for more than one month but less than three months	295
Past due for more than three months but less than six months	249
Past due for more than six months but less than one year	228
Past due for more than one year	305
Provisions for doubtful trade receivables	– 219
Total trade receivables, net	**10 323**

Provisions for doubtful trade receivables are established based upon the difference between the receivable value and the estimated net collectible amount. Novartis establishes provisions for doubtful trade receivables based on historical loss experience. Significant financial difficulties of a customer, such as probability of bankruptcy or financial reorganization or default/delinquency in payments are considered indicators that recovery of trade receivables are doubtful.

Trade receivable balances include sales to government-supported healthcare systems. Novartis continues to monitor sovereign debt issues and economic conditions in Greece, Italy, Spain, Portugal and other countries in Europe and evaluates accounts receivable in these countries for potential collection risks. Deteriorating credit and economic conditions and other factors in these countries have resulted in, and may continue to result in an increase in the average length of time that it takes to collect these accounts receivable and may require Novartis to re-evaluate the collectability of these receivables in future periods.

Novartis does not expect to write off trade receivable amounts that are not past due nor unprovided for. The Group holds security amounting to USD 36 million as collateral for certain trade receivables.

Trade receivables include amounts denominated in the following major currencies:

Currency	2011 USD millions
CHF	288
EUR	2 636
GBP	139
JPY	1 929
USD	2 865
Other	2 466
Total trade receivables, net	**10 323**

During 2011, Novartis entered into several significant irrevocable factoring arrangements. As a result USD 538 million of trade receivables have been sold and derecognized.

16. CASH, MARKETABLE SECURITIES AND DERIVATIVE FINANCIAL INSTRUMENTS

The following tables show the contract or underlying principal amounts and fair values of derivative financial instruments analyzed by type of contract at December 31, 2011 and 2010. Contract or underlying principal amounts indicate the volume of business outstanding at the consolidated balance sheet date and do not represent amounts at risk. The fair values are determined by reference to market prices or standard pricing models that used observable market inputs at December 31, 2011 and 2010.

DERIVATIVE FINANCIAL INSTRUMENTS

	Contract or underlying principal amount	Positive fair values	Negative fair values
	2011 USD millions	2011 USD millions	2011 USD millions
Currency related instruments			
Forward foreign exchange rate contracts	6 456	105	– 12
Over-the-Counter currency options	2 102	13	– 18
Total of currency related instruments	8 558	118	– 30
Interest rate related instruments			
Interest rate swaps			
Total of interest rate related instruments			
Total derivative financial instruments included in marketable securities and in current financial debts	8 558	118	– 30

The following table shows by currency contract or underlying principal amount the derivative financial instruments at December 31, 2011 and 2010:

December 31, 2011	EUR USD millions	USD USD millions	JPY USD millions	Other USD millions	Total USD millions
Currency related instruments					
Forward foreign exchange rate contracts	3 706	1 746	255	749	6 456
Over-the-Counter currency options		2 000		102	2 102
Total of currency related instruments	**3 706**	**3 746**	**255**	**851**	**8 558**
Total derivative financial instruments	**3 706**	**3 746**	**255**	**851**	**8 558**

Currency related instruments
Forward foreign exchange rate contracts
Over-the-Counter currency options
Total of currency related instruments
Interest rate related instruments
Interest rate swaps
Total of interest rate related instruments
Total derivative financial instruments

DERIVATIVE FINANCIAL INSTRUMENTS EFFECTIVE FOR HEDGE ACCOUNTING PURPOSES

At the end of 2011 and 2010 there were no open hedging instruments for anticipated transactions.

MARKETABLE SECURITIES, TIME DEPOSITS AND DERIVATIVE FINANCIAL INSTRUMENTS

	2011 USD millions
Available-for-sale marketable securities	
Debt securities	1 131
Equity securities	73
Fund investments	32
Total available-for-sale marketable securities	1 236
Derivative financial instruments	118
Accrued interest on debt securities	12
Total marketable securities, time deposits and derivative financial instruments	1 366

Debt securities and time deposits are denominated in USD except for debt securities of USD 694 million in CHF (2010: USD 580 million) and USD 26 million in EUR (2010: USD 176 million) respectively.

FAIR VALUE BY HIERARCHY

As required by IFRS, financial assets and liabilities recorded at fair value in the consolidated financial statements are categorized based upon the level of judgment associated with the inputs used to measure their fair value. The IFRS hierarchical levels, based on an increasing amount of subjectivity associated with the inputs to derive fair valuation for these assets and liabilities, are as follows:

Level 1 – Inputs are unadjusted and use quoted prices in active markets for identical assets or liabilities at the measurement date.

The types of assets carried at level 1 fair value are equity and debt securities listed in active markets.

Level 2 – Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly. These inputs are derived principally from, or corroborated by, observable market data by correlation or other means at the measurement date and for the duration of the instruments' anticipated life.

The assets generally included in this fair value hierarchy are time deposits, foreign exchange and interest rate derivatives and certain investment funds. Foreign exchange derivatives and interest rate derivatives are valued using corroborated market data. The liabilities generally included in this fair value hierarchy consist of foreign exchange derivatives and options on equity securities.

Level 3 – Inputs that are unobservable for the asset or liability. These inputs reflect the Group's best estimate of what market participants would use in pricing the asset or liability at the measurement date. Consideration is given to the risk inherent in the valuation techniques and the risk inherent in the inputs to the models.

The assets generally included in this fair value hierarchy are various investments in hedge funds and unquoted equity security investments of the Novartis Venture Funds investment activities. There were no liabilities carried at fair value in this category.

2011	Level 1 USD millions	Level 2 USD millions	Level 3 USD millions	Valued at amortized cost USD millions	Total USD millions
Available-for-sale marketable securities					
Debt securities	1 103	28			1 131
Equity securities	53		20		73
Fund investments			32		32
Total available-for-sale marketable securities	**1 156**	**28**	**52**		**1 236**
Derivative financial instruments		118			118
Accrued interest on debt securities				12	12
Total marketable securities, time deposits and derivative financial instruments	**1 156**	**146**	**52**	**12**	**1 366**
Financial investments and long-term loans					
Available-for-sale financial investments	261		331		592
Fund investments			12		12
Long-term loans and receivables, advances, security deposits				334	334
Total financial investments and long-term loans	**261**		**343**	**334**	**938**
Financial liabilities					
Derivative financial instruments		– 30			– 30
Total financial liabilities at fair value		**– 30**			**– 30**

Available-for-sale marketable securities					
Debt securities					
Equity securities					
Fund investments					
Total available-for-sale marketable securities					
Derivative financial instruments					
Accrued interest on debt securities				16	16
Total marketable securities, time deposits and derivative financial instruments	**1 371**	**1 353**	**75**	**16**	**2 815**
Financial investments and long-term loans					
Available-for-sale financial investments					
Fund investments					
Loans to associated companies					
Long-term loans and receivables, advances, security deposits					
Total financial investments and long-term loans					
Financial liabilities					
Derivative financial instruments					
Total financial liabilities at fair value					

The analysis above includes all financial instruments including those measured at amortized cost or at cost.

16. CASH, MARKETABLE SECURITIES AND DERIVATIVE FINANCIAL INSTRUMENTS (CONTINUED)

The change in carrying values associated with level 3 financial instruments using significant unobservable inputs during the year ended December 31 are set forth below:

2011	Equity securities USD millions	Fund investments USD millions	Available-for-sale financial investments USD millions	Total USD millions
January 1	**20**	**67**	**348**	**435**
Gains recognized in the consolidated income statement		1	23	24
Impairments and amortizations		– 3	– 24	– 27
Gains (losses) recognized in the consolidated statement of comprehensive income	1	2	– 7	– 4
Purchases			74	74
Redemptions		– 24		– 24
Proceeds from sales	– 1		– 82	– 83
Currency translation effects		1	– 1	
December 31	**20**	**44**	**331**	**395**
Total of gains and impairments, net recognized in the consolidated income statement for assets held at December 31, 2011		– 2	– 1	– 3

January 1
Impact of business combinations
Gains recognized in the consolidated income statement
Impairments and amortizations
Losses recognized in the consolidated statement of comprehensive income
Purchases
Redemptions
Proceeds on sales
Currency translation effects
December 31

Total of gains and impairments, net recognized in the consolidated income statement for assets held at December 31, 2010

If the pricing parameters for the level 3 input were to change for equity securities and fund investments by 5% and for available-for-sale financial investments by 10% positively or negatively, respectively, this would change the amounts recorded in the consolidated statement of comprehensive income by USD 3 million or USD 33 million, respectively (2010: USD 4 million and USD 35 million).

MARKET RISK

Novartis is exposed to market risk, primarily related to foreign currency exchange rates, interest rates and the market value of the investments of liquid funds. The Group actively monitors these exposures. To manage the volatility relating to these exposures, the Group enters into a variety of derivative financial instruments. The Group's objective is to reduce, where it deems appropriate to do so, fluctuations in earnings and cash flows associated with changes in interest rates, foreign currency exchange rates and market rates of investments of liquid funds and of the currency exposure of certain net investments in foreign subsidiaries. It is the Group's policy and practice to use derivative financial instruments to manage exposures and to enhance the yield on the investment of liquid funds. It does not enter any financial transactions containing a risk that cannot be quantified at the time the transaction is concluded. In addition, it does not sell short assets it does not have, or does not know it will have, in the future. The Group only sells existing assets or enters into transactions and future transactions (in the case of anticipatory hedges) that it confidently expects it will have in the future, based on past experience. In the case of liquid funds, the Group writes call options on assets it has or it writes put options on positions it wants to acquire and has the liquidity to acquire. The Group expects that any loss in value for these instruments generally would be offset by increases in the value of the underlying transactions.

FOREIGN CURRENCY EXCHANGE RATE RISK

The Group uses the USD as its reporting currency. As a result, the Group is exposed to foreign currency exchange movements, primarily in European, Japanese and other Asian and Latin American currencies. Consequently, it enters into various contracts that reflect the changes in the value of foreign currency exchange rates to preserve the value of assets, commitments and anticipated transactions. Novartis also uses forward contracts and foreign currency option contracts to hedge certain anticipated net revenues in foreign currencies.

Net investments in subsidiaries in foreign countries are long-term investments. Their fair value changes through movements of foreign currency exchange rates. In the very long term, however, the difference in the inflation rate should match the foreign currency exchange rate movement, so that the market value of the foreign non-monetary assets will compensate for the change due to foreign currency movements. For this reason, the Group only hedges the net investments in foreign subsidiaries in exceptional cases.

COMMODITY PRICE RISK

The Group has only a very limited exposure to price risk related to anticipated purchases of certain commodities used as raw materials by the Group's businesses. A change in those prices may alter the gross margin of a specific business, but generally by not more than 10% of the margin and thus below the Group's risk management tolerance levels. Accordingly, the Group does not enter into significant commodity futures, forward and option contracts to manage fluctuations in prices of anticipated purchases.

INTEREST RATE RISK

The Group addresses its net exposure to interest rate risk mainly through the ratio of its fixed rate financial debt to variable rate financial debt contained in its total financial debt portfolio. To manage this mix, Novartis may enter into interest rate swap agreements, in which it exchanges periodic payments based on a notional amount and agreed upon fixed and variable interest rates.

EQUITY RISK

The Group purchases equities as investments of its liquid funds. As a policy, it limits its holdings in an unrelated company to less than 5% of its liquid funds. Potential investments are thoroughly analyzed in respect to their past financial track record (mainly cash flow and return on investment), their market potential, their management and their competitors. Call options are written on equities that the Group owns, and put options are written on equities which the Group wants to buy and for which cash has been reserved.

CREDIT RISK

Current assets

Marketable securities

Derivative financial instruments and accrued interest on derivative financial instruments

Cash and cash equivalents

Total current assets

Non-current liabilities

Financial debts

Total non-current liabilities

Current liabilities

Financial debts

Derivative financial instruments

Total current liabilities

Net debt

The consolidated balance sheet amounts of financial liabilities included in the above analysis are not materially different to the contractual amounts due on maturity. The positive and negative fair values on derivative financial instruments represent the net contractual amounts to be exchanged at maturity.

Cash and cash equivalents at December 31, 2011 totaled USD 3.7 billion (2010: USD 5.3 billion) and include current accounts of USD 1.9 billion (2010: USD 2.0 billion) and deposits and short-term investments with an initial maturity of less than three months and Euro-commercial papers of USD 1.8 billion (2010: USD 3.3 billion). This amount contains USD 74 million (2010: nil) which covers a guarantee and so it is restricted in use.

The Group's contractual undiscounted potential cash flows from derivative financial instruments to be settled on a gross basis are as follows:

December 31, 2011	Due or due within one month USD millions	Due later than one month but less than three months USD millions	Due later than three months but less than one year USD millions	Due later than one year but less than five years USD millions	Total USD millions
Derivative financial instruments and accrued interest on derivative financial instruments					
Potential outflows in various currencies	– 4 315	– 738	– 1 208		– 6 261
Potential inflows in various currencies	4 366	738	1 241		6 345

Derivative financial instruments and accrued interest on derivative financial instruments

Potential outflows in various currencies

Potential inflows in various currencies

Other contractual liabilities, which are not part of management's monitoring of the net debt or liquidity consist of the following items:

December 31, 2011	Due or due within one month USD millions	Due later than one month but less than three months USD millions	Due later than three months but less than one year USD millions	Due later than one year but less than five years USD millions	Due after five years USD millions	Total USD millions
Contractual interest on non-current liabilities		– 236	– 247	– 1 410	– 637	– 2 530
Trade payables		– 4 989				– 4 989

Contractual interest on non-current liabilities

Trade payables

CAPITAL RISK MANAGEMENT

Novartis strives to maintain strong debt ratings. In managing its capital, Novartis focuses on a sound debt/equity ratio. Credit agencies in 2011 maintained their ratings for Novartis. Moody's rated the Group as Aa2 for long-term maturities and P-1 for short-term maturities and Standard & Poor's had a rating of AA- for long-term and A-1+ for short-term maturities. Fitch had a long-term rating of AA and a short-term rating of F1+.

The 2011 year-end debt/equity ratio decreased to 0.31:1 from 0.33:1 in 2010 principally due to less current financial debt being outstanding under the commercial paper program.

VALUE AT RISK

The Group uses a value at risk (VAR) computation to estimate the potential ten-day loss in the fair value of its financial instruments.

A 10-day period is used because of an assumption that not all positions could be undone in one day given the size of the positions. The VAR computation includes the Group's financial debt, short-term and long-term investments, foreign currency forwards, swaps and options as well as anticipated transactions. Foreign currency trade payables and receivables as well as net investments in foreign subsidiaries are included in the computation.

The VAR estimates are made assuming normal market conditions, using a 95% confidence interval. The Group uses a "Delta Normal" model to determine the observed inter-relationships between movements in interest rates, stock markets and various currencies. These inter-relationships are determined by observing interest rate, stock market movements and forward foreign currency rate movements over a 60 day period for the calculation of VAR amounts.

The estimated potential 10-day loss in pre-tax income from the Group's foreign currency instruments, the estimated potential 10-day loss of its equity holdings, and the estimated potential 10-day loss in fair value of its interest rate sensitive instruments (primarily financial debt and investments of liquid funds under normal market conditions) as calculated in the VAR model are the following:

	Dec 31, 2011 USD millions
All financial instruments	235
Analyzed by components:	
Instruments sensitive to foreign currency exchange rates	145
Instruments sensitive to equity market movements	56
Instruments sensitive to interest rates	102

The average, high, and low VAR amounts are as follows:

2011	Average USD millions	High USD millions	Low USD millions
All financial instruments	214	281	180
Analyzed by components:			
Instruments sensitive to foreign currency exchange rates	98	219	50
Instruments sensitive to equity market movements	49	74	28
Instruments sensitive to interest rates	154	190	96

All financial instruments

Analyzed by components:

Instruments sensitive to foreign currency exchange rates

Instruments sensitive to equity market movements

Instruments sensitive to interest rates

The VAR computation is a risk analysis tool designed to statistically estimate the maximum potential ten day loss from adverse movements in foreign currency exchange rates, equity prices and interest rates under normal market conditions. The computation does not purport to represent actual losses in fair value on earnings to be incurred by the Group, nor does it consider the effect of favorable changes in market rates. The Group cannot predict actual future movements in such market rates and it does not claim that these VAR results are indicative of future movements in such market rates or to be representative of any actual impact that future changes in market rates may have on the Group's future results of operations or financial position.

In addition to these VAR analyses, the Group uses stress testing techniques that aim to reflect a worst case scenario on the financial assets monitored by Group Treasury. For these calculations, the Group uses the worst movements during a period of six months over the past 20 years in each category. For 2011 and 2010, the worst case loss scenario was configured as follows:

	Dec 31, 2011 USD millions
All financial instruments	406
Analyzed by components:	
Instruments sensitive to foreign currency exchange rates	328
Instruments sensitive to equity market movements	31
Instruments sensitive to interest rates	47

In the Group's risk analysis, Novartis considered this worst case scenario acceptable as it could reduce income, but would not endanger the solvency or the investment grade credit standing of the Group. While it is highly unlikely that all worst case fluctuations would happen simultaneously, as shown in the model, the actual market can of course produce bigger movements in the future than it has historically. Additionally, in such a worst case environment, management actions could further mitigate the Group's exposure.

17. OTHER CURRENT ASSETS

	2011 USD millions
Withholding tax recoverable	173
Prepaid expenses	
– Third parties	694
– Associated companies	12
Other receivables	
– Third parties	1 864
– Associated companies	13
Total other current assets	**2 756**

18. DETAILS OF SHARES AND SHARE CAPITAL MOVEMENTS

	Number of shares[1]	
	Movement in year	Dec 31, 2011
Total Novartis shares	108 000 000	2 745 623 000
Total treasury shares	9 248 679	– 338 929 143
Total outstanding shares	**117 248 679**	**2 406 693 857**
	USD millions	**USD millions**
Share capital	59	1 016
Treasury shares	4	– 121
Outstanding share capital	**63**	**895**

[1] All shares are registered, authorized, issued and fully paid. All are voting shares and, except for 146 273 240 treasury shares at December 31, 2011 (2010: 159 381 837) are dividend bearing.

In 2011 an amount of 54.7 million shares net were purchased (2010: sales of 8.4 million shares). Out of these, 39.4 million shares (2010: nil) were acquired under the 2nd line buy-back program with the intention of cancellation, 20.4 million shares (2010: 0.4 million shares) were purchased on the 1st trading line on the Swiss stock exchange with the intention of retaining in Group Treasury and 5.1 million shares (2010: 8.8 million shares) were sold. Further, 7.2 million shares (2010: 6.7 million shares) were transferred to associates as part of the equity-based compensation and 56.7 million shares were used for the acquisition of the outstanding Alcon, Inc. non-controlling interests. Accordingly, the net reduction in treasury shares amounted to 9.2 million.

Following the Extraordinary General Meeting of Novartis AG on April 8, 2011, 108 million new Novartis shares were issued and these, together with the 56.7 million treasury shares, were exchanged for the outstanding interests in Alcon, Inc., which was then merged into Novartis AG on the same day.

There are outstanding written call options on Novartis shares of 35 million originally issued as part of the share-based compensation of associates. The market maker has acquired these options but they have not yet been exercised. The weighted average exercise price of these options is USD 51.35 and they have contractual lives of up to 10 years.

19. NON-CURRENT FINANCIAL DEBTS

	2011 USD millions
Straight bonds	13 483
Liabilities to banks and other financial institutions [1]	1 146
Finance lease obligations	4
Total (including current portion of non-current financial debt)	**14 633**
Less current portion of non-current financial debt	– 778
Total non-current financial debts	**13 855**
Straight bonds	
3.625% CHF 800 million bond 2008/2015 of Novartis AG, Basel, Switzerland, issued at 100.35%	844
3.5% CHF 700 million bond 2008/2012 of Novartis Securities Investment Ltd., Hamilton, Bermuda, issued at 100.32%	744
5.125% USD 3 000 million bond 2009/2019 of Novartis Securities Investment Ltd., Hamilton, Bermuda, issued at 99.822%	2986
4.125% USD 2 000 million bond 2009/2014 of Novartis Capital Corporation, New York, United States, issued at 99.897%	1996
4.25% EUR 1 500 million bond 2009/2016 of Novartis Finance S.A., Luxembourg, Luxembourg, issued at 99.757%	1935
1.9% USD 2 000 million bond 2010/2013 of Novartis Capital Corporation, New York, United States, issued at 99.867%	1998
2.9% USD 2 000 million bond 2010/2015 of Novartis Capital Corporation, New York, United States, issued at 99.522%	1990
4.4% USD 1 000 million bond 2010/2020 of Novartis Capital Corporation., New York, United States, issued at 99.237%	990
Total straight bonds	**13 483**

[1] Average interest rate 0.9% (2010: 1.6%)

		2011 USD millions
Breakdown by maturity	2011	
	2012	778
	2013	2 029
	2014	2 789
	2015	3 108
	2016	1 948
	After 2016	3 981
Total		**14 633**

		2011 USD millions
Breakdown by currency	USD	9 962
	EUR	2 042
	JPY	1 031
	CHF	1 589
	Others	9
Total		**14 633**

Fair value comparison	2011 Balance sheet USD millions	2011 Fair values USD millions
Straight bonds	13 483	14 794
Others	1 150	1 150
Total	**14 633**	**15 944**

Collateralized non-current financial debt and pledged assets	2011 USD millions
Total amount of collateralized non-current financial debts	7
Total net book value of property, plant & equipment pledged as collateral for non-current financial debts	100

The Group's collateralized non-current financial debt consists of loan facilities at usual market conditions.

The percentage of fixed rate financial debt to total financial debt was 72% at December 31, 2011, and 63% at the end of 2010.

Financial debts, including current financial debts, contain only general default covenants. The Group is in compliance with these covenants.

The average interest rate on total financial debt in 2011 was 2.7% (2010: 3.1%).

20. PROVISIONS AND OTHER NON-CURRENT LIABILITIES

	2011 USD millions
Accrued liability for employee benefits:	
– Defined benefit pension plans	2 991
– Other long-term employee benefits and deferred compensation	600
– Other post-employment benefits	1 098
Environmental provisions	1 059
Provisions for product liabilities and other legal matters	777
Contingent consideration	482
Other non-current liabilities	785
Total	7 792

PRODUCT LIABILITY PROVISIONS

For the Group's pharmaceutical products, sufficient product liability insurance is not available. In connection with potential product liability exposures for these products the Group establishes provisions for estimated obligations for claims and related legal defense costs. The provisions are based on management's judgment, advice from legal counsel and actuarially determined estimates. Actual liabilities, however, could substantially exceed the provisions that Novartis has put in place. Novartis believes that its insurance coverage and provisions are reasonable and its provisions are the best estimate in light of its business and the risk to which it is subject.

The largest portion of product liability risk provisions has been determined taking into consideration factors such as past experience, number and amount of claims reported, estimates of claims incurred but not reported, the cost of defending claims and other assumptions. As actual experience becomes known the Group refines and adjusts its product liability estimates. If any of the assumptions used in these calculations turn out to be incorrect or require material adjustment, there could be a material difference between the amount of provisions that have been recorded and the actual liability. At December 31, 2011, the discount rates used to calculate the provision are based on government bond rates and vary by payment duration and geography (US and non-US) between 0.9 % and 1.8 % (2010: between 2.2% and 2.5%). The consolidated income statement effect of a 1% increase or decrease in the discount rate is USD 25 million (2010: USD 26 million) income and USD 26 million expense (2010: USD 28 million), respectively.

ENVIRONMENTAL PROVISIONS

The material components of the environmental provisions consist of costs to sufficiently clean and refurbish contaminated sites to the extent necessary and to treat and where necessary continue surveillance at sites where the environmental exposure is less significant. The provision recorded at December 31, 2011 totals USD 1.1 billion (2010: USD 1.1 billion) of which USD 59 million (2010: USD 60 million) is included in current liabilities. USD 861 million (2010: USD 875 million) is provided for remediation at third party sites and USD 257 million (2010: USD 251 million) for remediation at owned facilities.

A substantial portion of the environmental provision relates to the remediation of Basel regional landfills in the adjacent border areas in Switzerland, Germany and France following the internal and external investigations completed during 2007 and the subsequent creation of an environmental remediation provision.

In the US, Novartis has been named under federal legislation (the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended) as a potentially responsible party (PRP) in respect of certain sites. Novartis actively participates in, or monitors, the clean-up activities at the sites in which it is a PRP. The provision takes into consideration the number of other PRPs at each site and the identity and financial position of such parties in light of the joint and several nature of the liability.

The requirement in the future for Novartis ultimately to take action to correct the effects on the environment of prior disposal or release of chemical substances by Novartis or other parties, and its costs, pursuant to environmental laws and regulations, is inherently difficult to estimate. The Novartis future remediation expenses are affected by a number of uncertainties which include, but are not limited to, the method and extent of remediation, the percentage of material attributable to Novartis at the remediation sites relative to that attributable to other parties, the financial capabilities of the other potentially responsible parties and the timing of expected expenditures. Novartis believes that its total provisions for environmental matters are adequate based upon currently available information. However, given the inherent difficulties in estimating liabilities in this area, Novartis may incur additional costs beyond the amounts provided. Management believes that such additional amounts, if any, would not be material to the Group's financial condition but could be material to the results of operations or cash flows in a given period.

The following table shows the movements in the environmental liability provisions during 2011 and 2010:

	2011 USD millions
January 1	1 126
Cash payments	– 29
Releases	– 8
Interest expense arising from discounting provisions	29
Currency translation effects	
December 31	1 118
Less current liability	– 59
Non-current environmental liability provisions at December 31	1 059

The expected timing of the related cash outflows as of December 31, 2011 is currently projected as follows:

	Expected cash outflows USD millions
Due within two years	167
Due later than two years, but less than five years	330
Due later than five years but less than ten years	506
Due after ten years	115
Total environmental liability provisions	**1 118**

LEGAL MATTERS

A number of Novartis subsidiaries are, and will likely continue to be, subject to various legal proceedings that arise from time to time, including proceedings regarding product liability, commercial disputes, employment and wrongful discharge, antitrust, securities, sales and marketing practices, health and safety, environmental, tax, privacy, and intellectual property matters. As a result, the Group may become subject to substantial liabilities that may not be covered by insurance and could affect our business and reputation. While Novartis does not believe that any of these legal proceedings will have a material adverse effect on its financial position, litigation is inherently unpredictable and large verdicts sometimes occur. As a consequence, Novartis may in the future incur judgments or enter into settlements of claims that could have a material adverse effect on its results of operations or cash flows.

Governments and regulatory authorities have been stepping up their compliance and law enforcement activities in recent years in key areas, including corruption, marketing practices, insider trading, antitrust and trade restrictions. Responding to such investigations is costly and a significant diversion of management's attention from our business. In addition, such investigations may affect our reputation and create a risk of potential exclusion from government reimbursement programs in the US and other countries. These factors have contributed to decisions by us and other companies in our industry to enter into settlement agreements with governmental authorities around the world. Those settlements have involved and may continue to involve large cash payments, including the potential repayment of amounts allegedly obtained improperly and penalties up to treble damages. In addition, settlements of healthcare fraud cases typically involve corporate integrity agreements which are intended to regulate company behavior for a period of years. Also, matters underlying governmental investigations and settlements may be the subject of separate private litigation.

Below is a summary of significant legal proceedings to which Novartis or its subsidiaries are a party or were a party and which were concluded in 2011.

GOVERNMENTAL INVESTIGATIONS

SDNY INVESTIGATION

In the fourth quarter of 2011, Novartis Pharmaceuticals Corporation (NPC) received a subpoena from the US Attorney's Office (USAO) for the Southern District of New York (SDNY) requesting the production of documents relating to marketing practices, including the remuneration of healthcare providers in connection with three NPC products (*Lotrel, Starlix and Valturna*). NPC is cooperating with the investigation which is civil and criminal in nature.

ALCON INVESTIGATION

In the third quarter of 2011, Alcon Laboratories Inc. (Alcon) received a subpoena from the US Department of Health & Human Services relating to an investigation into allegations of healthcare fraud. The subpoena requests the production of documents relating to marketing practices, including the remuneration of healthcare providers in connection with certain Alcon products (*Vigamox*, *Nevanac*, *Omnipred*, *Econopred*; surgical equipment). Alcon is cooperating with the investigation which is civil in nature

WDNY INVESTIGATION

In 2010, NPC became aware of an investigation by the USAO for the Western District of New York (WDNY) into informed consent issues relating to clinical trials in China and into marketing practices, including the remuneration of healthcare providers in connection with a number of Novartis products. NPC is cooperating with the investigation which is civil in nature.

EC DAWN RAID AT SANDOZ FRANCE

In 2009, the European Commission (EC), together with the French competition authority, searched the offices of Sandoz S.A.S. in France (Sandoz France), alleging that Sandoz France entered into anti-competitive price coordination practices with other generic pharmaceutical companies and via the French trade association for generic pharmaceutical companies. Sandoz France is cooperating with the EC and the French authorities. No follow-up requests have been received from the EC so far.

EC DAWN RAID AT SANDOZ NETHERLANDS AND SANDOZ GERMANY

In 2008, the EC conducted a dawn raid at Sandoz' offices in Holzkirchen, Germany, which was part of the EC sector inquiry. On July 6, 2010, the EC, together with the Dutch and German competition authorities, conducted a follow-up dawn raid at the Dutch and German offices of Sandoz. The EC's investigation focuses on allegations that Sandoz and/or its affiliates may have engaged in anti-competitive practices with respect to *Fentanyl* or other products in coordination with other pharmaceutical companies since 2005. On October 7, 2011, the EC informed Sandoz that it will formally initiate proceedings removing the national competition authorities' competence to investigate this case. The EC's decision was made public in the fourth quarter of 2011. Sandoz is cooperating with the EC.

PRODUCT LIABILITY MATTERS

***Zometa/Aredia* product liability litigation**

NPC together with other Novartis subsidiaries are defendants in more than 720 cases brought in US courts in which plaintiffs claim to have experienced osteonecrosis of the jaw after treatment with *Zometa* or *Aredia*, which are used to treat patients whose cancer has spread to the bones. There were four jury trials so far. The first trial began in Montana state court in October 2009 and resulted in a plaintiff's verdict which NPC appealed to the Montana Supreme Court. On December 30, 2010, the Montana Supreme Court affirmed the trial court's verdict. On March 30, 2011, NPC filed a petition for review with the US Supreme Court. On May 31, 2011, NPC was informed that the US Supreme Court decided not to take this case. The second trial took place in September and October 2010 in a New Jersey state court and resulted in a defense verdict in favor of NPC. This verdict is currently on appeal. The third trial took place in November 2010 in the US District Court for the Middle District of North Carolina and resulted in a plaintiffs' verdict. NPC filed an appeal against this verdict which is pending. The fourth trial took place in May 2011 in the US District Court for the Eastern District of New York and resulted in a defense verdict in favor of NPC. This verdict is also currently on appeal. Multiple trials are currently scheduled throughout the first half of 2012. The first trial began in the Western District of Kentucky on January 9, 2012.

Hormone Replacement Therapy product liability litigation

NPC and other Novartis subsidiaries are defendants, along with various other pharmaceutical companies, in more than 60 cases brought in US courts in which plaintiffs claim to have been injured by hormone replacement therapy products.

***Elidel*® product liability litigation**

NPC and other Novartis subsidiaries are defendants in more than 20 cases brought in US courts in which plaintiffs claim to have experienced injuries, mainly various types of cancer, after having been treated with *Elidel*®, a medicine for atopic dermatitis.

OTHER MATTERS

Average Wholesale Price litigation

Claims have been brought against various pharmaceutical companies, including certain Sandoz entities and NPC, alleging that they fraudulently overstated the Average Wholesale Price (AWP) and "best price", respectively, which are, or have been, used by the US federal and state governments in the calculation of Medicare reimbursements and Medicaid rebates.

In the third quarter of 2011, the US Department of Justice (DoJ) approved an agreement to settle the litigation brought by the State of Texas and the relator Ven-A-Care of the Florida Keys (VAC) as well as claims of the federal government relating to Texas against several Sandoz entities. The settlement amount of USD 66 million, which had already been fully provisioned during 2011, was paid in the third quarter of 2011 and the case has been dismissed.

In the second quarter of 2011, Sandoz Inc. (Sandoz) reached an agreement in principle to settle with the relator VAC the pending AWP action brought on behalf of the US Government as well as the AWP cases brought by the States of California and Florida for a total amount of USD 150 million. On November 3, 2011, the written settlement agreement was executed by all parties and the payment of the settlement amount, which had been fully provisioned for during 2011, was made in the fourth quarter of 2011.

A bench trial against Sandoz in Mississippi chancery court ended on April 15, 2011. On September 2, 2011, the court rendered judgment in favor of Sandoz on the false claims provisions but against Sandoz on the other causes of action and awarded plaintiff a total of USD 38.2 million (USD 23.7 million in compensatory damages, USD 2.7 million in civil penalties and USD 11.8 million in punitive damages). On October 4, 2011, the court granted Sandoz' post-judgment motion to strike the punitive damage award. An evidentiary hearing will now take place in order to determine whether punitive damages are appropriate and, if so, in what amount punitive damages should be awarded.

Further, Sandoz was a defendant in a trial in Alabama in 2009. The jury rendered a verdict against it and awarded compensatory damages of USD 28 million and punitive damages of USD 50 million. Sandoz appealed the verdict to the Supreme Court of Alabama in January 2010. A decision is still outstanding.

A further trial involving Sandoz took place in Kentucky in June 2009. The jury rendered a verdict against Sandoz and imposed USD 16 million in compensatory damages, and the Court awarded USD 13.6 million in penalties, which were subsequently reduced to USD 11.2 million. Sandoz appealed this verdict in March 2010. A decision is still outstanding.

On October 12, 2011, plaintiffs offered to settle the New York City, New York Counties, Erie, Oswego, Schenectady and Iowa cases for USD 25 million. Sandoz has agreed in principle and the terms of the settlement are currently being negotiated with plaintiffs. The settlement amount was fully provisioned for in the fourth quarter of 2011.

Wage and Hour litigation

Certain pharmaceutical sales representatives filed suit in a state court in California and in the US District Court for the SDNY against NPC alleging that NPC violated wage and hour laws by misclassifying the pharmaceutical sales representatives as "exempt" employees, and by failing to pay overtime compensation. These actions are part of a number of lawsuits pending against pharmaceutical companies that challenge the industry's long-term practice of treating pharmaceutical sales representatives as salaried employees. After the California state court action had been removed to the US District Court for the Central District of California, these collective and class action lawsuits were consolidated in the US District Court for the SDNY for coordinated pre-trial proceedings. A class was certified. In January 2009, after the case had been bifurcated into a liability and a damages phase, the US District Court for the SDNY granted NPC's summary judgment motion holding that NPC's pharmaceutical sales representatives were not entitled to overtime pay under the federal Fair Labor Standards Act and corresponding state wage and hour laws. Plaintiffs appealed that judgment to the US Court of Appeals for the Second Circuit (Second Circuit). Amicus briefs supporting plaintiffs' position were filed by the National Employment Lawyers Association and by the US Department of Labor, and the US Chamber of Commerce filed a brief in support of NPC. On July 6, 2010, the Second Circuit vacated the judgment of the lower court. On October 4, 2010, NPC filed its petition for a writ of certiorari with the US Supreme Court. Amicus briefs in support of NPC's certiorari petition were filed on November 5, 2010, by the US Chamber of Commerce and Pharmaceutical Research and Manufacturers of America (PhRMA). On February 28, 2011, NPC was informed that the US Supreme Court decided not to take this case. The case has now been remanded to the US District Court for the SDNY for pre-trial proceedings relating to damages.

***Lucentis* patent litigation**

Novartis has been sued by and has sued MedImmune in several European countries, including the United Kingdom, Germany, Switzerland, France and the Netherlands. MedImmune alleges that the sale of *Lucentis* in these countries infringes its patents and its rights under its Supplementary Protection Certificates (SPC). In the UK, a trial took place in May 2011. On July 5, 2011, the UK court issued its decision and held that Novartis did not infringe MedImmune's patents and that MedImmune's patents were invalid. MedImmune has filed an appeal against this decision. In Germany, the infringement trial took place on October 18, 2011. On November 10, 2011, the German court ruled that the import and sale of *Lucentis* infringes MedImmune's patent and rights under its SPC in Germany. This decision is being appealed.

CONCLUDED LEGAL MATTERS

***Trileptal*/Five products investigation**

On September 30, 2010, NPC reached a global settlement in order to bring to a close the USAO for the Eastern District of Pennsylvania's (EDPA) investigations into marketing practices and payments made to healthcare providers in connection with *Trileptal* and in connection with five other products, i.e. *Diovan*, *Exforge*, *Sandostatin*, *Tekturna* and *Zelnorm* (Five Products). As part of the settlement, NPC agreed to plead guilty to one misdemeanor violation of misbranding under the US Food, Drug and Cosmetic Act and to pay a fine of USD 185 million for *Trileptal*. NPC also resolved civil allegations under the False Claims Act relating to *Trileptal* and the Five Products and agreed to pay USD 237.5 million. As the fine was formally imposed on NPC at the sentencing hearing in the US District Court for the EDPA on January 28, 2011, and payment of the total overall settlement amount of USD 422.5 million, which had been fully provisioned for in 2010, has been completed in the first quarter of 2011, these investigations are closed now.

Alcon minority shareholder litigation

Beginning on January 7, 2010, shareholder class action complaints relating to the Alcon transactions announced on January 4, 2010, were filed against Novartis AG and others by minority shareholders of Alcon, Inc. These actions were filed in the US Federal District Courts for the SDNY, Eastern District of New York (EDNY) and the Northern District of Texas (NDTX) and in several Texas state courts. The case in the EDNY was voluntarily dismissed without prejudice by the plaintiffs on March 18, 2010. The case in the NDTX was transferred to the SDNY and formally consolidated with the actions pending there on June 25, 2010. In the SDNY, Novartis AG's motion to dismiss all cases pending there based on the doctrine of forum non conveniens (FNC) was granted on May 24, 2010, and the case was formally dismissed on July 2, 2010. On July 14, 2010, plaintiffs appealed this decision to the Second Circuit. On January 5, 2011, plaintiffs moved to dismiss this appeal. On January 6, 2011, the Second Circuit granted plaintiffs' motion and dismissed this appeal. The actions pending in Texas state courts were consolidated for pre-

trial proceedings in a Multi District Litigation on April 16, 2010. Novartis AG's motion to dismiss the consolidated Texas state court actions based on FNC was filed on June 30, 2010. On November 17, 2010, Novartis AG's motion was granted and all Texas state court class actions were dismissed. On December 17, 2010, plaintiffs appealed this decision to the Texas Fifth District Court of Appeals. On March 21, 2011, upon a motion made by plaintiffs, the Texas Fifth District Court of Appeals dismissed the appeal. The dismissals of both the federal and Texas state class actions based on FNC are final after plaintiffs dismissed their appeals. The case, therefore, is concluded.

***Zelnorm* product liability litigation**

NPC together with other Novartis subsidiaries are currently defending against product liability lawsuits brought in US courts in which plaintiffs claim to have experienced cardiovascular injuries after having been treated with *Zelnorm*, a medicine for irritable bowel syndrome and chronic constipation. In the third quarter of 2011, NPC finalized the previously disclosed group settlement agreement with 122 plaintiffs. The finalization of this group settlement alongside other settlements and dismissals in the fourth quarter of 2011 brought the current caseload in the US down from 154 to 2 active cases.

The following table shows the movements in the legal and product liability provisions during 2011 and 2010:

	2011 USD millions
January 1	1 384
Impact of business combinations	
Cash payments	– 772
Releases of provisions	– 16
Additions to provisions	584
Currency translation effects	2
December 31	1 182
Less current liability	– 405
Non-current legal and product liability provisions at December 31	777

Novartis believes that its total provisions for legal and product liability matters are adequate based upon currently available information. However, given the inherent difficulties in estimating liabilities, it cannot be guaranteed that additional costs will not be incurred beyond the amounts provided.

21. CURRENT FINANCIAL DEBT

	2011 USD millions
Interest bearing accounts of associates	1 357
Other bank and financial debt	2 053
Commercial paper	2 156
Current portion of non-current financial debt	778
Fair value of derivative financial instruments	30
Total current financial debt	6 374

The consolidated balance sheet values of current financial debt, other than the current portion of non-current financial debt, approximate the estimated fair value due to the short-term nature of these instruments.

The weighted average interest rate on the bank and other current financial debt (including employee deposits from the compensation of associates employed by Swiss entities) was 1.7% in 2011 and 2.0% in 2010.

22. PROVISIONS AND OTHER CURRENT LIABILITIES

	2011 USD millions
Taxes other than income taxes	578
Restructuring provisions	349
Accrued expenses for goods and services received but not invoiced	678
Provisions for royalties	443
Provisions for revenue deductions	3 742
Provisions for compensation and benefits including social security	2 116
Environmental liabilities	59
Deferred income relating to government grants	70
Provision for legal matters	405
Accrued share-based payments	217
Other payables	1 422
Total provisions and other current liabilities	10 079

Provisions are based upon management's best estimate and adjusted for actual experience. Such adjustments to the historic estimates have not been material.

PROVISION FOR DEDUCTIONS FROM REVENUE

Deductions from revenue are reported as a reduction of revenue. They include rebates, discounts, incentives to retail customers, government agencies, wholesalers, health insurance companies and managed care organizations. These deductions represent estimates of the related obligations, requiring the use of judgment when estimating the effect of these sales deductions. The following table shows the movement of the provision for deductions from revenue:

	2011 USD millions
January 1	3 097
Impact of business combinations	
Additions	11 713
Payments/utilizations	– 10 749
Changes in offset against gross trade receivables	– 227
Currency translation effects	– 92
December 31	3 742

RESTRUCTURING PROVISIONS

	Termination costs of associates USD millions	Other third party costs USD millions	Total USD millions
January 1, 2010			
Additions			
Cash payments			
Releases			
Currency translation effects			
December 31, 2010			
Additions	299	47	346
Cash payments	– 189	– 14	– 203
Releases	– 33	– 4	– 37
Currency translation effects	2		2
December 31, 2011	300	49	349

In 2011, there were additions to provisions of USD 151 million in the Pharmaceuticals Division in conjunction with the transfer, outsourcing, closure of selected research operations, as well as simplifying and streamlining of certain development and support functions. The charges comprised termination costs of associates of USD 139 million and other third party costs of USD 12 million. In total, approximately 1 000 associates were affected by this restructuring plan, though none of them had left the Group as of December 31, 2011. It is anticipated that most or all of these associates will leave the Group within the next twelve months.

Also in 2011, additions to provisions were made in conjunction with the integration of Alcon. The charges comprised termination costs of associates of USD 47 million and other third party costs of USD 15 million. In total, approximately 300 associates were affected by the various restructuring plans. Approximately 100 associates had left the Group as of December 31, 2011. It is anticipated that the remainder of these associates will leave the Group within the next twelve months.

The Group-wide review of its manufacturing sites led to additions in restructuring provisions of USD 79 million in 2011 related to the restructuring of the manufacturing and chemical operations, mainly in Switzerland, United Kingdom, US, Italy and Puerto Rico. The charges comprised termination costs of associates of USD 77 million and other third party costs of USD 2 million. As of December 31, 2011, 200 of the approximately 1 000 associates affected by the restructuring plans have left the Group and the remaining associates will leave the Group when their respective activity is transferred to other sites.

Various Group initiatives to further simplify the organization led to restructuring charges of USD 54 million, mainly in Italy and Switzerland. The charges comprised termination costs of associates of USD 36 million and other third party costs of USD 18 million. In total, approximately 300 associates were affected by the various restructuring plans, of which 100 had left the Group as of December 31, 2011. It is anticipated that the remainder of these associates will leave the Group within the next twelve months.

In 2010, additions to provisions of USD 89 million were incurred in conjunction with the adjustment of the field force structures to better support the portfolio of the primary care and neuroscience medicines business within the Pharmaceuticals Division in the United States. The charges comprised termination costs of associates of USD 78 million and other third party costs of USD 11 million. In total, approximately 1 400 associates were affected by the various restructuring plans, all of whom had left the Group as of December 31, 2011.

Also in 2010, additions to provisions of USD 44 million were incurred in conjunction with the consolidation of regional units of the primary care medicines business and the integration of a research entity within the Pharmaceuticals Division in the United States. The charges comprised termination costs of associates of USD 44 million. In total, 383 associates were affected by the various restructuring plans, all of whom had left the Group as of December 31, 2010.

Additions to provisions of USD 62 million were incurred in 2010 in conjunction with the restructuring of the technical and commercial operations of the Vaccines and Diagnostics Division in England, France, Germany, Italy and the United States. The charges comprised termination costs of associates of USD 46 million and other third party costs of USD 16 million. As of December 31, 2011, it is anticipated that all associates will have left the Group in the first quarter 2012.

2010 also saw additions to provisions of USD 66 million which were incurred in conjunction with the restructuring of the commercial operations of the Sandoz Division in Germany. The charges comprised termination costs of associates of USD 57 million and other third party costs of USD 9 million. As of December 31, 2011, it is anticipated that all associates will have left the Group in the first quarter 2012.

The releases to income in 2011 and 2010 of USD 37 million and USD 18 million, respectively, were mainly due to settlement of liabilities at lower amounts than originally anticipated, which in 2011 were principally due to provisions made in relation with prior years restructuring initiatives. Other third party costs are mainly associated with lease and other obligations due to the abandonment of certain facilities.

23. DETAILS TO THE CONSOLIDATED CASH FLOW STATEMENTS

23.1) REVERSAL OF NON-CASH ITEMS

	2011 USD millions
Taxes	1 528
Depreciation, amortization and impairments on	
Property, plant & equipment	2 141
Intangible assets	3 647
Financial assets	192
Income from associated companies	– 528
Gains on disposal of property, plant & equipment, intangible, financial and other non-current assets, net	– 518
Equity-settled compensation expense	790
Change in provisions and other non-current liabilities	1 295
Net financial income	753
Total reversal of non-cash items	**9 300**

23.2) CASH FLOWS FROM CHANGES IN WORKING CAPITAL AND OTHER OPERATING ITEMS INCLUDED IN OPERATING CASH FLOW

	2011 USD millions
Change in inventories	45
Change in trade receivables	– 732
Change in trade payables	195
Change in other net current assets and other operating cash flow items	379
Total	**– 113**

23.3) CASH FLOW ARISING FROM ACQUISITIONS AND DIVESTMENTS OF BUSINESSES

The following is a summary of the cash flow impact of acquisitions and divestments of businesses:

	2011 Acquisitions USD millions	2011 Divestments USD millions	
Property, plant & equipment	– 66	16	
Currently marketed products	– 101		
Marketing know-how			
Alcon brand name			
Acquired research & development	– 7		
Technologies	– 3		
Software and other intangible assets	– 1		
Financial and other assets including deferred tax assets	– 7		
Inventories	– 15	8	
Trade accounts receivables and other current assets	– 52	5	
Marketable securities and cash	– 186	1	
Long-term and short-term financial debts			
Trade payables and other liabilities including deferred tax liabilities	66	– 7	
Net identifiable assets acquired or divested	**– 372**	**23**	
Acquired / divested liquidity	63	– 1	
Non-controlling interest	19		
Fair value of previously held equity interests			10 320
Sub-total	**– 290**	**22**	
Goodwill	– 303		
Deferred consideration	2		
Net cash flow	**– 591**	**22**	

Note 2 provides further information regarding acquisitions and divestments of businesses. All acquisitions were for cash.

24. ACQUISITIONS OF BUSINESSES

ASSETS AND LIABILITIES ARISING FROM ACQUISITIONS

Fair value	2011 USD millions
Property, plant & equipment	66
Currently marketed products	101
Marketing know-how	
Alcon brand name	
Acquired research & development	7
Technologies	3
Software and other intangible assets	1
Financial and other assets including deferred tax assets	7
Inventories	15
Trade accounts receivable and other current assets (net of provisions for doubtful trade receivables of USD 56 m in 2010)	52
Marketable securities and cash	186
Long-term and short-term financial debts	
Trade payables and other liabilities including deferred tax liabilities	– 66
Net identifiable assets acquired	**372**
Acquired liquidity	– 63
Non-controlling interest	– 19
Goodwill	303
Net assets recognized as a result of business combinations	**593**

Note 2 provides details on all the significant acquisition of businesses. The 2011 and 2010 goodwill arising out of the acquisitions reflects mainly the value of expected synergies, future products and the acquired assembled workforce.

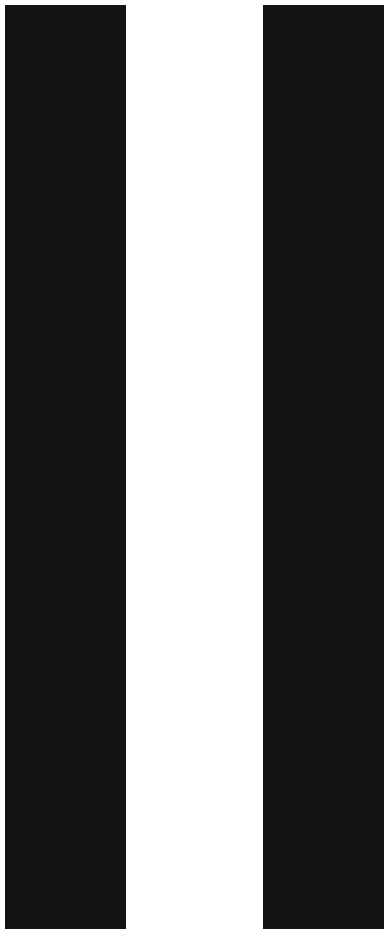
The following table provides a summary of the final acquisition accounting for Alcon, Inc. as at August 25, 2010:

	USD billions	USD billions
Purchase price for acquiring initial 25% of Alcon		10.4
Purchase price for additional 52% of Alcon		28.3
Total purchase price		**38.7**
Equity adjustments since acquiring the initial 25% interest		– 0.4
Revaluation gain on initial 25% interest		0.4
Investment value on date of change of majority ownership		**38.7**
Net assets reported by Alcon (excluding its goodwill but including any US GAAP/IFRS differences)	5.9	
Estimated fair value adjustments		
– property, plant and equipment	0.1	
– intangible assets	24.5	
– inventory	0.5	
– other liabilities	– 0.1	
– deferred tax liabilities	– 3.8	
Fair value of net assets acquired at December 31, 2010		27.1
Less value attributed to 23% non-controlling interest		– 6.3
Goodwill at December 31, 2010		**17.9**
Increase in goodwill due to reduction in fair value of net assets after final adjustment to acquisition accounting in 2011		0.1
Final goodwill at December 31, 2011		**18.0**

25. POST-EMPLOYMENT BENEFITS OF ASSOCIATES

DEFINED BENEFIT PLANS

Apart from the legally required social security schemes, the Group has numerous independent pension and other post-employment



25. POST-EMPLOYMENT BENEFITS OF ASSOCIATES (CONTINUED)

The net periodic benefit cost recorded in the consolidated income statement consists of the following components:

	Pension plans	Other post-employment benefit plans
	2011 USD millions	2011 USD millions
Components of net periodic benefit cost		
Service cost	423	60
Interest cost	732	60
Expected return on plan assets	– 909	– 15
Recognized past service cost	3	– 5
Curtailment and settlement losses/(gains)	18	
Net periodic benefit cost/(income)	**267**	**100**

The following table shows the principal actuarial weighted average assumptions used for calculating defined benefit plans and other post-employment benefits of associates:

	Pension plans	Other post-employment benefit plans
	2011 %	2011 %
Weighted average assumptions used to determine benefit obligations at December 31		
Discount rate	3.2%	4.3%
Expected rate of salary increase	3.3%	
Current average life expectancy for a 65-year-old male/female	20/22 years	20/22 years
Weighted average expected return on assets for the period	4.6%	

The following table shows a five-year summary reflecting the funding of defined benefit pensions and the impact of historical deviations between expected and actual return on plan assets and experience adjustments on defined benefit pension obligations.

	2011 USD millions
Plan assets	18 826
Defined benefit obligations	– 21 730
(Deficit)/Surplus	**– 2 904**
Differences between expected and actual return on plan assets	– 1 038
Experience adjustments on defined benefit obligation	18

The following table shows the weighted average asset allocation of funded defined benefit pension plans at December 31, 2011 and 2010:

	Pension plans	
	Long-term target %	2011 %
Equity securities	15–40	25
Debt securities	45–70	49
Real estate	0–15	13
Cash and other investments	0–15	13
Total		**100**

Strategic pension plan asset allocations are determined with the objective of achieving an investment return which, together with the contributions paid, is sufficient to maintain reasonable control over the various funding risks of the plans. Based upon the market and economic environments, actual asset allocations may periodically be permitted to deviate from policy targets. Expected return assumptions are reviewed periodically and are based on each plan's strategic asset mix. Factors considered in the estimate of the expected return are the risk free interest rate together with risk premiums on the assets of each pension plan.

The expected future cash flows in respect of pension and other post-employment benefit plans at December 31, 2011 were as follows:

	Pension plans USD millions	Other post-employment benefit plans USD millions
Novartis Group contributions		
2012 (estimated)	455	40
Expected future benefit payments		
2012	1 258	51
2013	1 264	53
2014	1 273	56
2015	1 285	59
2016	1 288	62
2017–2021	6 476	363

The healthcare cost trend rate assumptions for other post-employment benefits are as follows:

Healthcare cost trend rate assumptions used	2011
Healthcare cost trend rate assumed for next year	7.7%
Rate to which the cost trend rate is assumed to decline	5.0%
Year that the rate reaches the ultimate trend rate	2020

A one percentage point change in the assumed healthcare cost trend rates compared to those used for 2011 would have had the following effects:

	1% point increase USD millions	1% point decrease USD millions
Effects on total of service and interest cost components	16	– 13
Effect on post-employment benefit obligations	196	– 159

The number of Novartis AG shares held by pension and similar benefit funds at December 31, 2011 was 19.8 million shares with a market value of USD 1.1 billion (2010: 19.8 million shares with a market value of USD 1.2 billion).

DEFINED CONTRIBUTION PLANS

In many Group companies associates are covered by defined contribution plans and other long-term benefits. Contributions charged to the 2011 consolidated income statement for the defined contribution plans were USD 337 million (2010: USD 269 million).

26. EQUITY-BASED PARTICIPATION PLANS OF ASSOCIATES

The expense recorded in the consolidated income statement spreads the cost of each grant equally over the vesting period. Assumptions are made concerning the forfeiture rate which is adjusted during the vesting period so that at the end of the vesting period there is only a charge for vested amounts. The expense related to all Novartis equity plans and Alcon, Inc., equity plans granted to associates prior to the merger in the 2011 consolidated income statement was USD 1 billion (2010: USD 841 million) resulting in a total carrying amount for liabilities arising from share-based payment transactions of USD 217 million (2010: USD 200 million).

Equity-based participation plans can be separated into the following plans.

NOVARTIS EQUITY PLAN "SELECT"

The equity plan "Select" is a global equity incentive plan under which all associates, including Executive Committee members, may annually be eligible for a grant, which is capped at 200% of target. The equity-based long-term incentive is subject to the achievement of predetermined business and individual performance objectives at grant. No awards are granted for performance ratings below a certain threshold.

The Equity Plan "Select" allows its participants to choose the form of their equity compensation in restricted shares (or, in some jurisdictions, restricted share units (RSUs), tradable share options, or a combination of both, with a vesting period of three years.

In some jurisdictions, RSUs are granted rather than shares. Each RSU is equivalent in value to one Novartis share and is converted into one share at the vesting date. RSUs do not carry any voting or dividend rights, except for the US where employees receive a dividend equivalent for the 2009 and 2010 grants during the vesting period. Each restricted share is entitled to voting rights and payment of dividends during the vesting period.

Tradable share options expire on their 10th anniversary from grant date. Each tradable share option granted to associates entitles the holder to purchase after vesting (and before the 10th anniversary from grant date) one Novartis share at a stated exercise price that equals the closing market price of the underlying share at the grant date (January 19, 2011).

If a participant leaves Novartis, for reasons other than retirement, disability or death, unvested shares, RSUs and share options are forfeited, unless determined otherwise by the Compensation Committee (for example, in connection with a reorganization or divestment).

NOVARTIS EQUITY PLAN "SELECT" OUTSIDE NORTH AMERICA

Directors, executives and other selected associates of Group companies (collectively, the "Participants") may receive equity awards. The vesting period for the plan is three years except Switzerland which had until 2010 a vesting period of two years that will be increased to three years as of the 2011 performance onwards.

The expense recorded in the 2011 consolidated income statement relating to both shares and share options under this plan amounted to USD 158 million (2010: USD 149 million). Participants in this plan were granted a total of 2.2 million units at CHF 54.70 (2010: 2.3 million units at CHF 55.85).

The following table shows the assumptions on which the valuation of share options granted during the period was based:

	Novartis Equity Plan "Select" outside North America
	2011
Valuation date	January 19, 2011
Expiration date	January 19, 2021
Closing share price on grant date	CHF 54.70
Exercise price	CHF 54.70
Implied bid volatility	14.90%
Expected dividend yield	4.82%
Interest rate	2.06%
Market value of option at grant date	CHF 5.06

The following table shows the activity associated with the share options during the period. The weighted average prices in the table below are translated from Swiss Francs into USD at historical rates for the granted, sold, and forfeited or expired figures. The year-end prices are translated using the corresponding year-end rates.

	2011	
	Options (millions)	Weighted average exercise price (USD)
Options outstanding at January 1	**34.7**	**52.3**
Granted	5.7	57.0
Sold or exercised	–3.9	46.4
Forfeited or expired	–1.0	56.6
Outstanding at December 31	**35.5**	**53.5**
Exercisable at December 31	**22.2**	**52.4**

All share options were granted at an exercise price which was equal to the market price of the Group's shares at the grant date and between 2000 and 2003 was greater than the market price of the Group's shares at the grant date. The weighted average exercise price during the period the options were sold or exercised in 2011 was USD 46.4. The weighted average share price at the dates of exercise was USD 49.0.

The following table summarizes information about share options outstanding at December 31, 2011:

	Options outstanding		
Range of exercice prices (USD)	Number outstanding (millions)	Average remaining contractual life (years)	Weighted average exercise price (USD)
30–34	0.6	0.2	34.8
35–39			
40–44			
45–49	9.3	5.6	46.9
50–54	11.2	7.0	54.4
55–59	14.4	6.7	57.9
Total	**35.5**	**6.4**	**53.5**

NOVARTIS EQUITY PLAN "SELECT" FOR NORTH AMERICA

The plan provides for equity awards to North American based Directors, executives and other selected associates. The terms and conditions of the Novartis Equity Plan "Select" for North America are substantially equivalent to the Novartis Equity Plan "Select" outside North America. Share options in this plan have only been tradable since 2004.

The expense recorded in the 2011 consolidated income statement relating to both shares and share options under this plan amounted to USD 263 million (2010: USD 237 million). Participants in this plan were granted a total of 4.1 million units at USD 57.07 (2010: 3.5 million units at USD 53.70).

The following table shows the assumptions on which the valuation of share options granted during the period was based:

	Novartis Equity Plan "Select" for North America
	2011
Valuation date	January 19, 2011
Expiration date	January 19, 2021
Closing ADS price on grant date	USD 57.07
Exercise price	USD 57.07
Implied bid volatility	13.80%
Expected dividend yield	4.83%
Interest rate	3.50%
Market value of option at grant date	USD 5.94

The following table shows the activity associated with the share options during the period:

	2011	
	ADS options (millions)	Weighted average exercise price (USD)
Options outstanding at January 1	**60.0**	**51.1**
Granted	11.8	57.1
Sold or exercised	– 10.2	52.2
Forfeited or expired	– 3.1	51.6
Outstanding at December 31	**58.5**	**52.1**
Exercisable at December 31	**19.6**	**52.6**

All share options were granted at an exercise price which was equal to the market price of the American Depositary Shares (ADSs) at the grant date. The weighted average exercise price during the period the share options were sold or exercised in 2011 was USD 52.2. The weighted average share price at the dates of exercise was USD 59.4.

The following table summarizes information about ADS options outstanding at December 31, 2011:

	ADS options outstanding		
Range of exercice prices (USD)	Number outstanding (millions)	Average remaining contractual life (years)	Weighted average exercise price (USD)
35–39	2.5	0.9	36.5
40–44			
45–49	19.1	6.2	46.6
50–54	15.4	7.4	53.9
55–59	21.5	7.3	57.6
Total	**58.5**	**6.7**	**52.1**

LONG-TERM PERFORMANCE PLAN

The Long-Term Performance Plan (LTPP) is an equity plan for key executives designed to foster long-term commitment by aligning the incentives of key executives to the performance of Novartis. The LTPP is offered to selected executives, who are in key positions and have a significant impact on the long-term success of Novartis and is capped at 200% of target. The rewards are based on predetermined rolling three year global performance objectives focused on the Novartis Economic Value Added (NVA) measured annually. The NVA is calculated based on Group operating income adjusted for interest, taxes and cost of capital charge. The performance realization of a plan cycle is obtained right after the end of the third plan year by adding together the annual NVA realizations of all plan years of the plan cycle. The performance ratio for a plan cycle is obtained by dividing the performance realization for the plan cycle with the performance target for the plan cycle, expressing the result as a percentage. The LTPP only allows a payout when the actual NVA exceeds predetermined target thresholds.

At the beginning of the performance period, plan participants are allocated RSUs, which will be converted into Novartis shares after the performance period.

At the end of the three-year performance period, the Compensation Committee adjusts the number of RSUs earned based on actual performance. RSUs are converted into unrestricted Novartis shares without an additional vesting period. In the United States, awards may also be delivered in cash under the US deferred compensation plan.

The expense recorded in the 2011 income statement related to this plan amounted to USD 40 million (2010: USD 32 million). On January 19, 2011 a total of 0.4 million performance share units (2010: 0.4 million performance share units) were granted to 127 key executives participating in this plan.

SPECIAL SHARE AWARDS

Selected associates may exceptionally receive special awards of restricted shares or RSUs. These special Share Awards provide an opportunity to reward outstanding achievements or exceptional performance and aim at retaining key contributors. They are based on a formal internal selection process, in which the individual performance of each candidate is thoroughly assessed at several management levels. In addition, Special Share Awards may also be granted to attract special expertise and new talents into the organization. These grants are consistent with the Novartis' philosophy to attract, retain and motivate best in class talents around the world.

Restricted special awards generally have a five-year vesting period. If an associate leaves Novartis for reasons other than retirement, disability or death, unvested shares or RSUs are generally forfeited. Worldwide 597 associates at different levels in the organization were awarded restricted shares in 2011. The expense recorded for such special share awards in the 2011 income statement amounted to USD 27 million (2010: USD 33 million). During 2011, a total of 1.5 million restricted shares or RSUs (2010: 1.1 million

restricted shares or RSUs) were granted to executives and selected associates.

LEVERAGED SHARE SAVINGS PLANS

A number of associates in certain countries and certain key executives worldwide are encouraged to invest their Annual Incentive in a share savings plan, which is capped at 200% of target. Under the share savings plan, they will receive their annual incentive awards fully or partially in Novartis shares in lieu of cash. As a reward for their participation in the share savings plan, Novartis matches their investments in shares after a holding period of 3 or 5 years. As a rule, no shares are matched under these plans if an associate leaves Novartis prior to expiration of the holding period for reasons other than retirement, disability or death.

Novartis currently has three share savings plans:

- In Switzerland, the Employee Share Ownership Plan (ESOP) was available to 11 997 associates. Participants within this plan may choose to receive the incentive (i) 100% in shares, (ii) 50% in shares and 50% in cash or (iii) 100% in cash. After expiration of a three-year holding period of Novartis shares invested under ESOP, each participant will receive one free matching share for every two Novartis shares granted. A total of 5 454 associates chose to receive shares under the ESOP for their performance in 2010.
- In the United Kingdom, 2 790 associates can invest up to 5% of their monthly salary in shares (up to a maximum of GBP 125) and also may be invited to invest all or part of their net annual incentive in shares. Two invested shares are matched with one share with a holding period of three years. During 2011, 1 870 associates elected to participate in this plan.
- Worldwide 26 key executives were invited to participate in a Leveraged Share Savings Plan based on their performance in 2010. Instead of cash, their annual incentive was awarded in shares and subject to a holding period of five years. At the end of the holding period, Novartis will match the invested shares at a ratio of 1:1 (i.e. one share awarded for each invested share).

Associates may only participate in one of these plans in any given year.

The expense recorded in the 2011 income statement related to these plans amounted to USD 429 million (2010: USD 366 million). During 2011, a total of 5.4 million shares (2010: 5.8 million shares) were granted to participants of these plans.

SUMMARY OF NON-VESTED SHARE MOVEMENTS

The table below provides a summary of non-vested share movements (restricted shares, RSUs and ADSs) for all plans:

	2011	
	Number of shares in millions	Fair value in USD millions
Non-vested shares at January 1	17.7	1015.7
Granted	14.3	823.9
Vested	– 10.0	– 590.1
Forfeited	– 1.2	– 69.4
Non-vested shares at December 31	20.8	1 180.1

ALCON, INC., EQUITY PLANS GRANTED TO ASSOCIATES PRIOR TO THE MERGER

The expense recorded in the 2011 consolidated income statement relating to equity-based compensation awards granted to Alcon, Inc., associates prior to the merger on April 8, 2011 amounted to USD 98 million (August 25 to December 31, 2010: USD 22 million). Participants in those plans were granted 1.9 million restricted share units (RSUs) during 2011 (from August 25 to December 31, 2010: 0.7 million converted Novartis RSUs).

CHANGE OF CONTROL PROVISIONS

Upon the change of majority ownership in Alcon, Inc., from Nestlé to Novartis, Alcon equity-based compensation awards granted to associates prior to January 1, 2009 vested immediately. However, the vesting of similar awards granted after January 1, 2009 accelerates only if the respective participant's employment with Novartis subsidiaries is terminated without cause, or by the participant under certain circumstances, within six months preceding or during the two years following a change of control. At the completion of the merger of Alcon, Inc., into Novartis, all awards outstanding under the Alcon equity plans were converted to awards based upon Novartis shares as defined in the Merger Agreement.

SHARE OPTIONS AND SHARE-SETTLED APPRECIATION RIGHTS

Share options entitle the recipient to purchase Novartis shares at the closing market price of the former Alcon, Inc., share on the day of grant divided by the conversion factor of 3.0727.

Share-settled appreciation rights (SSAR) entitle the participant to receive, in the form of Novartis shares, the difference between the values of the former Alcon, Inc., share at the date of grant, converted into Novartis shares using the conversion factor of 3.0727, and the Novartis share price at the date of exercise. Share options and SSARs are exercisable upon satisfaction of the conditions set forth in the respective award agreement, generally three years following the date of grant.

The compensation expense for equity awards was calculated on a straight-line basis over the three-year vesting period of the applicable equity awards, with acceleration of the expense for individuals meeting the requirements for retirement and under the change of control provisions, as described above. There were no grants of share options or SSARs under these plans in 2011 and 2010.

The following table shows the activity associated with the converted Novartis share options and SSARs during 2011 and from August 25 to December 31, 2010:

	Number of options (millions)	Weighted average exercise price (USD)	Number of SSARs (millions)	Weighted average exercise price (USD)
Outstanding at August 25, 2010				
Sold or exercised				
Outstanding at December 31, 2010				
Exercisable at December 31, 2010				
Outstanding at January 1, 2011	9.7	22.0	11.7	36.3
Sold or exercised	–5.2	20.7	–3.3	41.8
Outstanding at December 31, 2011	4.5	23.5	8.4	34.2
Exercisable at December 31, 2011	4.0	22.9	3.3	43.4

RESTRICTED SHARE UNITS

Restricted Share Units (RSUs) entitle the recipient to receive a specified number of Novartis shares on the date of vesting. RSUs will vest and become transferable upon satisfaction of the conditions set forth in the restricted share unit award agreements, generally three years following the grant date. Holders of RSUs have no voting rights and receive dividend equivalents prior to vesting.

The fair value of each RSU was estimated at the closing market price on the day of grant. At the date of the merger on April 8, 2011, the awards were converted into Novartis RSUs at a conversion factor of 3.0727. The compensation expense is recognized over the required service period, generally three years following the day of grant.

Until the merger on April 8, 2011, participants were granted 1.9 million converted Novartis RSUs (from August 25 to December 31, 2010: 0.7 million converted Novartis RSUs). The fair value of those instruments amounted to USD 108 million. At December 31, 2011, there were 5.0 million Novartis RSUs outstanding with a fair value of USD 261 million.

27. RELATED PARTIES

GENENTECH/ROCHE

Novartis has two agreements with Genentech, Inc., USA, a subsidiary of Roche Holdings AG which is indirectly included in the consolidated financial statements using equity accounting since Novartis holds 33.3% of the outstanding voting shares of Roche.

LUCENTIS

Novartis has licensed the exclusive rights to develop and market *Lucentis* outside the US for indications related to diseases of the eye. As part of this agreement, Novartis paid Genentech/Roche an initial milestone and shared the cost for the subsequent development by making additional milestone payments upon the achievement of certain clinical development points and product approval. Novartis also pays royalties on the net sales of *Lucentis* products outside the US. *Lucentis* sales of USD 2.0 billion (2010: USD 1.5 billion) have been recognized by Novartis.

XOLAIR

In February 2004, Novartis Pharma AG, Genentech, Inc., and Tanox, Inc., finalized a three-party collaboration to govern the development and commercialization of certain anti-IgE antibodies including *Xolair* and TNX-901. Under this agreement, all three parties co-developed *Xolair*. On August 2, 2007, Genentech, Inc. completed the acquisition of Tanox, Inc. and has taken over its rights and obligations. Novartis and Genentech/Roche are co-promoting *Xolair* in the US where Genentech/Roche records all sales. Novartis records sales outside of the US.

Novartis markets *Xolair* and records all sales and related costs in Europe as well as co-promotion costs in the US. Genentech/Roche and Novartis share the resulting profits from sales in the US, Europe and other countries, according to agreed profit-sharing percentages. Novartis recognized total sales of *Xolair* of USD 478 million (2010: USD 369 million) including sales to Genentech/Roche for the US market.

The net expense for royalties, cost sharing and profit sharing arising out of the *Lucentis* and *Xolair* agreements with Genentech/Roche totaled USD 396 million (2010: USD 300 million).

Furthermore, Novartis has several patent license, supply and distribution agreements with Roche and several Novartis entities hold Roche bonds totaling USD 20 million (2010: USD 17 million).

IDENIX

Novartis Pharma AG entered into a collaboration agreement with Idenix in May 2003 relating to the worldwide development and commercialization of drug candidates and purchased approximately 54% of the common stock of Idenix. As Novartis had the ability to exercise control, Idenix was fully consolidated. In August 2009, Novartis opted not to purchase shares that were issued pursuant to an underwritten offering and waived and amended certain rights under the development and commercialization agreement. As a result of this, the Novartis shareholding was diluted from the pre-offering level of 53% to 47% and since September 1, 2009 Idenix has been accounted for according to the equity method. Novartis has a license agreement with Idenix for *Tyzeka/Sebivo* and may pay additional license fees and development expenses for drug candidates that Novartis may elect to license from Idenix. The sales of *Tyzeka/Sebivo* totaled USD 114 million in 2011 (2010: USD 95 million).

EXECUTIVE OFFICER AND NON-EXECUTIVE DIRECTOR COMPENSATION

During 2011, there were 12 Executive Committee members and Permanent Attendees ("Executive Officers"), including those who stepped down (14 members in 2010 also including those who stepped down).

The total compensation for members of the Executive Committee and the 11 Non-Executive Directors (12 in 2010) using IFRS 2 rules for accounting for equity-based compensation was as follows:

	Executive Officers	Non-Executive Directors	Total
	2011 USD millions	2011 USD millions	2011 USD millions
Short-term benefits	13.7	23.9	37.6
Post-employment benefits	1.9	0.2	2.1
Termination benefits	5.1		5.1
Equity-based compensation	53.3	16.0	69.3
Total	74.0	40.1	114.1

The annual incentive award, which is fully included in equity-based compensation even when paid out in cash, is granted in January in the year following the reporting period.

The above table excludes amounts for any grants made to any of the current Executive Officers and non-Executive Directors by Alcon, Inc., prior to its merger into Novartis AG on April 8, 2011, since these were granted by this company's independent Compensation Committee.

The disclosures required by the Swiss Code of Obligations on Board and Executive compensation are shown in note 12 to the Novartis AG financial statements.

A non-executive director has options to acquire minor Group assets at fair market values.

28. COMMITMENTS AND CONTINGENCIES

LEASING COMMITMENTS

The Group has entered into various fixed term operational leases, mainly for cars and real estate. As of December 31, 2011 the Group's commitments with respect to these leases were as follows:

	2011 USD millions
2012	355
2013	270
2014	175
2015	124
2016	109
Thereafter	2 003
Total	**3 036**
Expense of current year	**412**

RESEARCH & DEVELOPMENT COMMITMENTS

The Group has entered into long-term research agreements with various institutions which provide for potential milestone payments and other payments by Novartis that may be capitalized. As of December 31, 2011 the Group's commitments to make payments under those agreements were as follows:

	Unconditional commitments 2011 USD millions	Potential milestone payments 2011 USD millions	Total 2011 USD millions
2012	105	282	387
2013	73	288	361
2014	53	377	430
2015	42	388	430
2016	39	172	211
Thereafter	31	1 146	1 177
Total	**343**	**2 653**	**2 996**

OTHER COMMITMENTS

The Novartis Group entered into various purchase commitments for services and materials as well as for equipment in the ordinary course of business. These commitments are generally entered into at current market prices and reflect normal business operations.

CONTINGENCIES

Group companies have to observe the laws, government orders and regulations of the country in which they operate.

The Group's potential environmental liability is assessed based on a risk assessment and investigation of the various sites identified by the Group as at risk for environmental exposure. The Group's future remediation expenses are affected by a number of uncertainties. These uncertainties include, but are not limited to, the method and extent of remediation, the percentage of material attributable to the Group at the remediation sites relative to that attributable to other parties, and the financial capabilities of the other potentially responsible parties.

A number of Group companies are currently involved in administrative proceedings, litigations and investigations arising out of the normal conduct of their business. These litigations include certain legal and product liability claims. Whilst provisions have been made for probable losses that management deems to be reasonable or appropriate there are uncertainties connected with these estimates. Note 20 contains a more extensive discussion of these matters.

In the opinion of management, however, the outcome of these actions will not materially affect the Group's financial position but could be material to the results of operations or cash flow in a given period.

29. PRINCIPAL CURRENCY TRANSLATION RATES

		2011 USD
Year-end exchange rates used for consolidated balance sheets:		
1	CHF	1.064
1	EUR	1.294
1	GBP	1.543
100	JPY	1.289

		2011 USD
Average of monthly exchange rates during the year used for consolidated income, other comprehensive income and cash flow statements:		
1	CHF	1.130
1	EUR	1.392
1	GBP	1.603
100	JPY	1.255

30. EVENTS SUBSEQUENT TO THE DECEMBER 31, 2011 BALANCE SHEET DATE

DIVIDEND PROPOSAL FOR 2011 AND APPROVAL OF THE GROUP'S 2011 CONSOLIDATED FINANCIAL STATEMENTS

On January 24, 2012, the Novartis AG Board of Directors proposed the acceptance of the 2011 consolidated financial statements of the Novartis Group for the approval by the Annual General Meeting on February 23, 2012. Furthermore, on January 19, 2012, the Board proposed a dividend of CHF 2.25 per share to be approved at the Annual General Meeting on February 23, 2012. If approved, total dividend payments would amount to approximately USD 5.8 billion.

US RESTRUCTURING

On January 13, 2012, Novartis announced a plan to restructure Novartis Pharmaceuticals (NPC) in the US. This will result in the reduction of approximately 1 960 positions and result in an exceptional charge of approximately USD 160 million to be recorded in the first quarter of 2012.

31. PRINCIPAL GROUP SUBSIDIARIES AND ASSOCIATED COMPANIES

As at December 31, 2011	Share/paid-in capital[1]	Equity interest %	Activities
Argentina			
Novartis Argentina S.A., Buenos Aires	ARS 231.3 m	100	
Alcon Laboratorios Argentina S.A., Buenos Aires	ARS 83.9 m	100	
Sandoz S.A., Buenos Aires	ARS 131.8 m	100	
Australia			
Novartis Australia Pty Ltd., North Ryde, NSW	AUD 11.0 m	100	
Novartis Pharmaceuticals Australia Pty Ltd., North Ryde, NSW	AUD 3.8 m	100	
Alcon Laboratories (Australia) Pty Ltd., Frenchs Forest	AUD 2.6 m	100	
Sandoz Pty Ltd., North Ryde, NSW	AUD 11.6 m	100	
Novartis Consumer Health Australasia Pty Ltd., Melbourne, Victoria	AUD 7.6 m	100	
Novartis Animal Health Australasia Pty Ltd., North Ryde, NSW	AUD 3.0 m	100	
Austria			
Novartis Austria GmbH, Vienna	EUR 1.0 m	100	
Novartis Pharma GmbH, Vienna	EUR 1.1 m	100	
Sandoz GmbH, Kundl	EUR 32.7 m	100	
EBEWE Pharma Ges.m.b.H Nfg., Unterach am Attersee	EUR 1.0 m	100	
Novartis Animal Health GmbH, Kundl	EUR 37 000	100	
Bangladesh			
Novartis (Bangladesh) Limited, Dhaka	BDT 162.5 m	60	
Belgium			
N.V. Novartis Pharma S.A., Vilvoorde	EUR 7.1 m	100	
S.A. Alcon-Couvreur N.V., Puurs	EUR 362.1 m	100	
N.V. CIBA Vision Benelux S.A., Mechelen	EUR 62 000	100	
N.V. Sandoz S.A., Vilvoorde	EUR 19.2 m	100	
N.V. Novartis Consumer Health S.A., Vilvoorde	EUR 4.3 m	100	
Bermuda			
Triangle International Reinsurance Ltd., Hamilton	CHF 1.0 m	100	
Novartis Securities Investment Ltd., Hamilton	CHF 30 000	100	
Novartis International Pharmaceutical Ltd., Hamilton	CHF 20 000	100	
Trinity River International Investments (Bermuda), Ltd., Hamilton	USD 12 000	100	
Trinity River Insurance Co.Ltd., Hamilton	USD 370 000	100	
Brazil			
Novartis Biociências S.A., São Paulo	BRL 255.8 m	100	
Alcon Laboratorios do Brasil Ltda., São Paulo	BRL 7.7 m	100	
Sandoz do Brasil Indústria Farmacêutica Ltda., Cambé	BRL 190.0 m	100	
Novartis Saúde Animal Ltda., São Paulo	BRL 50.7 m	100	
Canada			
Novartis Pharmaceuticals Canada Inc., Dorval/ Montreal	CAD 0[2]	100	
Alcon Canada Inc., Mississauga, Ontario	CAD 0[2]	100	
CIBA Vision Canada Inc., Mississauga, Ontario	CAD 1	100	
Sandoz Canada Inc., Boucherville, Quebec	CAD 76.8 m	100	
Novartis Consumer Health Canada Inc., Mississauga, Ontario	CAD 2	100	
Novartis Animal Health Canada Inc., Charlottetown, Prince Edward Island	CAD 2	100	
Chile			
Novartis Chile S.A., Santiago de Chile	CLP 2.0 bn	100	
Alcon Laboratorios Chile Limitada, Santiago de Chile	CLP 2.0 bn	100	
China			
Beijing Novartis Pharma Co., Ltd., Beijing	USD 30.0 m	100	
Novartis Pharmaceuticals (HK) Limited, Hong Kong	HKD 200	100	
China Novartis Institutes for BioMedical Research Co., Ltd., Shanghai	USD 108.0 m	100	
Suzhou Novartis Pharma Technology Co. Ltd., Changshu	USD 97.4 m	100	
Shanghai Novartis Trading Ltd., Shanghai	USD 2.45 m	100	
Alcon (China) Ophthalmic Product Co., Ltd., Beijing	USD 2.2 m	100	
Sandoz (China) Pharmaceutical Co., Ltd., Zhongshan	USD 22.0 m	100	
Novartis Vaccines and Diagnostics (HK) Ltd., Hong Kong	HKD 80.0 m	100	
Zhejiang Tianyuan Bio-Pharmaceutical Co., Ltd., Hangzhou	CNY 46.8 m	85	
Shanghai Novartis Animal Health Co., Ltd., Shanghai	CHF 21.5 m	87	
Colombia			
Novartis de Colombia S.A., Santafé de Bogotá	COP 7.9 bn	100	
Laboratorios Alcon de Colombia S.A., Bogotá	COP 20.9 m	100	
Croatia			
Sandoz d.o.o., Zagreb	HRK 25.6 m	100	
Czech Republic			
Novartis s.r.o., Prague	CZK 51.5 m	100	
Sandoz s.r.o., Prague	CZK 44.7 m	100	
Denmark			
Novartis Healthcare A/S, Copenhagen	DKK 14.0 m	100	
Sandoz A/S, Copenhagen	DKK 8.0 m	100	
Ecuador			
Novartis Ecuador S.A., Quito	USD 4.0 m	100	
Egypt			
Novartis Pharma S.A.E., Cairo	EGP 33.8 m	99	
Finland			
Novartis Finland Oy, Espoo	EUR 459 000	100	
France			
Novartis Groupe France S.A., Rueil-Malmaison	EUR 103.0 m	100	
Novartis Pharma S.A.S., Rueil-Malmaison	EUR 43.4 m	100	
Laboratoires Alcon S.A., Rueil-Malmaison	EUR 12.6 m	100	
CIBA Vision S.A.S., Blagnac	EUR 1.8 m	100	
Sandoz S.A.S., Levallois-Perret	EUR 5.0 m	100	
Novartis Vaccines and Diagnostics S.A.S., Suresnes	EUR 1.5 m	100	
Novartis Santé Familiale S.A.S., Rueil-Malmaison	EUR 21.9 m	100	
Novartis Santé Animale S.A.S., Rueil-Malmaison	EUR 900 000	100	
Germany			
Novartis Deutschland GmbH, Wehr	EUR 155.5 m	100	
Novartis Pharma GmbH, Nuremberg	EUR 25.6 m	100	
Novartis Pharma Produktions GmbH, Wehr	EUR 2.0 m	100	
Alcon Pharma GmbH, Freiburg	EUR 511 292	100	
WaveLight GmbH, Erlangen	EUR 6.6 m	100	
CIBA Vision GmbH, Grosswallstadt	EUR 15.4 m	100	
CIBA Vision Vertriebs GmbH, Grossostheim	EUR 2.6 m	100	
Sandoz International GmbH, Holzkirchen	EUR 100 000	100	
Sandoz Pharmaceuticals GmbH, Holzkirchen	EUR 5.1 m	100	
Sandoz Industrial Products GmbH, Frankfurt a. M.	EUR 2.6 m	100	
1 A Pharma GmbH, Oberhaching	EUR 26 000	100	
Salutas Pharma GmbH, Barleben	EUR 42.1 m	100	
Hexal AG, Holzkirchen	EUR 93.7 m	100	
Novartis Vaccines and Diagnostics GmbH, Marburg	EUR 5.0 m	100	
Novartis Vaccines Vertriebs GmbH, Marburg	EUR 25 564	100	
Novartis Consumer Health GmbH, Munich	EUR 14.6 m	100	
Novartis Tiergesundheit GmbH, Munich	EUR 256 000	100	
LTS Lohmann Therapie-Systeme AG, Andernach	EUR 31.2 m	43	
Gibraltar			
Novista Insurance Limited, Gibraltar	CHF 130.0 m	100	
Great Britain			
Novartis UK Limited, Frimley/Camberley	GBP 25.5 m	100	
Novartis Pharmaceuticals UK Limited, Frimley/ Camberley	GBP 5.4 m	100	
Novartis Grimsby Limited, Frimley/Camberley	GBP 230 m	100	
Alcon Laboratories (UK) Limited, Hemel Hempstead	GBP 9.1 m	100	
CIBA Vision (UK) Limited, Southampton	GBP 550 000	100	
Sandoz Limited, Bordon	GBP 2.0 m	100	
Novartis Vaccines and Diagnostics Limited, Frimley/Camberley	GBP 100	100	
Novartis Consumer Health UK Limited, Horsham	GBP 25 000	100	
Novartis Animal Health UK Limited, Frimley/ Camberley	GBP 100 000	100	
Greece			
Novartis (Hellas) S.A.C.I., Metamorphosis/Athens	EUR 14.6 m	100	
Alcon Laboratories Hellas Commercial & Industrial S.A., Maroussi/Athens	EUR 4.7 m	100	
Hungary			
Novartis Hungary Healthcare Limited Liability Company, Budapest	HUF 545.6 m	100	
Sandoz Hungary Limited Liability Company, Budapest	HUF 883.0 m	100	
India			
Novartis India Limited, Mumbai	INR 159.8 m	76	
Novartis Healthcare Private Limited, Mumbai	INR 60.0 m	100	
Alcon Laboratories (India) Private Limited, Bangalore	INR 1.1 bn	100	
Sandoz Private Limited, Mumbai	INR 32.0 m	100	

31. PRINCIPAL GROUP SUBSIDIARIES AND ASSOCIATED COMPANIES (CONTINUED)

As at December 31, 2011	Share/paid-in capital[1]	Equity interest %	Activities
Indonesia			
PT Novartis Indonesia, Jakarta	IDR 7.7 bn	100	
PT CIBA Vision Batam, Batam	IDR 11.9 bn	100	
Ireland			
Novartis Ireland Limited, Dublin	EUR 25 000	100	
Novartis Ringaskiddy Limited, Ringaskiddy, County Cork	EUR 2.0 m	100	
Alcon Laboratories Ireland Limited, Cork	EUR 541 251	100	
Italy			
Novartis Farma S.p.A., Origgio	EUR 18.2 m	100	
Alcon Italia S.p.A., Milan	EUR 1.3 m	100	
CIBA Vision S.r.l., Marcon	EUR 2.4 m	100	
Sandoz S.p.A., Origgio	EUR 679 900	100	
Sandoz Industrial Products S.p.A., Rovereto	EUR 2.6 m	100	
Novartis Vaccines and Diagnostics S.r.l., Siena	EUR 41.5 m	100	
Novartis Consumer Health S.p.A., Origgio	EUR 2.9 m	100	
Japan			
Novartis Holding Japan K.K., Tokyo	JPY 10.0 m	100	
Novartis Pharma K.K., Tokyo	JPY 6.0 bn	100	
Alcon Japan Ltd., Tokyo	JPY 500.0 m	100	
CIBA Vision K.K., Tokyo	JPY 100.0 m	100	
Sandoz K.K., Tokyo	JPY 100.0 m	100	
Novartis Animal Health K.K., Tokyo	JPY 50.0 m	100	
Luxembourg			
Novartis Investments S.à r.l., Luxembourg City	USD 2.6 bn	100	
Novartis Finance S.A., Luxembourg City	USD 100 000	100	
Malaysia			
Novartis Corporation (Malaysia) Sdn. Bhd., Kuala Lumpur	MYR 3.3 m	100	
CIBA Vision Johor Sdn. Bhd., Gelang Patah	MYR 5.0 m	100	
Mexico			
Novartis Farmacéutica, S.A. de C.V., Mexico City	MXN 205.0 m	100	
Alcon Laboratorios, S.A. de C.V., Mexico City	MXN 5.9 m	100	
Sandoz S.A. de C.V., Mexico City	MXN 468.2 m	100	
Netherlands			
Novartis Netherlands B.V., Arnhem	EUR 1.4 m	100	
Novartis Pharma B.V., Arnhem	EUR 4.5 m	100	
Alcon Nederland B.V., Gorinchem	EUR 18 151	100	
Sandoz B.V., Almere	EUR 907 570	100	
Novartis Consumer Health B.V., Breda	EUR 23 830	100	
New Zealand			
Novartis New Zealand Ltd., Auckland	NZD 820 000	100	
Norway			
Novartis Norge AS, Oslo	NOK 1.5 m	100	
Pakistan			
Novartis Pharma (Pakistan) Limited, Karachi	PKR 24.8 m	99	
Panama			
Novartis Pharma (Logistics), Inc., Panama City	USD 10 000	100	
Peru			
Novartis Biosciences Peru S.A., Lima	PEN 6.1 m	100	
Philippines			
Novartis Healthcare Philippines, Inc., Makati/Manila	PHP 298.8 m	100	
Poland			
Novartis Poland Sp. z o.o., Warszawa	PLN 44.2 m	100	
Alcon Polska Sp. z o.o., Warszawa	PLN 750 000	100	
Sandoz Polska Sp. z o.o., Warszawa	PLN 25.6 m	100	
Lek S.A., Strykow	PLN 11.4 m	100	
Portugal			
Novartis Portugal SGPS Lda., Sintra	EUR 500 000	100	
Novartis Farma-Produtos Farmacêuticos S.A., Sintra	EUR 2.4 m	100	
Alcon Portugal-Produtos e Equipamentos Oftalmologicos Lda., Paco d'Arcos	EUR 4.1 m	100	
Sandoz Farmaceutica Lda., Sintra	EUR 5.0 m	100	
Novartis Consumer Health-Produtos Farmacêuticos e Nutrição Lda., Lisbon	EUR 100 000	100	
Puerto Rico			
Ex-Lax, Inc., Humacao	USD 10 000	100	
Alcon (Puerto Rico) Inc., Catano	USD 100	100	
CIBA Vision Puerto Rico, Inc., Cidra	USD 1 000	100	

As at December 31, 2011	Share/paid-in capital[1]	Equity interest %	Activities
Romania			
Sandoz S.R.L., Targu-Mures	RON 105.2 m	100	
Russian Federation			
Novartis Pharma LLC, Moscow	RUR 20.0 m	100	
Alcon Farmacevtika LLC, Moscow	RUR 44.1 m	100	
ZAO Sandoz, Moscow	RUR 57.4 m	100	
Novartis Neva LLC, St. Petersburg	RUR 250.0 m	100	
Novartis Consumer Health LLC, Moscow	RUR 80.0 m	100	
Saudi Arabia			
Saudi Pharmaceutical Distribution Co. Ltd., Riyadh	SAR 26.8 m	75	
Singapore			
Novartis (Singapore) Pte Ltd, Singapore	SGD 100 000	100	
Novartis Singapore Pharmaceutical Manufacturing Pte Ltd., Singapore	SGD 45.0 m	100	
Novartis Asia Pacific Pharmaceuticals Pte Ltd., Singapore	SGD 1.0 m	100	
Novartis Institute for Tropical Diseases Pte Ltd., Singapore	SGD 2 004	100	
Alcon Singapore Manufacturing Pte Ltd., Singapore	SGD 101 000	100	
CIBA Vision (Singapore) Pte Ltd, Singapore	SGD 400 000	100	
CIBA Vision Asian Manufacturing and Logistics Pte Ltd., Singapore	SGD 1.0 m	100	
Slovakia			
Novartis Slovakia s.r.o., Bratislava	EUR 2.0 m	100	
Slovenia			
Lek Pharmaceuticals d.d., Ljubljana	EUR 48.4 m	100	
Sandoz Pharmaceuticals d.d., Ljubljana	EUR 1.5 m	100	
South Africa			
Novartis South Africa (Pty) Ltd., Kempton Park	ZAR 86.3 m	100	
Alcon Laboratories (South Africa) (Pty) Ltd., Bryanston, Gauteng	ZAR 201 820	100	
Sandoz South Africa (Pty) Ltd, Kempton Park	ZAR 3.0 m	100	
South Korea			
Novartis Korea Ltd., Seoul	KRW 24.5 bn	99	
Alcon Korea Ltd, Seoul	KRW 33.8 bn	100	
Spain			
Novartis Farmacéutica, S.A., Barcelona	EUR 63.0 m	100	
Alcon Cusi S.A., El Masnou	EUR 11.6 m	100	
CIBA Vision, S.A., Barcelona	EUR 1.4 m	100	
Sandoz Farmacéutica, S.A., Madrid	EUR 270 450	100	
Sandoz Industrial Products, S.A., Les Franqueses del Vallés/Barcelona	EUR 9.3 m	100	
Bexal Farmacéutica, S.A., Madrid	EUR 1.0 m	100	
Novartis Vaccines and Diagnostics, S.L., Barcelona	EUR 675 450	100	
Novartis Consumer Health, S.A., Barcelona	EUR 876 919	100	
Sweden			
Novartis Sverige Participations AB, Täby/Stockholm	SEK 1.0 m	100	
Novartis Sverige AB, Täby/Stockholm	SEK 5.0 m	100	
Alcon Sverige AB, Bromma	SEK 100 000	100	
CIBA Vision Nordic AB, Askim/Göteborg	SEK 2.5 m	100	
Switzerland			
Novartis International AG, Basel	CHF 10.0 m	100	
Novartis Holding AG, Basel	CHF 100.2 m	100	
Novartis Research Foundation, Basel	CHF 29.3 m	100	
Novartis Foundation for Management Development, Basel	CHF 100 000	100	
Novartis Foundation for Employee Participation, Basel	CHF 100 000	100	
Novartis Sanierungsstiftung, Basel	CHF 2.0 m	100	
Novartis Pharma AG, Basel	CHF 350.0 m	100	
Novartis Pharma Services AG, Basel	CHF 20.0 m	100	
Novartis Pharma Schweizerhalle AG, Muttenz	CHF 18.9 m	100	
Novartis Pharma Stein AG, Stein	CHF 251 000	100	
Novartis Pharma Schweiz AG, Bern	CHF 5.0 m	100	
Alcon Switzerland SA, Hünenberg	CHF 100 000	100	
Alcon Pharmaceuticals Ltd., Fribourg	CHF 200 000	100	
ESBATech, an Alcon Biomedical Research Unit GmbH, Schlieren	CHF 14.0 m	100	
CIBA Vision AG, Embrach	CHF 300 000	100	
Sandoz AG, Basel	CHF 5.0 m	100	
Sandoz Pharmaceuticals AG, Steinhausen	CHF 100 000	100	
Novartis Vaccines and Diagnostics AG, Basel	CHF 800 000	100	

As at December 31, 2011	Share/paid-in capital [1]	Equity interest %	Activities
Switzerland (continued)			
Novartis Vaccines and Diagnostics Services AG, Basel	CHF 100 000	100	■▼
Novartis Consumer Health S.A., Nyon	CHF 30.0 m	100	■◆▼▲
Novartis Consumer Health Schweiz AG, Bern	CHF 250 000	100	◆
Novartis Animal Health AG, Basel	CHF 101 000	100	■◆▼▲
Novartis Centre de Recherche Santé Animale S.A., St. Aubin	CHF 250 000	100	▲
Roche Holding AG, Basel	CHF 160.0 m	33/6 [3]	■
Taiwan			
Novartis (Taiwan) Co., Ltd., Taipei	TWD 170.0 m	100	◆▼
Thailand			
Novartis (Thailand) Limited, Bangkok	THB 230.0 m	100	◆
Alcon Laboratories (Thailand) Ltd., Bangkok	THB 2.1 m	100	◆
Turkey			
Novartis Saglik, Gida ve Tarim Ürünleri Sanayi ve Ticaret A.S., Istanbul	TRY 98.0 m	100	◆▼
Alcon Laboratuvarlari Ticaret A.S., Istanbul	TRY 25.2 m	100	◆
Sandoz Ilaç Sanayi ve Ticaret A.S., Istanbul	TRY 120.0 m	100	◆▼
USA			
Novartis Corporation, East Hanover, NJ	USD 72.2 m	100	■
Novartis Finance Corporation, New York, NY	USD 1.7 bn	100	■
Novartis Capital Corporation, New York, NY	USD 1	100	■
Novartis Pharmaceuticals Corporation, East Hanover, NJ	USD 5.2 m	100	◆▼▲
Novartis Institutes for BioMedical Research, Inc., Cambridge, MA	USD 1	100	▲
Novartis Institute for Functional Genomics, Inc., San Diego, CA	USD 21 000	100	▲
Genoptix, Inc., Carlsbad, CA	USD 1	100	◆▲
Alcon Laboratories, Inc., Wilmington, DE	USD 1 000	100	■◆▼
Alcon Refractive Horizons, LLC, Wilmington, DE	USD 10	100	▼
Alcon Research, Ltd., Wilmington, DE	USD 10	100	▼▲
Alcon LenSx, Inc., Wilmington, DE	USD 100	100	▼
CIBA Vision Corporation, Duluth, GA	USD 301.3 m	100	■◆▼▲
Sandoz Inc., Princeton, NJ	USD 25 000	100	◆▼▲

As at December 31, 2011	Share/paid-in capital [1]	Equity interest %	Activities
USA (continued)			
Eon Labs, Inc., Princeton, NJ	USD 1	100	◆▼
Falcon Pharmaceuticals, Ltd., Wilmington, DE	USD 10	100	◆
Novartis Vaccines and Diagnostics, Inc., Cambridge, MA	USD 3	100	■◆▼▲
Novartis Consumer Health, Inc., Parsippany, NJ	USD 0 [2]	100	◆▼▲
Novartis Animal Health US, Inc., Greensboro, NC	USD 100	100	◆▼▲
Idenix Pharmaceuticals, Inc., Cambridge, MA	USD 72 863	31	■
Venezuela			
Novartis de Venezuela, S.A., Caracas	VEF 1.4 m	100	◆
Alcon Pharmaceutical, C.A., Caracas	VEF 5.5 m	100	◆

In addition, the Group is represented by subsidiaries, associated companies or joint ventures in the following countries: Algeria, Bosnia/Herzegovina, Bulgaria, Cayman Islands, Costa Rica, Dominican Republic, Guatemala, the Former Yugoslav Republic of Macedonia, Morocco, Ukraine and Uruguay.

Equity interest % – above 50% and up to 100% of the voting rights – fully consolidated
– above 20% and up to 50% of the voting rights – investment in associated company – equity method accounting

[1] Share/paid-in capital may not reflect the taxable share/paid-in capital amount and does not include any paid-in surplus.
[2] shares without par value
[3] Approximately 33% of voting shares; approximately 6% of total net income and equity attributable to Novartis
m = million; bn = billion

The following describe the various types of entities within the Group:
■ Holding/Finance: This entity is a holding company and/or performs finance functions for the Group.
◆ Sales: This entity performs sales and marketing activities for the Group.
▼ Production: This entity performs manufacturing and/or production activities for the Group.
▲ Research: This entity performs research and development activities for the Group.

32. RISK ASSESSMENT DISCLOSURES REQUIRED BY SWISS LAW

The Risk Committee of the Board ensures the Group has implemented an appropriate and effective risk management system and process. It reviews with management and internal audit the identification, prioritization and management of the risks, the accountabilities and roles of the functions involved with risk management, the risk portfolio and the related actions implemented by management. The Risk Committee informs the Board of Directors on a periodic basis.

The Corporate Risk Management function coordinates and aligns the risk management processes, and reports to the Risk Committee on a regular basis on risk assessment and risk management. Organizational and process measures have been designed to identify and mitigate risks at an early stage. Organizationally, the responsibility for risk assessment and management is allocated to the Divisions, with specialized Corporate Functions such as Financial Reporting & Accounting, Treasury, Group Quality Operations, Corporate Health, Safety and Environment, and Business Continuity providing support and controlling the effectiveness of the risk management by the Divisions.

Financial risk management is described in more detail in Note 16 to the Group's consolidated financial statements.

REPORT OF THE STATUTORY AUDITOR ON THE CONSOLIDATED FINANCIAL STATEMENTS OF NOVARTIS AG AND INTERNAL CONTROL OVER FINANCIAL REPORTING

TO THE GENERAL MEETING OF NOVARTIS AG, BASEL

REPORT OF THE STATUTORY AUDITOR ON THE CONSOLIDATED FINANCIAL STATEMENTS OF NOVARTIS AG

As statutory auditor, we have audited the consolidated financial statements of Novartis AG and its consolidated subsidiaries ("Novartis Group"), which comprise the consolidated income statements, consolidated statements of comprehensive income, consolidated statements of changes in equity, consolidated balance sheets, consolidated cash flow statements and notes (pages 190 to 258) for the year ended December 31, 2011.

Board of Directors' Responsibility

The Board of Directors is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Financial Reporting Standards (IFRS) and the requirements of Swiss law. This responsibility includes designing, implementing and maintaining an internal control system relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error. The Board of Directors is further responsible for selecting and applying appropriate accounting policies and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with Swiss law, Swiss Auditing Standards, International Standards on Auditing and the standards of the Public Company Accounting Oversight Board of the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers the internal control system relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of accounting estimates made, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements for the year ended December 31, 2011 present fairly, in all material respects, the financial position, the results of operations and the cash flows in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board and comply with Swiss law.

REPORT ON OTHER LEGAL REQUIREMENTS

We confirm that we meet the legal requirements on licensing according to the Auditor Oversight Act (AOA) and independence (article 728 CO and article 11 AOA) and that there are no circumstances incompatible with our independence.

In accordance with article 728a paragraph 1 item 3 CO and Swiss Auditing Standard 890, we confirm that an internal control system exists which has been designed for the preparation of consolidated financial statements according to the instructions of the Board of Directors.

We recommend that the consolidated financial statements submitted to you be approved.

REPORT ON THE EFFECTIVENESS OF INTERNAL CONTROL OVER FINANCIAL REPORTING

We have also audited the effectiveness of Novartis Group's internal control over financial reporting as of December 31, 2011, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

The Board of Directors and management of Novartis Group are responsible for maintaining effective internal control over financial reporting and management is responsible for the assessment of the effectiveness of internal control over financial reporting included in the accompanying *Report of Novartis Management on Internal Control Over Financial Reporting* in this financial report on page 259. Our responsibility is to express an opinion on the effectiveness of Novartis Group's internal control over financial reporting based on our integrated audit.

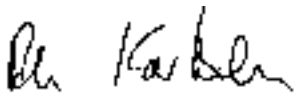
We conducted our audit of internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board of the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. An audit of internal control over financial reporting includes obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also includes performing such other procedures as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with the applicable accounting standards. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with the applicable accounting standards, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Novartis Group maintained, in all material respects, effective internal control over financial reporting as of December 31, 2011, based on criteria established in *Internal Control – Integrated Framework* issued by the COSO.

PricewaterhouseCoopers AG



Peter M. Kartscher
Audit expert
Auditor in charge

Michael P. Nelligan
Global relationship partner

Basel, January 24, 2012

INCOME STATEMENTS

(For the years ended December 31, 2011 and 2010)

	Note	2011 CHF millions
Income		
Income from financial assets		5 284
Gain from disposal of intangible assets		356
License fees		1 419
Other income		4
Total income		7 063
Expenses		
Financial expense		– 326
Administrative expenses		– 21
Amortization of intangible assets	3	– 1 153
Other expenses		– 69
Taxes		– 123
Total expenses		– 1 692
Net income		5 371

The notes form an integral part of these unconsolidated financial statements.

BALANCE SHEETS (PRIOR TO PROFIT APPROPRIATION)
(At December 31, 2011 and 2010)

	Note	2011 CHF millions
Assets		
Non-current assets		
Goodwill and other intangible assets	3	21 407
Financial assets-subsidiaries and associated companies	4	20 881
Total non-current assets		**42 288**
Current assets		
Receivables		
– subsidiaries		9 428
– others		46
Marketable securities	5	2 183
Total current assets		**11 657**
Total assets		**53 945**
Equity and liabilities		
Equity		
Total share capital	6	1 373
Reserves		
Legal reserves	7	
– General reserve		320
– Capital contribution reserve		198
– Reserve for treasury shares		5 744
Free reserves	8	39 271
Total reserves		**45 533**
Unappropriated earnings		
Net income of the year		5 371
Total unappropriated earnings		**5 371**
Total equity		**52 277**
Liabilities		
Bonds	9	794
Provisions		534
Accounts payable and accrued liabilities		
– subsidiaries		116
– others		224
Total liabilities		**1 668**
Total equity and liabilities		**53 945**

The notes form an integral part of these unconsolidated financial statements.

1. INTRODUCTION

The financial statements of Novartis AG comply with the requirements of the Swiss law for companies, the Code of Obligations (SCO).

2. ACCOUNTING POLICIES

EXCHANGE RATE DIFFERENCES

Current assets and current liabilities denominated in foreign currencies are converted at year end exchange rates. Realized exchange gains and losses as well as all unrealized exchange losses arising from these as well as those from business transactions are recorded in the income statement.

GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill and other intangible assets are capitalized and amortized over a period of between five and twenty years. Goodwill and other intangible assets are reviewed for impairment on a yearly basis. If necessary an impairment loss is recognized.

FINANCIAL ASSETS

These are valued at acquisition cost less adjustments for foreign currency losses and any other impairment of value.

MARKETABLE SECURITIES

These are valued at the lower of cost and market value.

BONDS

These are valued on an amortized cost basis such that additional interest is accrued over the duration of the bonds so that at maturity the balance sheet amount will equal the amount that is due to be paid.

PROVISIONS

Provisions are made to cover general business risks of the Group.

3. GOODWILL AND OTHER INTANGIBLE ASSETS

At the Extraordinary General Meeting (EGM) on April 8, 2011 Novartis AG shareholders approved the retrospective merger as of January 1, 2011 of Novartis AG with Alcon, Inc. which was a Swiss company. Based on the EGM approval and on the merger agreement, Alcon, Inc. assets and liabilities have been integrated into Novartis AG at book value.

	2011 CHF millions
Goodwill	
Cost	
January 1	
Arising on Alcon, Inc. merger with Novartis AG	39 101
Disposal as a result of a Novartis Group internal legal company reorganization	– 16 717
December 31	22 384
Accumulated amortization	
January 1	
Amortization charges	– 1 140
December 31	– 1 140
Net book value at December 31	21 244
Other intangible assets	
Cost	
January 1 and December 31	242
Accumulated amortization	
January 1	– 66
Amortization charges	– 13
December 31	– 79
Net book value at December 31	163
Goodwill and other intangible assets	
Net book value at December 31	21 407

4. FINANCIAL ASSETS

Included in financial assets are CHF 14 412 million (2010: CHF 50 135 million) of investments in subsidiaries and associated companies and CHF 6 469 million (2010: CHF 284 million) of loans to subsidiaries.

The principal direct and indirect subsidiaries and other holdings of Novartis AG are shown in note 31 to the Group's consolidated financial statements.

5. MARKETABLE SECURITIES

Included in marketable securities are Novartis AG treasury shares with a net book value of CHF 2 108 million (2010: CHF 54 million) (see notes 6 and 7 below). This position includes time deposits of CHF 72 million (2010: CHF nil) to cover a guarantee and so it is restricted in its use.

6. SHARE CAPITAL

Number of shares	Movement in year	Dec 31, 2011
Total Novartis AG shares	108 000 000	2 745 623 000
Treasury shares		
Treasury shares held by Novartis AG	17 250 542	– 90 737 458
Treasury shares held by subsidiaries	– 8 541 945	– 67 435 782
Total treasury shares	8 708 597	– 158 173 240

The Novartis AG share capital consists of registered shares with a nominal value of CHF 0.50 each.

The number of issued shares increased by 108 million during the year to 2 745.6 million at December 31, 2011 as a result of shares exchanged for acquiring the remaining outstanding interests in Alcon Inc. approved at the Extraordinary General Meeting on April 8, 2011. This increased the amount of the issued share capital by CHF 54.0 million to CHF 1 372.8 million at December 31, 2011.

During 2010 the Novartis AG share capital was unchanged.

Treasury share purchases during 2011 totaled 60.1 million (2010: 0.7 million) with an average purchase price of CHF 52 (2010: CHF 60), treasury share sales totaled 5.3 million (2010: 2.9 million) with an average sale price of CHF 51 (2010: CHF 56), share-based compensation transactions totaled 6.8 million shares (2010: 6.3 million shares) respectively and treasury shares used for the Alcon merger totaled 164.7 million (108.0 million shares issued on April 8, 2011 plus 56.7 million shares already held as treasury shares).

The number of treasury shares held by the Company and subsidiaries meet the definitions and requirements of Art. 659b SCO.

Out of the 158 173 240 treasury shares held at December 31, 2011, 146 273 240 are non-dividend bearing with the balance held for share-based compensation and being dividend bearing. It should be noted that the Novartis Group's consolidated financial statements comply with IFRS. This requires consolidation of entities, mainly foundations, which do not qualify as subsidiaries in the sense of Article 659b SCO.

7. LEGAL RESERVES

GENERAL RESERVE

	2011 CHF millions
January 1 and December 31	320

CAPITAL CONTRIBUTION RESERVE

	2011 CHF millions
January 1	
Created as a result of Alcon, Inc. merger with Novartis AG	198
December 31	198

RESERVE FOR TREASURY SHARES HELD BY THE GROUP

	2011 CHF millions
January 1	3 374
Transfer from/to free reserves	2 370
December 31	5 744

The general reserve must be accumulated until it is at least 20% of the share capital of Novartis AG in order to comply with the SCO.

Novartis AG has met the legal requirements for legal reserves under Articles 659 et. seq. and 663b.10 SCO for the treasury shares detailed in note 5.

8. FREE RESERVES

	2011 CHF millions
January 1	40 065
Transfer from unappropriated earnings	1 576
Transfer to/from reserve for treasury shares	– 2 370
December 31	39 271

9. CHF 800 MILLION BONDS 3.625% 2008/2015

On June 26, 2008 Novartis AG issued CHF 800 million of bonds bearing interest at 3.625% per annum and due on June 26, 2015. The bonds were issued at 100.35% and proceeds received after deducting related costs amounted to CHF 787.9 million. The bonds are valued on an amortized cost basis.

10. CONTINGENT LIABILITIES

	Outstanding liabilities Dec 31, 2011 CHF millions
Guarantees in favor of subsidiaries to cover capital and interest of bonds and commercial paper program – total maximum amount CHF 24 486 million (2010: CHF 24 353 million)	13 950
Other guarantees in favor of subsidiaries, associated companies and others – total maximum amount CHF 2 989 million (2010: CHF 2 643 million)	1 711
Total	15 661

11. REGISTRATION, VOTING RESTRICTIONS AND MAJOR SHAREHOLDERS

The Company's Articles of Incorporation state that no person or entity shall be registered with the right to vote for more than 2% of the share capital as set forth in the Commercial Register. In particular cases the Board of Directors may allow exemptions from the limitation for registration in the share register.

According to the share register, shareholders owning 2% or more of the Company's capital at December 31, excluding Novartis AG together with Novartis subsidiaries holding treasury shares, are as follows:

	% holding of share capital December 31, 2011
Novartis Foundation for Employee Participation, Basel, Switzerland	4.1
Emasan AG, Basel, Switzerland	3.2

In addition:
Shareholders registered as nominees:
– JPMorgan Chase Bank, New York, US, holds 10.9% (2010: 10.7%)
– Nortrust Nominees, London, GB, holds 3.2% (2010: 2.8%)
– Mellon Bank, Everett, Massachusetts, US, holds 3.0% (2010: 2.9%)

Shareholder acting as American Depositary Share (ADS) depositary:
– JPMorgan Chase Bank, New York, US, holds 11.0% (2010: 9.6%)

Shareholder according to a disclosure notification filed with Novartis AG and the SIX Swiss Exchange:
– Capital Group Companies, Inc., Los Angeles, US, holds between 3% and 5%.

12. BOARD AND EXECUTIVE COMPENSATION DISCLOSURES

Novartis AG's financial statements have been prepared in accordance with the requirements of Swiss company law, the Swiss Code of Obligations (SCO). This note therefore differs in certain significant respects from compensation disclosures in note 27 to the Group's consolidated financial statements, which have been prepared in accordance with International Financial Reporting Standards (IFRS), mainly due to different expense recognition rules being applied.

12.1) COMPENSATION OF BOARD MEMBERS

GENERAL PRINCIPLES

The compensation of the Chairman is based on a contract, which provides for Dr. Daniel Vasella a fixed remuneration of CHF 12.2 million, indexed to the average compensation increase for associates based in Switzerland. One third of his total compensation is paid out in monthly cash installments; the remaining two-thirds are in the form of unrestricted Novartis shares that are granted to him each year at the closing market price of the underlying share at the end of the day at grant date, in 2011 on January 19, 2011. Following his term as Chairman, Dr. Vasella agreed to continue to make available his know-how to Novartis and to refrain from activities that compete with any business of Novartis for a multi-year period. Dr. Vasella will receive fair market compensation in return for his services and for complying with the restriction not to compete. Dr. Vasella carries forward tradable options, shares and benefits (including pension) as a result of his 14-year tenure as the CEO of Novartis. In his current capacity he receives no variable compensation, tradable options or equity other than the shares that are part of his retainer as Chairman.

The other members of the Board of Directors receive an annual fixed Board membership fee and additional fees for committee chairmanships, committee memberships, and other functions to compensate for their increased responsibilities and engagements. They do not receive additional fees for attending meetings. With the exception of the Chairman, the members of the Board of Directors can choose to receive their fees in cash, shares, or a combination of both and they receive neither share options nor pension benefits.

The Board of Directors determines the compensation of the other Board members each year, based on a proposal by the Compensation Committee.

The fee rates for Board membership and functional roles of other members of the Board of Directors are as follows:

BOARD MEMBER ANNUAL FEE RATES (EXCL. CHAIRMAN)

	Annual fee (CHF)
Board membership	350 000
Vice Chairman	350 000
Board Committee chairmanship	10 000
Chairman's Committee membership	150 000
Audit and Compliance Committee membership	100 000
Risk Committee membership	50 000
Compensation Committee membership	50 000
Corporate Governance and Nomination Committee membership	50 000
Delegated board membership[1]	125 000

[1] The Board of Directors has delegated Rolf M. Zinkernagel to the Scientific Advisory Board of the Novartis Institute for Tropical Diseases (NITD). The Board of Directors has delegated both Rolf M. Zinkernagel and William Brody to the Board of Directors of the Genomics Institute of the Novartis Research Foundation (GNF).

COMPENSATION IN 2011 AND 2010

The following compensation tables disclose the compensation granted to Board members in 2011 with comparatives to 2010.

BOARD MEMBER COMPENSATION IN 2011 (MARKET VALUE)[1]

	Board membership	Vice Chairman	Chairman's Committee	Audit and Compliance Committee	Risk Committee	Compensation Committee	Corporate Governance and Nomination Committee	Delegated board membership	Annual cash compensation (CHF) (A)	Shares (Market value) (CHF) (B)[2]	Shares (Number)	Other (CHF) (C)	Total (CHF) (A)+(B)+(C)
Daniel Vasella	Chair			• [3]	• [3]	• [3]	• [3]		4 060 004	8 786 735 [4]	160 635 [4]	654 207 [5]	13 500 946 [7]
Ulrich Lehner	•	•	•	•	•	•	Chair		1 110 000	–	–	62 650 [6]	1 172 650
William Brody [8]	•					•		•	229 688	295 325	5 399	–	525 013
Srikant Datar	•		•	Chair	•	•			550 250	159 779	2 921	–	710 029
Ann Fudge	•				•		•		450 000	–	–	–	450 000
Pierre Landolt [9]	•						•		106 000	294 013	5 375	24 177 [6]	424 190
Enrico Vanni	•			•		•			425 000	75 048	1 372	29 404 [6]	529 452 [7]
Andreas von Planta	•			•	Chair		•		448 000	112 026	2 048	32 685 [6]	592 711
Wendelin Wiedeking	•			•	•				132 500	367 529	6 719	30 965 [6]	530 994
Marjorie M.T. Yang	•					Chair			410 000	–	–	24 719 [6]	434 719
Rolf M. Zinkernagel [10]	•						•	•	–	650 000	11 883	34 381 [6]	684 381
Total [11]									**7 921 442**	**10 740 454**	**196 352**	**893 188**	**19 555 084**

[1] Does not include reimbursement for travel and other necessary business expenses incurred in the performance of their services as these are not compensation.
[2] The value of the shares reflected in this column has been calculated based on market value of the shares at grant date. All shares were granted as per January 19, 2011 against the prevailing share price of CHF 54.70.
[3] Daniel Vasella attended the meetings of these Committees as a guest without voting rights.
[4] Includes 12 188 shares paid in 2011 related to the grant of 2010.
[5] Includes social security costs due by the individual and paid by the company, pension and life insurance.
[6] Includes social security costs due by the individual and paid by the company.
[7] Does not include Board member compensation granted by Alcon, Inc. until April 8, 2011.
[8] The Board of Directors has delegated William Brody to the Board of Directors of the Genomics Institute of the Novartis Research Foundation (GNF).
[9] According to Pierre Landolt, the Sandoz Family Foundation is the economic beneficiary of the compensation.
[10] The Board of Directors has delegated Rolf M. Zinkernagel to the Scientific Advisory Board of the Novartis Institute for Tropical Diseases (NITD) and to the Board of Directors of the Genomics Institute of the Novartis Research Foundation (GNF).
[11] Alexandre F. Jetzer-Chung and Hans-Jörg Rudloff were members of the Board of Directors until February 22, 2011. Their compensation was reported in the 2010 Annual Report.

BOARD MEMBER COMPENSATION IN 2010 (MARKET VALUE)[1]

Daniel Vasella

Ulrich Lehner

Hans-Joerg Rudloff

William Brody[5]

Srikant Datar

Ann Fudge

Alexandre F. Jetzer-Chung[6]

Pierre Landolt[7]

Andreas von Planta

Wendelin Wiedeking

Marjorie M.T. Yang

Rolf M. Zinkernagel[8]

Total

[1] Does not include reimbursement for travel and other necessary business expenses incurred in the performance of their services as these are not compensation. All shares were granted as per January 19, 2010 against the prevailing share price of CHF 55.85.
[2] Pension and social security costs due by the individual and paid by the company.
[3] Daniel Vasella attended the meetings of these Committees as a guest from February 1, 2010 without voting rights.
[4] Does not include Board member compensation granted by Alcon, Inc. and reflects only the compensation for the period starting February 1, 2010 to the end of the year 2010.
[5] The Board of Directors has delegated William Brody to the Board of Directors of the Genomics Institute of the Novartis Research Foundation (GNF).
[6] In addition, Alexandre F. Jetzer-Chung was paid CHF 380 004 for consulting services.
[7] According to Pierre Landolt, the Sandoz Family Foundation is the economic beneficiary of the compensation.
[8] The Board of Directors has delegated Rolf M. Zinkernagel to the Scientific Advisory Board of the Novartis Institute for Tropical Diseases (NITD) and to the Board of Directors of the Genomics Institute of the Novartis Research Foundation (GNF).

12.2) COMPENSATION OF EXECUTIVE COMMITTEE MEMBERS

GENERAL PRINCIPLES

The compensation policies, performance management process and incentive plans apply equally to the Executive Committee members.

Decisions concerning the compensation of the Executive Committee members are based on an evaluation of the individual performance of the members of the Executive Committee as well as on the performance of their respective business area or function. Compensation of Executive Committee members is highly linked to Novartis' performance against performance objectives. The metrics of performance objectives, including net sales, operating income, market share, Novartis Economic Value Added (NVA) or innovation, are designed to appropriately balance short-term and long-term objectives. On the one hand, objectives are set at ambitious levels each year to motivate a high degree of business performance with emphasis on longer term financial objectives. On the other hand, they are also designed to avoid inappropriate or excessive risk.

COMPENSATION FOR PERFORMANCE IN 2011 AND 2010

The following compensation tables disclose the compensation granted to the Executive Committee members for performance in 2011 with comparatives to 2010. The following paragraphs describe the principles underlying the data in the tables.

ALIGNMENT OF REPORTING AND PERFORMANCE

The compensation tables synchronize the reporting of annual compensation with the performance in the given year, i.e., all amounts awarded for performance in 2011 and 2010, including the future ESOP/LSSP match, are disclosed in full in the tables of 2011 and 2010.

DISCLOSURE STRUCTURE

The compensation table shows the compensation granted to the CEO and each Executive Committee member for performance in 2011 for all compensation elements.

The column "Future ESOP/LSSP match" reflects shares to be awarded in the future if the Executive Committee member remains with Novartis for at least three or five years, respectively.

The Executive Committee members were invited to invest their annual incentive awards for 2011 and 2010 in the leveraged share saving plans – either the three-year Swiss Employee Share Ownership Plan (ESOP) or the five-year Leveraged Share Savings Plan (LSSP) – to further align their interests with those of our shareholders. Under the plan rules, participants will receive additional shares ("matching shares") after the expiration of either the three- or five-year vesting period. Under the three-year ESOP, for every two shares invested, the participant receives one matching share. Under the five-year LSSP, each share invested entitles the participant to receive one matching share. If a participant leaves Novartis prior to the expiration of the vesting period, in general, no matching shares are awarded.

VALUATION PRINCIPLES

In order to allow a comparison with other companies, the Compensation Committee decided to disclose shares, restricted shares, RSUs and ADS at their market value on the date of grant. Market value is the current quoted share price at which a director or an associate is granted a share, a restricted share or a restricted stock unit at grant date. The market value of share options is calculated by using an option pricing valuation model as per grant date.

Shares, RSUs and share options under the variable compensation plans are generally granted with a vesting[1] period and associates in Switzerland (including Executive Committee members) may block[2] shares received under any variable compensation plan for up to 10 years. According to the Swiss Federal Tax Administration and as the Compensation Committee also firmly believes, such restrictions affect the value of shares, RSUs and share options negatively. In its "Kreisschreiben Nr. 5", the Swiss Tax Administration provides for a methodology pursuant to which unvested or blocked shares or share options shall be valued with a discount for each year they are unvested or blocked. In addition, for the valuation of share options, the Swiss Tax Authorities apply – in a standing practice for Novartis (since 1997) – an option valuation model based on Black-Scholes.

See also Note 27 to the Group's consolidated financial statements for information on executive officer and non-executive director compensation in accordance with IFRS.

[1] Vesting refers to the waiting period under a share-based incentive plan that must expire before the associate becomes irrevocably entitled to the shares, RSUs or share options involved. The associate cannot sell or exercise unvested share, RSUs or share options. If an associate leaves Novartis prior to the expiration of the vesting period for reasons other than retirement, disability or death, the associate will generally forfeit rights to such shares, RSUs or share options.

[2] Blocking refers to the ability of associates in Switzerland to opt for an extended trading restriction period of up to 10 years from the award date (including vesting). Novartis encourages associates to block their shares because doing so aligns the associates' interests with those of shareholders.

EXECUTIVE COMMITTEE MEMBER COMPENSATION FOR PERFORMANCE YEAR 2011 (MARKET VALUE)[1]

		Base compensation	Variable compensation						Benefits		Total		Total compensation
			Short-term incentive plans		Long-term incentive plans								
					Equity Plan "Select"		Long-Term Performance Plan	Special share awards	Pension benefits	Other benefits		Future ESOP/LSSP match[10]	Including future ESOP/LSSP match[11,12]
	Currency	Cash (Amount)	Cash (Amount)	Shares (Market value)[2]	Shares (Market value)[3]	Options (Market value)[4]	Shares (Market value)[5]	Shares (Market value)[6]	(Amount)[7]	(Amount)[8]	(Amount)[9]	Shares (Market value)	(Amount)
Joseph Jimenez (Chief Executive Officer)	CHF	1 916 667	704 000	1 056 033	6 160 047	0	4 550 524	0	172 193	106 889	14 666 353	1 056 033	15 722 386
Juergen Brokatzky-Geiger	CHF	696 670	0	616 037	1 232 020	0	582 379	0	150 268	26 117	3 303 491	616 037	3 919 528
Kevin Buehler (since April 8, 2011)[13]	USD	803 611	618 799	1 078 872	2 716 195	0	1 312 775	0	229 624	45 974	6 805 850	1 078 872	7 884 722
David Epstein	USD	933 333	402 630	583 475	2 794 007	0	1 293 468	0	279 409	115 086	6 401 408	583 475	6 984 883
Mark C. Fishman	USD	986 333	13 997	951 304	3 861 038	0	1 347 831	0	252 712	122 315	7 535 530	951 304	8 486 834
Jeff George	CHF	733 334	365 650	365 687	1 462 533	0	443 410	940 000	105 934	48 053	4 464 601	182 871	4 647 472
George Gunn	CHF	845 836	663 000	0	1 105 030	0	930 397	0	98 584	9 992	3 652 839	0	3 652 839
Andrin Oswald	CHF	733 334	682 500	0	1 365 027	0	443 410	940 000	118 403	57 507	4 340 181	0	4 340 181
Jonathan Symonds	CHF	890 000	0	792 025	1 980 034	0	766 171	0	196 350	0	4 624 580	792 025	5 416 605
Thomas Werlen (until September 30, 2011)[14]	CHF	560 001	0	412 516	0	0	0	0	99 836	1 598 454	2 670 807	0	2 670 807
Naomi Kelman (as from March 2, 2011)[15]	USD	497 826	262 500	0	525 028	0	81 720	4 773 120	18 466	638 443	6 797 103	0	6 797 103
Felix R. Ehrat (as from October 1, 2011)[16]	CHF	175 000	0	130 405	260 810	0	76 639	0	36 296	4 352	683 502	130 405	813 907
Total[17]	**CHF**	**9 401 376**	**3 563 757**	**5 685 668**	**22 323 260**	**0**	**11 364 429**	**6 104 000**	**1 668 316**	**2 667 132**	**62 777 939**	**5 090 336**	**67 868 275**

[1] Does not include reimbursement for travel and other necessary business expenses incurred in the performance of their services as these are not considered compensation.

[2] Participants elected to invest some or all of the value of their annual incentive in the five-year Leveraged Share Savings Plan (LSSP) or the three-year Swiss Employee Share Ownership Plan (ESOP) rather than to receive cash.

[3] Novartis shares granted under the Novartis Equity Plan "Select" have a three-year vesting period.

[4] Novartis share options granted under the Novartis Equity Plan "Select" are tradable. Share options granted outside North America will expire on January 19, 2022, have a three-year vesting period and have an exercise price of CHF 54.20 per share (the closing price of Novartis shares on the grant date of January 19, 2012). Based on the option pricing valuation model as per grant date, the value of the share options granted outside North America used in this table was CHF 4.30. Share options on ADSs granted to participants in North America will expire on January 19, 2022, have a three-year vesting period and an exercise price of USD 58.33 per ADS (the closing price of Novartis ADSs on the grant date of January 19, 2012). Based on the option pricing valuation model as per grant date, the value of the share options on ADSs granted to participants in North America used in this table was USD 4.14.

[5] Awarded based on the achievement of Novartis Economic Value Added (NVA) objectives over the performance period ended December 31, 2011.

[6] The special share awards consist of RSUs to Jeff George and to Andrin Oswald awarded on September 1, 2011, against the closing share price of that day (CHF 47.00). These RSUs have a five year vesting period. The special share awards also consist of a special award of 88 000 shares granted to Naomi Kelman to compensate her loss of equity from her former employer. This grant was awarded on April 1, 2011 at the price of USD 54.24 with staggered vesting over seven years.

[7] Service costs of pension and post-retirement healthcare benefits accumulated in 2011.

[8] Includes perquisites and other compensation paid during 2011. Does not include cost allowances and tax-equalization payments regarding the international assignment of David Epstein, Jeff George and Andrin Oswald. Does not include an annual pension in payment for Kevin Buehler as a result of a change of control clause (USD 346 362 being the time pro-rated amount for the period from April 8, 2011 to December 31, 2011).

[9] The value of all equity grants included in this table has been calculated based on market value.

[10] Reflects shares to be awarded in the future under the share saving plans, either the three-year Swiss Employee Share Ownership Plan (ESOP) or the five-year Leveraged Share Savings Plan (LSSP). Participants will receive additional shares ("matching shares") after the expiration of either the three- or five-year vesting period.

[11] The values of the shares, RSUs and share options reflected in this table have been calculated based on market value. The closing share price on the grant date January 19, 2012 was CHF 54.20 per Novartis share and USD 58.33 per ADS.

[12] All amounts are gross amounts (i.e., before deduction of social security and income tax due by the executives). The employer social security contribution is not included.

[13] Excludes the annual incentive and an equity grant that were awarded to K. Buehler prior to April 8, 2011 and which relate to past performance.

[14] Thomas Werlen stepped down from the Executive Committee as per September 30, 2011 and decided to leave Novartis on January 31, 2012. The base compensation and benefits information in the table reflects his pro rata compensation over the period from January 1, 2011 to September 30, 2011 (i.e. the period during which he was member of the Executive Committee). The other compensation ("Other benefits") includes the contractual salary payments from October 1, 2011 to January 31, 2012 and the pension benefits costs over this period. The other compensation ("Other benefits") does not include, however, the fair market compensation for refraining to compete with any business of Novartis over an agreed period after leaving the Company. Mr. Werlen will receive fair market compensation in return for complying with the restriction not to compete.

[15] The table reflects the compensation as Permanent Attendee to the Executive Committee from date of hiring (March 2, 2011) until December 31, 2011.

[16] The table reflects the compensation as Permanent Attendee to the Executive Committee from hire date (October 1, 2011) until December 31, 2011.

[17] Amounts in USD for Kevin Buehler, David Epstein, Mark C. Fishman and Naomi Kelman were converted at a rate of CHF 1.00 = USD 1.130, which is the same average exchange rate used in the Group's consolidated financial statements.

EXECUTIVE COMMITTEE MEMBER COMPENSATION FOR PERFORMANCE IN 2010 (MARKET VALUE)[1]

Joseph Jimenez (Chief Executive Officer since February 1, 2010, previously ECN member)	CHF
Juergen Brokatzky-Geiger	CHF
David Epstein[13]	USD
Mark C. Fishman	USD
Jeff George[13]	CHF
George Gunn[13]	CHF
Andrin Oswald[13]	CHF
Jonathan Symonds[13]	CHF
Thomas Werlen	CHF
Total[14,15]	**CHF**

[1] Does not include reimbursement for travel and other necessary business expenses incurred in the performance of their services as these are not considered compensation.
[2] Participants elected to invest some or all of the value of their incentive in the five-year Leveraged Share Savings Plan (LSSP) or the three-year Swiss Employee Share Ownership Plan (ESOP; if eligible) rather than to receive cash.
[3] Novartis shares granted under the Novartis Equity Plan "Select" have either a two or three-year vesting period depending on the jurisdiction of the participant.
[4] Novartis share options granted under the Novartis Equity Plan "Select" are tradable. Share options granted outside North America will expire on January 19, 2021, have a two-year vesting period in Switzerland (three years in other countries) and have an exercise price of CHF 54.70 per share (the closing price of Novartis shares on the grant date of January 19, 2011). Based on the option pricing valuation model as per grant date, the value of the share options granted outside North America used in this table was CHF 5.06. Share options on ADSs granted to participants in North America will expire on January 19, 2021, have a three-year vesting period and an exercise price of USD 57.07 per ADS (the closing price of Novartis ADSs on the grant date of January 19, 2011). Based on the option pricing valuation model as per grant date, the value of the share options on ADSs granted to participants in North America used in this table was USD 5.94.
[5] Awarded based on the achievement of Novartis Economic Value Added (NVA) objectives over the performance period ended December 31, 2010.
[6] The special share awards consist of RSUs to Jeff George and to Andrin Oswald awarded on September 1, 2010, against the closing share price of that day of CHF 54.05. These awarded RSUs have a five-year vesting period.
[7] Service costs of pension and post-retirement healthcare benefits accumulated in 2010, and employer contributions to defined contribution pension plans in 2010.
[8] Includes perquisites and other compensation paid during 2010. Does not include cost allowances and tax-equalization payments regarding the international assignment of David Epstein, Jeff George and Andrin Oswald.
[9] The value of all equity grants included in this table has been calculated based on market value.
[10] Reflects shares to be awarded in the future under the share saving plans, either the three-year Swiss Employee Share Ownership Plan (ESOP) or the five-year Leveraged Share Savings Plan (LSSP). Participants will receive additional shares ("matching shares") after the expiration of either the three- or five-year vesting period.
[11] The values of the shares, RSUs and share options reflected in this table have been calculated based on market value. The closing share price on the grant date January 19, 2011 was CHF 54.70 per Novartis share and USD 57.07 per ADS.
[12] All amounts are gross amounts (i.e., before deduction of social security and income tax due by the executives). The employer's share of social security contributions is not included.
[13] The table reflects the compensation as a Permanent Attendee to the Executive Committee over the period from January 1, 2010 to January 31, 2010 and as a member of the Executive Committee over the period from February 1, 2010 to December 31, 2010.
[14] Amounts in USD for David Epstein and Mark C. Fishman were converted at a rate of CHF 1.00 = USD 0.961, which is the same average exchange rate used in the Group's consolidated financial statements.
[15] Daniel Vasella (Chairman and CEO of Novartis until January 31, 2010), Raymund Breu, Jörg Reinhardt, Andreas Rummelt and Thomas Wellauer stepped down from the Executive Committee as of January 31, 2010. Their remuneration for this period is disclosed in the table "Compensation for Executive Committee members who stepped down during 2010".

EXECUTIVE COMMITTEE MEMBER - EQUITY AWARDS FOR PERFORMANCE YEAR 2011 (NUMBER OF EQUITY INSTRUMENTS)

	Variable compensation					
	Short-term incentive plans	Long-term incentive plans				
		Equity Plan "Select"		Long-Term Performance Plan	Special share awards	Future ESOP/LSSP match
	Shares (Number)	Shares (Number)	Options (Number)	Shares (Number)	Shares (Number)	Shares (Number)
Joseph Jimenez (Chief Executive Officer)	19 484	113 654	0	83 958	0	19 484
Juergen Brokatzky-Geiger	11 366	22 731	0	10 745	0	11 366
Kevin Buehler (since April 8, 2011)	18 496	46 566	0	22 506	0	18 496
David Epstein	10 003	47 900	0	22 175	0	10 003
Mark C. Fishman	16 309	66 193	0	23 107	0	16 309
Jeff George	6 747	26 984	0	8 181	20 000	3 374
George Gunn	0	20 388	0	17 166	0	0
Andrin Oswald	0	25 185	0	8 181	20 000	0
Jonathan Symonds	14 613	36 532	0	14 136	0	14 613
Thomas Werlen (until September 30, 2011)	7 611	0	0	0	0	0
Naomi Kelman (as from March 2, 2011)[1]	0	9 001	0	1 401	88 000	0
Felix R. Ehrat (as from October 1, 2011)[1]	2 406	4 812	0	1 414	0	2 406
Total	**107 035**	**419 946**	**0**	**212 970**	**128 000**	**96 051**

[1] The table reflects the compensation as Permanent Attendee to the Executive Committee from date of hiring until December 31, 2011.

EXECUTIVE COMMITTEE MEMBER COMPENSATION FOR PERFORMANCE IN 2010 (NUMBER OF EQUITY INSTRUMENTS)

SHARE OPTIONS OWNED BY EXECUTIVE COMMITTEE MEMBERS

	Number of share options[1]						
	2012					Other	As of January 19, 2012
Joseph Jimenez				552 076	157 266		709 342
Juergen Brokatzky-Geiger				75 705	109 016	146 436	331 157
Kevin Buehler (as from April 8, 2011)						782 485[2]	782 485
David Epstein						267 777	267 777
Mark C. Fishman					184 870	587 149	772 019
Jeff George		141 396				114 979	256 375
George Gunn						94 371	94 371
Andrin Oswald						5 633	5 633
Jonathan Symonds						54 348	54 348
Thomas Werlen (until September 30, 2011)	NA	NA	NA	NA	NA	NA	NA
Naomi Kelman (as from March 2, 2011)[3]							
Felix R. Ehrat (as from October 1, 2011)[3]							
Total	–	**141 396**	–	**627 781**	**451 152**	2 053 178	3 273 507

NA – Not applicable.

[1] Share options disclosed for a specific year were granted under the Novartis Equity Plan "Select." The column "Other" refers to share options granted in 2005 or earlier, to share options granted to these executives while they were not Executive Committee members, and to share options bought by the Executive Committee members or "persons closely linked" to them (see definition under 12.3) on the market.

[2] Consists of non tradable options and share settled appreciation rights resulting from conversion of Alcon equity into Novartis equity.

[3] Naomi Kelman and Felix R. Ehrat became members of the Executive Committee as from 1 January 2012. From March 2, 2011 to December 31, 2011, Naomi Kelman was Permanent Attendee to the Executive Committee. From October 1, 2011 to December 31, 2011, Felix R. Ehrat was Permanent Attendee to the Executive Committee.

TERMS OF SHARE OPTIONS GRANTED

The share options granted to the Executive Committee members under the variable compensation plans are exercisable for one share each (1:1). The terms of the share options granted since 2007 are shown in the table below.

TERMS OF SHARE OPTIONS

Grant year	Exercise price (CHF/USD)	Vesting (years) (CH/other countries)	Term (years)
2012	54.20/58.33	3/3	10
2011	54.70/57.07	2/3	10
2010	55.85/53.70	2/3	10
2009	53.65/46.42	2/3	10
2008	64.05/57.96	2/3	10

12.5) LOANS AND OTHER PAYMENTS

LOANS TO BOARD MEMBERS OR EXECUTIVE COMMITTEE MEMBERS

No loans were granted to current or former Board members or Executive Committee members during 2011 and 2010. No such loans were outstanding as of December 31, 2011 and December 31, 2010.

OTHER PAYMENTS TO BOARD MEMBERS OR EXECUTIVE COMMITTEE MEMBERS

During 2011 and 2010, no payments (or waivers of claims) other than those set out in the Board Member Compensation tables, the Executive Committee Member Compensation tables and the table of compensation of Executive Committee members who stepped down during 2011 were made to current Board members or Executive Committee members or to "persons closely linked" to them (see definition under 12.3).

PAYMENTS TO FORMER BOARD MEMBERS OR EXECUTIVE COMMITTEE MEMBERS

During 2011 and 2010, no payments (or waivers of claims) were made to former Board members or Executive Committee members or to "persons closely linked" to them (see definition under 12.3), except for an amount of CHF 62 346 (2010: CHF 62 298) that was paid to the Honorary Chairman, and an amount of CHF 1 129 for social security arrears which was paid in favor of a former member of the Board of Directors and an amount of CHF 25 596, which was paid to a former member of the Executive Committee as deferred compensation.

13. RISK ASSESSMENT DISCLOSURES

Novartis AG, as the ultimate parent company of the Novartis Group, is fully integrated into the Group-wide internal risk assessment process and is fully integrated into the process described in note 32 to the Group's consolidated financial statements.

PROPOSAL FOR THE APPROPRIATION OF THE AVAILABLE EARNINGS OF NOVARTIS AG

	2011 CHF
Available unappropriated earnings	
Balance brought forward	–
Net income of the year	5 370 749 043
Partial use of free reserves	477 787 917
Total available earnings	5 848 536 960
Appropriation	
Payment of a dividend of CHF 2.25 (2010: CHF 2.20) gross on 2 599 349 760 (2010: 2 478 241 163) dividend bearing shares with a nominal value of CHF 0.50 each	– 5 848 536 960
Transfer to free reserves	–
Balance to be carried forward	–

REPORT OF THE STATUTORY AUDITOR ON THE FINANCIAL STATEMENTS OF NOVARTIS AG

TO THE GENERAL MEETING OF NOVARTIS AG, BASEL

REPORT OF THE STATUTORY AUDITOR ON THE FINANCIAL STATEMENTS OF NOVARTIS AG

As statutory auditor, we have audited the financial statements of Novartis AG, which comprise the income statement, balance sheet and notes (pages 262 to 279), for the year ended December 31, 2011.

Board of Directors' Responsibility

The Board of Directors is responsible for the preparation of the financial statements in accordance with the requirements of Swiss law and the Company's articles of incorporation. This responsibility includes designing, implementing and maintaining an internal control system relevant to the preparation of financial statements that are free from material misstatement, whether due to fraud or error. The Board of Directors is further responsible for selecting and applying appropriate accounting policies and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Swiss law and Swiss Auditing Standards. Those standards require that we plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers the internal control system relevant to the entity's preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control system. An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of accounting estimates made, as well as evaluating the overall presentation of the financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements for the year ended December 31, 2011 comply with Swiss law and the Company's articles of incorporation.

REPORT ON OTHER LEGAL REQUIREMENTS

We confirm that we meet the legal requirements on licensing according to the Auditor Oversight Act (AOA) and independence (article 728 CO and article 11 AOA) and that there are no circumstances incompatible with our independence.

In accordance with article 728a paragraph 1 item 3 CO and Swiss Auditing Standard 890, we confirm that an internal control system exists which has been designed for the preparation of financial statements according to the instructions of the Board of Directors.

We further confirm that the proposed appropriation of available earnings complies with Swiss law and the Company's articles of incorporation. We recommend that the financial statements submitted to you be approved.

PricewaterhouseCoopers AG

Peter M. Kartscher
Audit expert
Auditor in charge

Gerd Tritschler
Audit expert

Basel, January 24, 2012

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KEY DATES FOR 2012

Anticipated key reporting dates

A ?	23, 2012
2012 A	24, 2012
2012	19, 2012
2012	25, 2012
2012	2013

CONTACT INFORMATION

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Media relations
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FORWARD-LOOKING STATEMENTS

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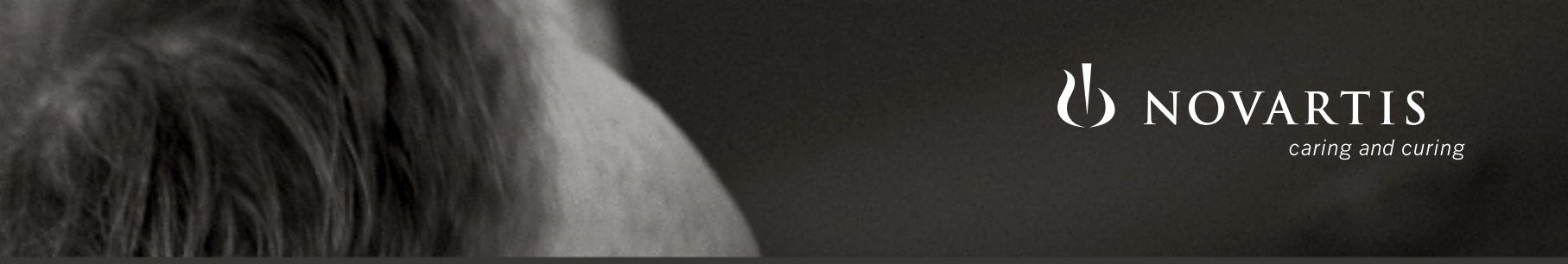
NOVARTIS
caring and curing