

Annual Report

03

Lonza

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Letter to shareholders

Dear Shareholders

2003 was a difficult year for our Group and we experienced a significant setback in performance. Sales fell by 11.6% to CHF 2 242 million. Operating income (exclusive of non-recurring costs) decreased by 27.9% from CHF 419 million to CHF 302 million. Group net income excluding non-recurring items was CHF 198 million compared with CHF 297 million in 2002. Net income including the non-recurring pre-tax charges of CHF 158 million declined to CHF 91 million. The non-recurring charges resulted from the decommissioning of a number of fine chemicals assets and restructuring initiatives.

As a result of the difficult market conditions in most of its business lines and due to failures and delays of product approvals late in clinical development, both in the exclusive chemical synthesis business and mammalian cell culture technology, the Group revised its 2003 guidance in May and started a company-wide restructuring program. Measures designed to improve efficiency and reduce overhead costs in all business sectors and service functions were initiated to improve Lonza's competitive position. By the end of December 2003, 71% of all personnel measures and 55% of the other initiatives had been implemented. The total headcount was reduced by 9%, from 6 216 in 2002 to 5 659 at year-end 2003, and nearly 60% of the CHF 100 million savings set as a 12-month target had already been achieved by December 2003.

The recovery expected for the second half of the year did not materialize. Despite the temporary setback in our 2000 L and 5000 L capacity utilization, our new 3 x 20 000 L large-scale mammalian capacity in Portsmouth, NH (USA), is now almost fully booked and will come on stream mid-2004 as planned. We strengthened our customer base for that facility with two long-term supply agreements, one with a top-ten pharma company and the other with Genentech for its blockbuster drug Rituxan.

After the setback in 2003, the Group needs to rebase both its operations and expectations, and reaffirm its leadership position which has been earned over many years of outstanding delivery in terms of both technology and customer service. The commitment to life sciences is unchanged. The expansion projects in biotechnology (mammalian and microbial) are well advanced. With its state-of-the-art technology, superb research and development skills and a reduced cost base, Lonza is well positioned to deliver on its strategy in the medium term.

In response to the change in market conditions, Lonza has redesigned its custom manufacturing business model in order to increase market coverage and penetration. Focusing on continuous pipeline expansion, the processes for the acquisition of customers and projects for custom manufacturing contracts in the areas of chemical synthesis, microbial fermentation and mammalian cell culture technology are fully aligned and coordinated. The aim is to improve significantly the utilization of our large reactors.

Market conditions in Exclusive Synthesis are expected to remain difficult throughout 2004. The Biologics assets will begin to see a good level of utilization in the second half of 2004, as the three 20 000 L bioreactors in Portsmouth, NH (USA), come on stream on the back of strong customer commitments. Organic Fine and Performance Chemicals are expecting better market conditions, although the impact of a weak dollar and high oil prices will continue to dampen the recovery. Given the dilutive effect of divestitures on cash and earnings and the efforts required during this rebasing period, the Board of Directors has decided not to divest the Polymer Intermediates business, which is expected to recover to better levels during 2004.

The combined effect of all the negative factors which have come to bear on the performance of Lonza for 2003 requires that the company take a conservative and cautious view of its earnings guidance. As a result, the Board of Directors feels comfortable setting minimum levels for expected returns, with operating income of CHF 225 million and earnings per share of CHF 3.00 for 2004. No further non-recurring charges relating to restructuring are expected.

Markus Gemuend, Chief Executive Officer of Lonza, has advised the Board of Directors of his decision to step down from the position as soon as a suitable replacement has been identified. Mr. Gemuend feels that, given the market developments which affected the performance of Lonza in 2003, a different type of leadership is required to move the Group forward. The Board respects his decision to step down and is appreciative of his efforts during the last two years.

With regard to the shareholder structure, Lonza has been informed by EMS-Chemie Holding AG that it held 11 359 047 nominal shares, representing 22.52% of the voting rights as of 31 December 2003. This ownership was reduced to 19.54% as of 13 February 2004 and EMS-Chemie Holding AG now views its investment in Lonza as purely financial. On 8 January 2004, Lonza was informed by Harris Associates L.P., Chicago, that its participation in the voting rights of Lonza Group Ltd exceeded the threshold of 5% and it holds 5.01% of the voting rights, represented by 2 525 950 registered shares.

In March 2003, Peter Matter and Sir Richard Sykes joined the Board of Directors as new members. Peter Matter, who spent nearly 30 years with F. Hoffmann-La Roche, has brought with him substantial financial and industry-related experience and has represented the EMS-Chemie Holding AG interests. Sir Richard Sykes, who was Chairman of GlaxoSmithKline plc until May 2002, brings with him some 30 years of experience in the pharmaceutical and biotechnology industries. His contribution has substantially strengthened the Board in the implementation of Lonza's life sciences objectives. Peter Matter has advised the Board of his intention not to stand for re-election.

We would like to express our gratitude for your confidence in our company especially during these challenging times. We would also like to thank our customers for their continuing trust. We extend our heartfelt thanks to our employees for their invaluable contributions and performance in an extremely difficult year.



Sergio Marchionne
Chairman of the Board



Markus Gemuend
Chief Executive Officer



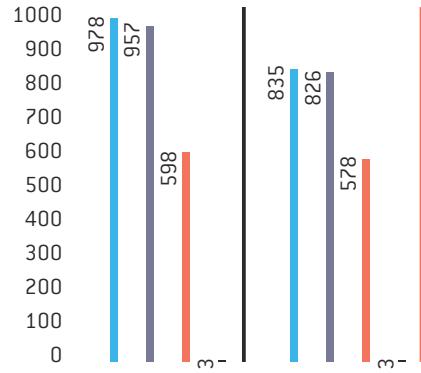
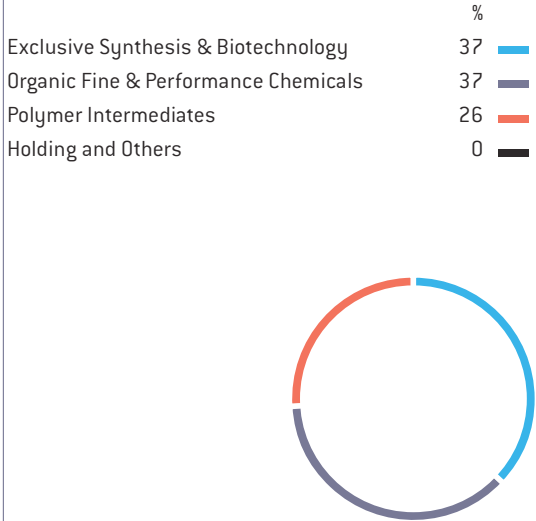
Financial highlights

million CHF		2002	2003
Lonza			
Sales		2 536	2 242
Operating income		419	302
Non-recurring items		(112)	(158)
Income before income taxes		283	115
Net income		221	91
Cash flow before change in net working capital		368	264
Investments in property, plant and equipment and intangibles (at cost)		(350)	(424)
Shareholders' equity		1 235	1 235
Net debt		869	978
Basic earnings per share before non-recurring items	CHF	6.12	4.18
Basic earnings per share	CHF	4.55	1.92
Book value per share	CHF	26.07	26.07
Dividend payout ratio before non-recurring items	%	30	31
Dividend payout ratio	%	41	68
Number of shares (par value CHF 1.00)		50 450 000	50 450 000
Share price (high/low)	CHF	120.50/79.90	85.55/60.55
Market capitalization		4 238	3 587
Lonza Group Ltd			
Net income		205	312
Shareholders' equity		927	1 149
Shareholders' equity as a percentage of total assets	%	56	67
Dividends		90	62
Dividend per share	CHF	1.90	1.30

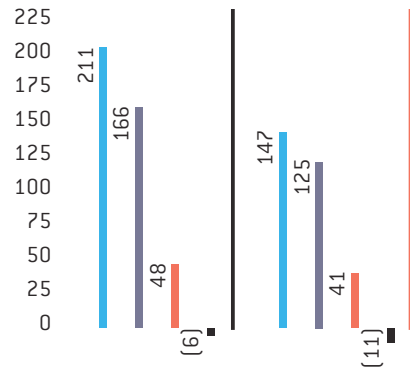
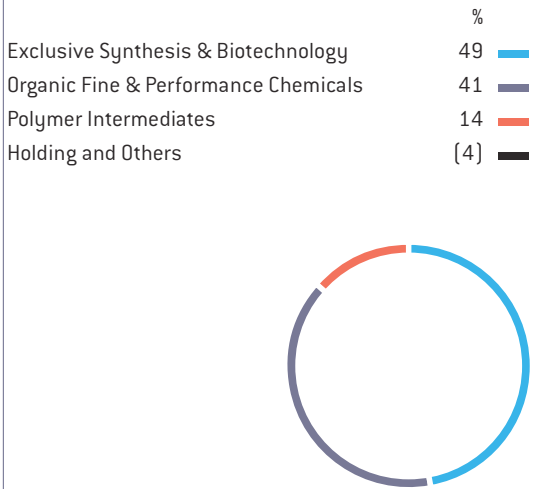
million CHF

2002

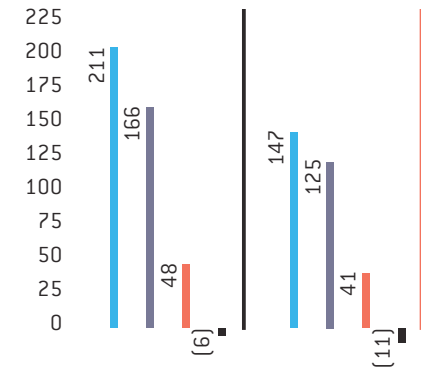
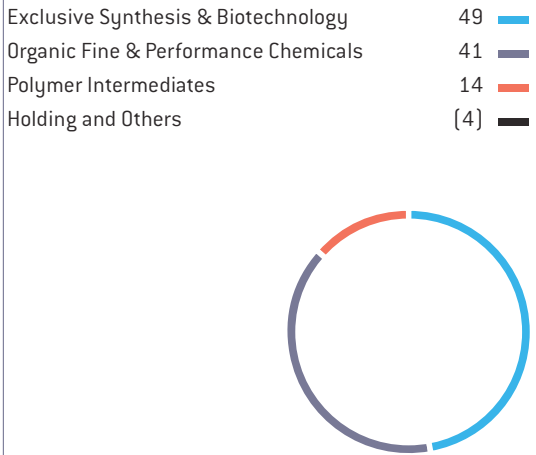
2003



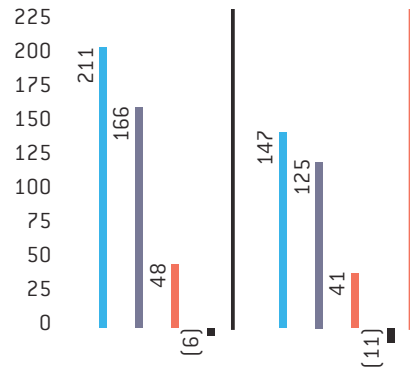
Sales by division



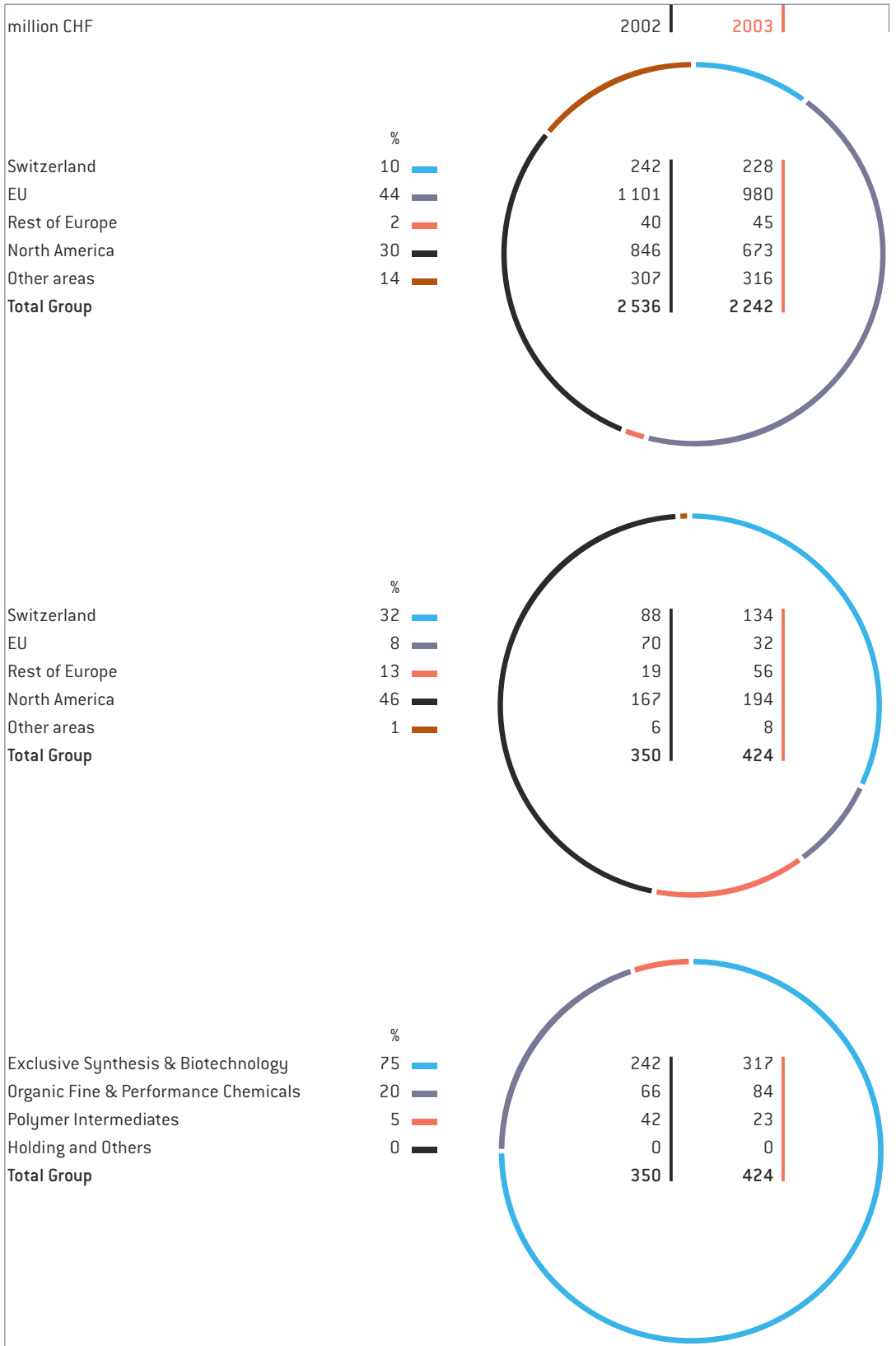
Operating income by division

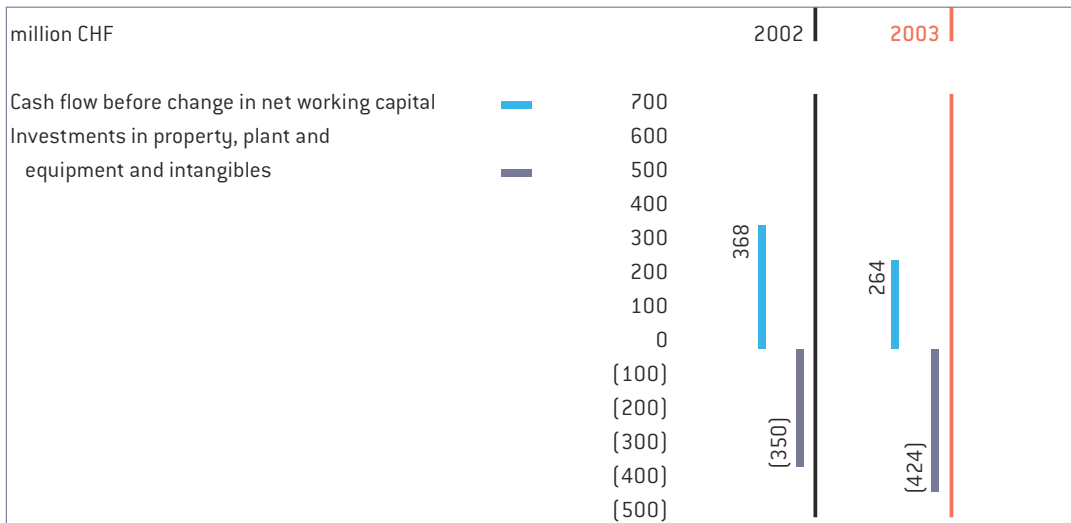


Operating income by division

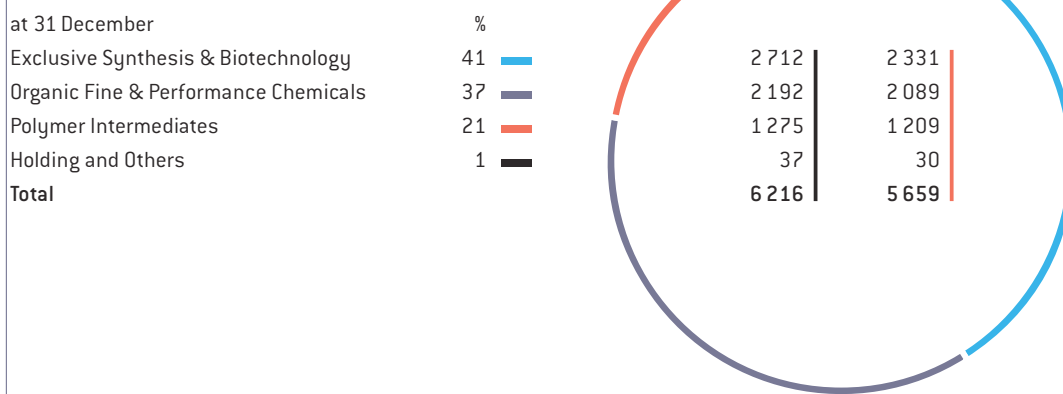


Operating income by division





Cash flow and investments



Employees by division

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Group performance – The recovery expected in the second half of the year did not materialize, with the result that Group sales decreased in 2003 by 11.6% to CHF 2 242 million. Adjusted for the impact of currency fluctuations, the decrease amounted to 9.0%.

The Group experienced a significant setback in performance, and operating income (before non-recurring items) of CHF 302 million was 27.9% below the previous year's record level of CHF 419 million. Operating margins decreased to 13.5% from 16.5% in 2002.

Our custom manufacturing facilities remained at low levels of activity throughout the year, with sales and margins down compared with the previous year. Exclusive Synthesis was adversely affected by a low rate of drug approvals, continuing destocking at customers and overcapacity in both custom manufacturing and the pharmaceutical industry itself. The mammalian cell culture fermentation business was negatively influenced by failures of customer products late in clinical development. Organic Fine and Performance Chemicals suffered from high prices for raw materials and energy and reduced demand for some of its major products with lower results in sales and operating income. Nonetheless, overall production capacity utilization was high and market shares were successfully defended. In addition to high raw material and energy costs, the business with Polymer Intermediates experienced low demand and unfavorable currency influences resulting in lower sales and operating income compared with last year. Despite this, a significant improvement was registered in the second half.

Due to overcapacity and the persistence of difficult market conditions, Lonza has decided to decommission fine chemicals production assets in both the USA and Europe with the aim of rebasing and realigning its capabilities to the current business environment and competing only with its newest and best production assets in what is now a highly competitive market. As a result, Lonza recorded a non-cash, pre-tax charge of

CHF 100 million in 2003. The efficiency improvement and overhead cost reduction program started in May 2003 and related initiatives will improve our cost position by CHF 100 million by the end of the first half of 2004 at a pre-tax cost, recorded in 2003, of CHF 58 million.

Given the dilutive effect of divestitures on cash and earnings, and the efforts required during the ongoing rebasing period in the other businesses, the Board has decided not to pursue the divestiture of the Polymer Intermediates business.

Due to the lower results and the high capital expenditure program, the Group's net debt position increased to CHF 978 million, compared with CHF 869 million at the end of 2002. Net financial expenses rose accordingly to CHF 24 million, compared with CHF 19 million in 2002. Due to restructuring activities and tax optimization possibilities, the tax rate of 21% is still at the low end of the Group's expected range.

As a result, Group net income excluding non-recurring items was CHF 198 million, compared with CHF 297 million in 2002. Net income including the non-recurring items decreased by 58.8% to CHF 91 million.

Capital expenditure in 2003 increased to CHF 424 million, compared with CHF 350 million in the prior year, due to the investment cycle in the biotechnology area now nearing completion.

Holding – In 2003, Lonza Group Ltd achieved a net income of CHF 312 million. In line with our accounting principles, write-offs on investments of CHF 18 million were booked in 2003. Total shareholders' equity, measured as a percentage of total assets, increased from 56.1% in 2002 to 66.9% in 2003. This increase is attributable to the higher dividend payments of subsidiaries.

In February 2003, Lonza Group Ltd issued a 2% bond of CHF 375 million, at an issue price of 100.69%, with maturity date 14 February 2006. Consistent with the Group's stated policy of distributing between 25 and 33% of consolidated

net income (excluding non-recurring items) as dividends, the Board of Directors will propose a dividend of CHF 1.30 (CHF 1.90 for 2002).

Our employees – At the end of 2003, Lonza had 5659 employees. As a result of the company-wide restructuring initiative to improve efficiency and reduce overhead costs in all business sectors and service functions, the headcount was reduced in 2003 by 9% compared with the previous year. In line with our organization and employee development initiatives, we continued in 2003 with a series of leadership development workshops in Switzerland, led by the participants themselves on an action-learning basis. In 2003, more than 250 employees completed management education programs, and most of our employees participated in technical and skills training. Thus, the majority of our workforce was involved in development programs.

Our custom manufacturing activities, in both Exclusive Synthesis and Biotechnology, suffered a setback in 2003. Exclusive Synthesis faced persistently difficult market conditions. Biotechnology was hit by failures and delays of customer products in late clinical development. Consequently, the division's sales of CHF 835 million were 14.6% (11.8% on a currency-adjusted basis) below the previous year's level of CHF 978 million. Operating income decreased from CHF 211 million to CHF 147 million, with operating margins declining from 21.6% to 17.6%.

Exclusive Synthesis – Our chemical custom manufacturing for the pharmaceutical industry continued to be adversely affected by the low rate of new drug approvals, continuing destocking at customers and delayed product approvals. Overcapacity continued and brought additional competitive pressures. The demand for our major established products, particularly in the HIV and cardiovascular indications, remained stable, but new product introductions at our commercial plants were well below expectations. The recovery expected in the second half did not materialize. Our agrochemicals business performed as expected, mainly due to good take-up of established products, despite the flatness of the global crop protection market.

Biotechnology – In the mammalian cell culture technology business (Lonza Biologics), sales and capacity utilization of the 2 000 L and 5 000 L reactors suffered as a result of failures and delays of customer products in late clinical development. Take-or-pay contractual payments by customers offset only part of the profit shortfall in 2003. As a result of our strong marketing initiatives, the project pipeline continued to grow. We are confident of refilling the capacity during 2004, but positive effects on capacity utilization are not expected until the second half of the year.

The investment project in Portsmouth, NH (USA), will go on stream in July 2004 as planned. The customer base for the new 60 000 L capacity was further strengthened by concluding two long-term supply agreements, one with a top-ten pharma

company and the other with Genentech for its blockbuster product Rituxan. As a result, the new capacity will be almost fully utilized in 2005.

The performance of our microbial fermentation activities (Lonza Biotec) was characterized by lower sales compared with the previous year. Our L-Carnitine sales remained at the 2002 level despite increased competition from Asian countries. L-Carnitine received approval in Japan in 2003, thus opening new market opportunities. In the custom manufacturing business, demand for existing pharmaceutical products suffered from lower call-offs and project delays. Strong marketing efforts are underway to further strengthen the pipeline. Construction of the microbial biopharmaceuticals plant in Visp (CH) is ongoing but the scope of the investment has been reduced. The small-scale plant will come on stream in the second quarter of 2004.

Research and development – In Exclusive Synthesis, the R & D portfolio for small molecules, including peptides and oligonucleotides, was strengthened in all clinical phases, resulting in a healthy mix of R & D projects and a broadening of the customer base. We successfully conducted a large scale peptide campaign in the launch plant and had a significant R&D program focused on delivering laboratory quantities (5 to 50 g) in peptides and oligonucleotides.

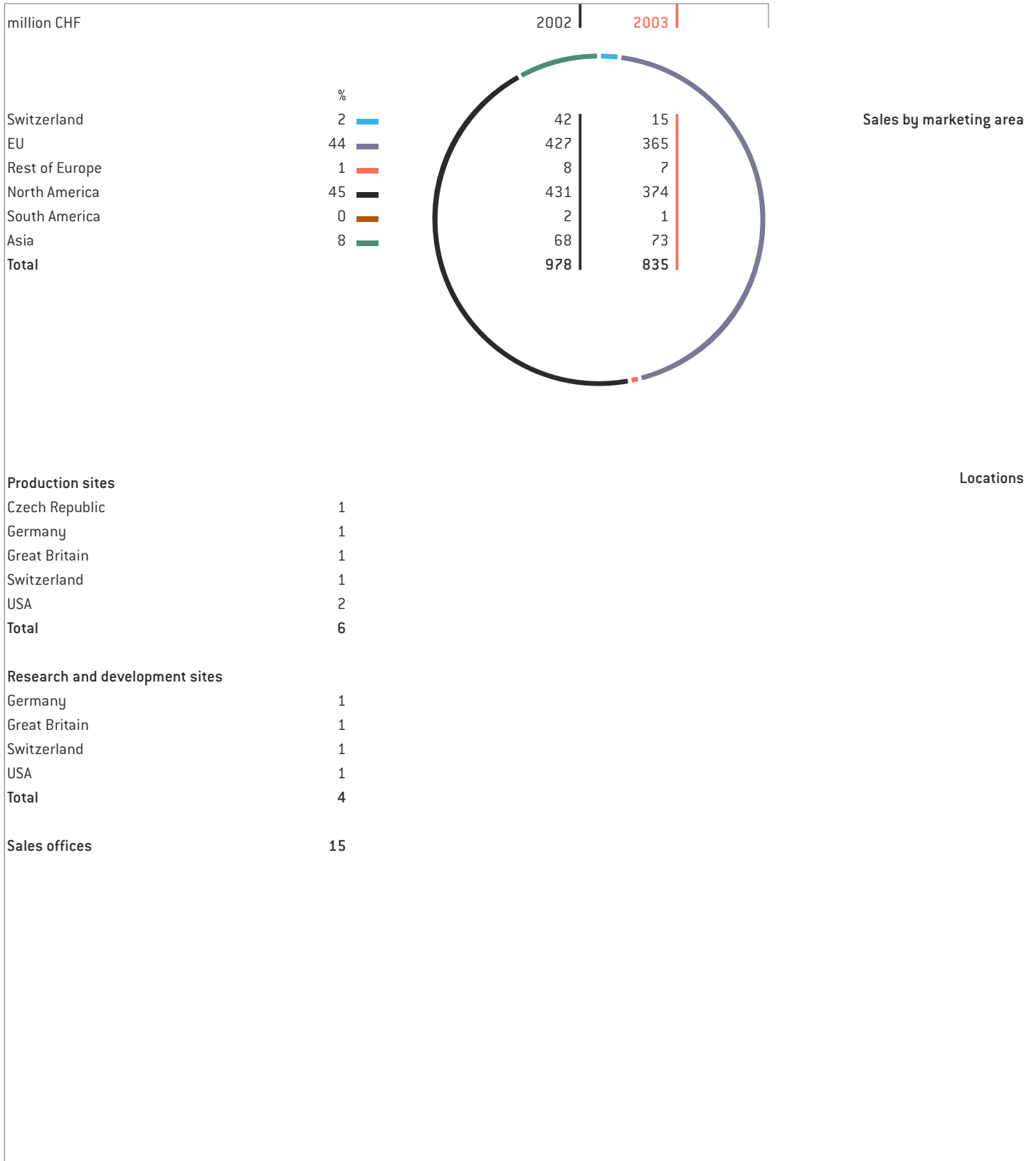
The Small Scale Plant (SSP) in Visp (CH) went on stream as planned in mid-2003 and is now almost fully occupied. With the service offered by the SSP we have been able to attract new customers.

In the mammalian cell culture technology business, demand for our development services remained strong and the R & D group worked on over 35 projects, ranging from cell line construction through to support for product approval filings. The expansion of the development labs in Slough (UK) included new pilot plant facilities which have been used both for customer projects and to provide scale-up data for our new manufacturing facilities. The in-house research has con-

tinued to focus on reducing development timelines and improving productivity. The development of a novel CHO (Chinese hamster ovary) cell line and fermentation process improvements have led to yields in excess of 3.5 g/l for a monoclonal antibody.

In the microbial fermentation business significant efforts were made in the development of processes using bacteria and yeast for the production of biopharmaceutical proteins. Progress on process development has been underpinned by the introduction of a new microbial expression technology in E. coli. This has been successfully tested with several different proteins, ranging from recombinant enzymes to therapeutic proteins, including antibody fragments. Significant improvements in productivity have been achieved with this technology. New R & D laboratories have been commissioned in Visp to support the work in biotechnology.

	Products	Main application	Market position
Exclusive chemical synthesis	Intermediates and active substances	Life sciences industry, pharmaceuticals, crop protection agents and animal health products	Among the leading producers
Exclusive microbial fermentation and bioconversion	Development and manufacture of intermediates and active substances	Life sciences industry, pharmaceuticals and cosmetics	Among the leading producers
	L-Carnitine	Sports nutrition, food, pharmaceuticals and feedstuffs	No 1 worldwide
Exclusive mammalian cell fermentation	Process development and manufacture of therapeutic monoclonal antibodies and recombinant proteins, proprietary GS-expression system	Pharmaceutical and biotechnology industry	No 1 worldwide
Key technologies	<p>Asymmetric reactions Racemic separations with transition metal catalysts (hydrogenation, oxidation, Heck/Aldol) Synthesis of chiral building blocks with biocatalysts</p> <p>Expertise in handling hazardous and highly reactive chemicals such as Acetylene/ethylene Cyclopentadiene Ethylene oxide HCN/CICN/chlorosulfonyl-isocyanate Ketene/diketene Malononitrile Phosgene (cGMP)/CO SOCl₂/Cl₂ (gas/liquid)</p> <p>Organometallic reactions Grignard Heck reactions: with organolithium compounds with organozinc compounds Sodium in liquid ammonia</p>	<p>Oxidations With nitric acid With oxygen/air With peroxides With transition metal catalysts Amoxidation Ozonolysis</p> <p>Reactions under special conditions High-pressure reactions High-temperature reactions Low-temperature reactions</p> <p>Reductions Catalytic hydrogenations (homogeneous and heterogeneous): with metal hydrides with Raney nickel</p> <p>Biotechnological processes Enzyme-catalysed reactions (biotransformations) Mammalian cell fermentation (GS and other expression systems, protein purification and analysis) Microbial fermentation (batch and fed-batch mode)</p>	<p>Peptide and oligonucleotide technologies Solid-phase synthesis Liquid-phase synthesis Recombinant technology Large-scale downstream processing (ion exchange, HPLC, lyophilization)</p>



Sales reached CHF 826 million, down 13.7 % on 2002 and 8.7 % on a currency-adjusted basis. The businesses were exposed to higher raw material and energy prices and a weakening US dollar. As a result, operating income declined to CHF 125 million, 24.7 % down on last year. Operating margins decreased from 17.3 % in 2002 to 15.1 %.

Organic Fine Chemicals – Tough conditions for metaldehyde and niacin, combined with the high price of raw materials, high energy costs and unfavorable US dollar exchange rates, had a negative impact on the division's performance. Nonetheless, overall production capacity utilization was high and market shares were defended. Demand for vitamin intermediates was high. The nicotines (Vitamin B3) business was negatively affected by SARS in Asia and the outbreak of a poultry disease in northern Europe in the first half of the year. As a result, market demand slowed and prices came under pressure. The medium- to long-term market view remains strong, and on this basis it has been decided to build a second niacinamide production plant with a capacity of 6 000 metric tons per annum (expandable to 9 000 tons) in China, which will start up in the second half of 2005.

The diketene derivatives business faced strong competitive pressure from producers in low-cost countries. Sales of engineering polymers for high-performance applications exceeded last year's levels, with volumes to the electronics industry up in the second half of 2003.

Revenues from metaldehyde – a molluscicide – suffered from dry weather conditions in major markets in Europe.

Performance Chemicals – Sales in this predominantly US-based business decreased by 18.4 %. In local currencies and adjusted for the reduced sales resulting from the divestment of the glycerine plant in Painesville, OH (USA) at the end of 2002, sales slightly exceeded last year's level. Our strong marketing efforts for products for wood protection and water treatment resulted in a good performance. Competitive price pressure,

mainly in the functional chemical segments of plastic lubricants and technical esters, combined with substantially higher raw material and energy costs, led to a slight decline in operating income for the full year. At the end of 2003, a new production facility for Carboquat – a wood protection fungicide meeting the requirements of the new EPA (Environmental Protection Agency) regulations – came on stream. Lonza has secured firm commitments from two major wood treaters, which will ensure good utilization of the new facility.

Research and development – A new generation of catalysts for the ammoxidation of beta-picoline to cyanopyridine was introduced in our Guangzhou (CN) plant and produced an excellent performance. As a result, the niacinamide capacity increased substantially. The new Lonza technology for the direct oxidation of beta-picoline to niacin (vitamin B3) is well advanced and the process will be ready soon. A project for the production of pyridine derivatives as feedstock for our new niacin technology is well advanced, too. In the area of new business development, the division is focusing on non-cGMP intermediates for the life sciences industry. Our efforts have also led to the market introduction of new products for various industrial applications.

In the area of performance chemicals, new product developments included CarboShield – Carboquat technology applied as an effective corrosion inhibitor – and the Natrulon series of personal care products, including a natural preservative, a skin rejuvenating system utilizing L-Carnitine as well as a skin-lightening product. Further new products developed and introduced into the market included: Equinox, a branded water treatment product for the pulp and paper industry; Cata-guard, another branded water treatment product, predominantly for the pool and spa markets; and PGPR, a new chocolate emulsifier.

	Products	Main application	Market position
Organic Fine Chemicals	Niacin, niacinamide	Food and feedstuffs, pharmaceuticals	No 1 worldwide for niacin
	Diketene derivatives	Pharmaceuticals, agrochemicals, colorants	No 1 worldwide
	Hydrocyanic acid derivatives	Vitamins, optical brighteners, agrochemicals	No 2 worldwide
	Engineering polymers	Electronics, aerospace industry, coating	No 1 worldwide in PT resins, No 1 worldwide in specialty chain-extenders
	Meta® – Metaldehyde	Snail and slug control agents	No 1 worldwide
Performance Chemicals	Microbiologically active substances		
	Quaternary ammonium compounds	Disinfectants for household, industrial and institutional applications, including water treatment and wood preservation	No 1 worldwide
	Halogenated hydantoins	Biocides for water treatment, pools and spas, and household disinfection	Among the leading producers
	Hydantoin derivatives	Preservatives for personal care and household products	Among the leading producers
	Oleochemical derivatives	Food ingredients, humectants and emollients for personal care, processing aids and lubricants for polymer and textile industry, and industrial defoamers	Among the leading producers in North America
Key technologies	<p>Expertise in handling hazardous and highly reactive chemicals such as Acetylene/ethylene Cyclopentadiene Ethylene oxide HCN/CICN/chlorosulfonyl-isocyanate Ketene/diketene Malonodinitrile Phosgene (cGMP)/CO SOCl₂/Cl₂ (gas/liquid)</p> <p>Organometallic reactions Grignard Heck reactions: with organolithium compounds with organozinc compounds Sodium in liquid ammonia</p>	<p>Oxidations With nitric acid With oxygen/air With peroxides With transition metal catalysts Ammoxidation Ozonolysis</p> <p>Reactions under special conditions High-pressure reactions High-temperature reactions Low-temperature reactions</p> <p>Reductions Catalytic hydrogenations (homogeneous and heterogeneous): with metal hydrides with Raney nickel</p>	<p>Performance Chemicals technologies Amination and quaternization for biocide production Fatty-acid-based esterification technologies Hydantoin technology Ethoxylation technology</p>



The division's sales of CHF 578 million declined by 3.3 % compared with the previous year's level and were 5.1 % down on a currency-adjusted basis. Practically all the business units were affected by the strong euro, higher raw material and energy costs and soft demand in the first half. Operating income in 2003 decreased by 14.6 % to CHF 41 million and margins fell to 7.1 %, compared with 8.0 % in the same period of last year. The second half showed a market improvement with margins at 7.9 %.

Sales of phthalic anhydride and plasticizers were adversely affected by the weak demand of some end markets, especially the construction sector and the Italian automotive industry, as well as by the lack of orders from Asia, particularly during the second and third quarters.

Sales of maleic anhydride and derivatives in Europe were satisfactory thanks to a balanced demand and supply situation. Low demand from China – due to currency factors – affected the overall result.

Sales of catalysts were hit by the lack of investment in phthalic and maleic anhydride production units. New catalysts were developed and successfully introduced into the European market.

Performance of trimellitic anhydride, mainly utilized in coating and cables, suffered from the downturn in the automotive sector. Sales of special plasticizers grew thanks to the substitution of old general-purpose phthalates.

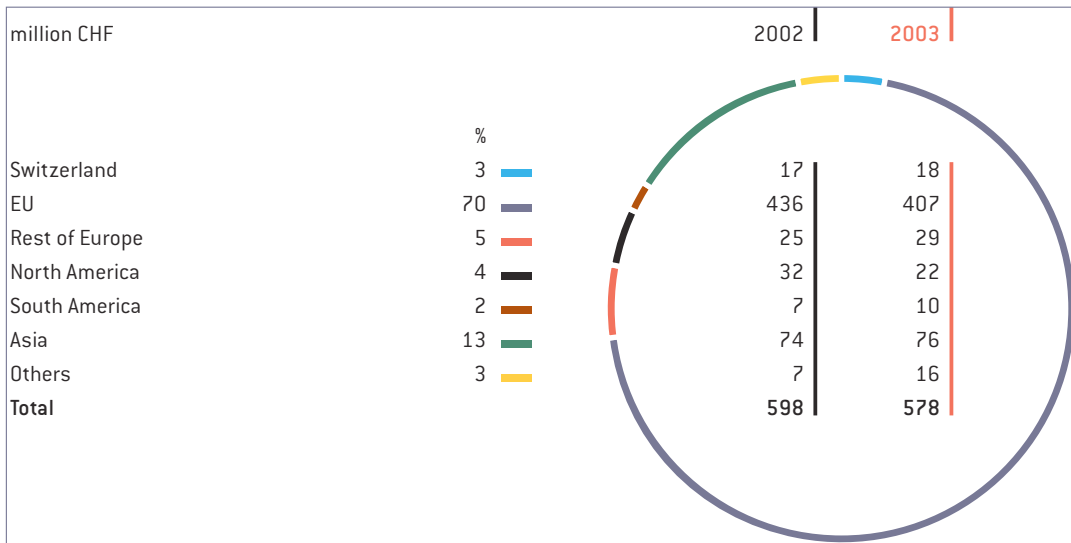
Resins and compounds performed in line with expectations. The newly launched DCPD (dicyclopentadiene) resins have a proven low styrene emission and were well accepted by the market. Pure isophthalic acid production in Singapore reached the highest output since the plant came on stream in December 1998. Prices were stable but margins came under pressure due to high raw material prices.

Research and development – The division's R & D was focused on gas and liquid phase oxidation and resulted in process improvements and new products which expanded our product portfolio.

A third-generation high-yield catalyst for maleic anhydride fluid bed oxidation was tested in pilot plant trials with promising results.

Several polymeric plasticizers, a family of trimellitates specially formulated for lube oil applications, new vinylester and DCPD polyester resins as well as formulated anhydrides for reinforced plastic applications were developed and successfully introduced into the market.

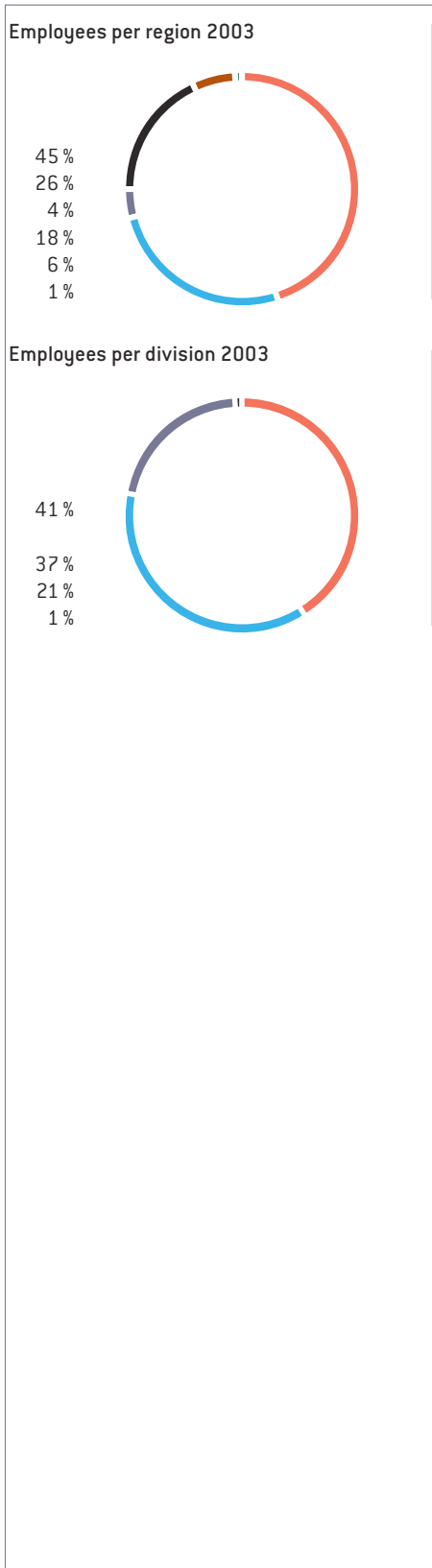
	Products	Main application	Market position
Anhydrides and chemicals	Dibasic acids and anhydrides: phthalic anhydride, maleic anhydride, pyromellitic anhydride, fumaric acid, malic acid, trimellitic anhydride	Unsaturated polyester resins, plasticizers, adhesives, paints, lubricants, additives for food and feedstuffs, pharmaceuticals	No 1 in Europe for trimellitic anhydride and malic acid No 1 in Europe and co-leader worldwide for fumaric acid
	Pure isophthalic acid and meta xylene	Unsaturated polyester resins, PET bottle grade, paints and coatings	Among Asia's leading producers
Special anhydrides and esters	Succinic anhydrides, hydrogenated anhydrides, hardeners for epoxy resins, tetrahydrophthalic, diethylacetyl succinate, tetrahydrophthalimide, dimethylsuccinate, other esters.	Electrical equipment and electronics, paints and pigments, additives in plastics, pharmaceutical and agricultural products	No 1 worldwide
Plasticizers	General-purpose and special plasticizers: linear phthalates, polymeric, trimellitates	Plasticizers for PVC, electrical equipment, automotive, furnishing, clothing, sport	No 1 in Europe for special plasticizers
Resins	Unsaturated polyester resins and derivatives (gel-coats)	Nautical engineering, construction and transport industries, electrotechnical equipment, sport, furniture, sanitary wear	Among Europe's leading producers
Compounds	Technocompounds and molded composites: BMC, SMC, TMC	Electrical equipment and electronics, construction and transport industries	No 2 in Europe for technocompounds
Catalysts and technologies	Catalysts and technologies, custom manufacturing of catalysts	Production of phthalic and maleic anhydride, pyromellitic anhydride and formaldehyde	No 1 worldwide: catalysts for maleic anhydride No 1 worldwide: fluid bed technology for maleic anhydride
Key technologies	<p>Oxidation</p> <p>Vapor phase (fixed and fluid bed)</p> <p>Liquid phase</p> <p>Epoxydation</p> <p>Esterification</p> <p>Hydrogenation</p> <p>Diels-Alder reaction</p> <p>Double-bond addition (hydration)</p>	<p>Isomerization</p> <p>All technologies for the production and development of heterogeneous catalysts</p> <p>Compounding technologies</p>	



Sales by marketing area

Category	Location	Count
Production sites	China	1
	Germany	1
	Italy	4
	Singapore	1
	Total	7
Research and development sites	Italy	3

Locations



Our commitment is to be the preeminent supplier to the life sciences industry through chemicals and biotechnology platforms driven by an unrelenting passion to unambiguously deliver value to our customers to enable our employees to be successful to continuously improve performance and to make Lonza a recognized contributor to its communities

To realize the objectives of our corporate vision, all employees must be able to keep step with the rapid pace of change and overcome seemingly insurmountable barriers. The nurturing and advancement of our personnel play a vital role in this endeavor. Ultimately, the company's success depends on the effort and commitment of our people, achieving top results and living our culture and values to the full.

The Lonza Code of Conduct¹ is the basis for the behavior and activities of all employees as they strive to fulfill the company's social and ethical responsibilities. The Code covers the core areas of legal affairs, trade controls, safety, health and environmental protection, discrimination, conflicts of interest, insider trading, fair competition, use and protection of assets and confidential information, as well as business relations.

Lonza Human Resources Management sees itself as an internal service. HR staff support and advise the operational units in all personnel matters. Its ambit includes the realization of the corporate vision and values, and the creation of a climate in which working conditions are optimized and the focus is on organizational development, team building and the advancement of employees.

Personnel management is governed by clear objectives which require each and every employee to take individual responsibility, underpinned by an entrepreneurial approach oriented towards customers and markets. We have formulated criteria for executives; superiors are seen as coaches whose task is to shape the development and learning process and motivate employees to perform to the best of their ability.

¹ <http://www.lonza.com/group/en/company/corporate/policies.html>

Personnel development – In December 2003, Lonza's worldwide operations counted 5 659 employees. The proportion of female employees was 17%. In the area of biotechnology, the corresponding proportion is approximately 45%, substantially higher than in traditional chemical activities. As part of our initiative on organizational and personal development, more than 400 executives and staff with leadership potential had the opportunity to participate in management training programs during 2001 and 2002. Encouraged by the positive results, we decided to open up focused management training for more employees in 2003. The programs for team leaders and line managers were designed by the participants themselves in consultation with their superiors and taking into account the specific requirements of their actual work situations. More than 250 young candidates took part in the 2003 management development program. Training in specialist skills is another priority: most of our employees have attended various training and continuing education courses. In Switzerland, apprenticeship schemes have played a key role in training for many years. In 2003, more than 160 apprentices attended three- to four-year training courses in close collaboration with the local vocational training institutions.

We are firmly convinced that companies can only achieve long-term success if their employees are well prepared for the highly responsible and complex demands of the future through continuing education and customer- and market-oriented working practices.

Compensation – The pay and salary system at Lonza rewards effort and achievement of goals by individuals and teams. The overall compensation comprises a basic salary plus variable components. As a result, the majority of employees – including those subject to a collective employment contract – receive performance-related compensation, with an incentive component that can reach as much as 40% of the annual salary, depending on grade.

Another kind of reward is represented by the share purchase program for all employees and

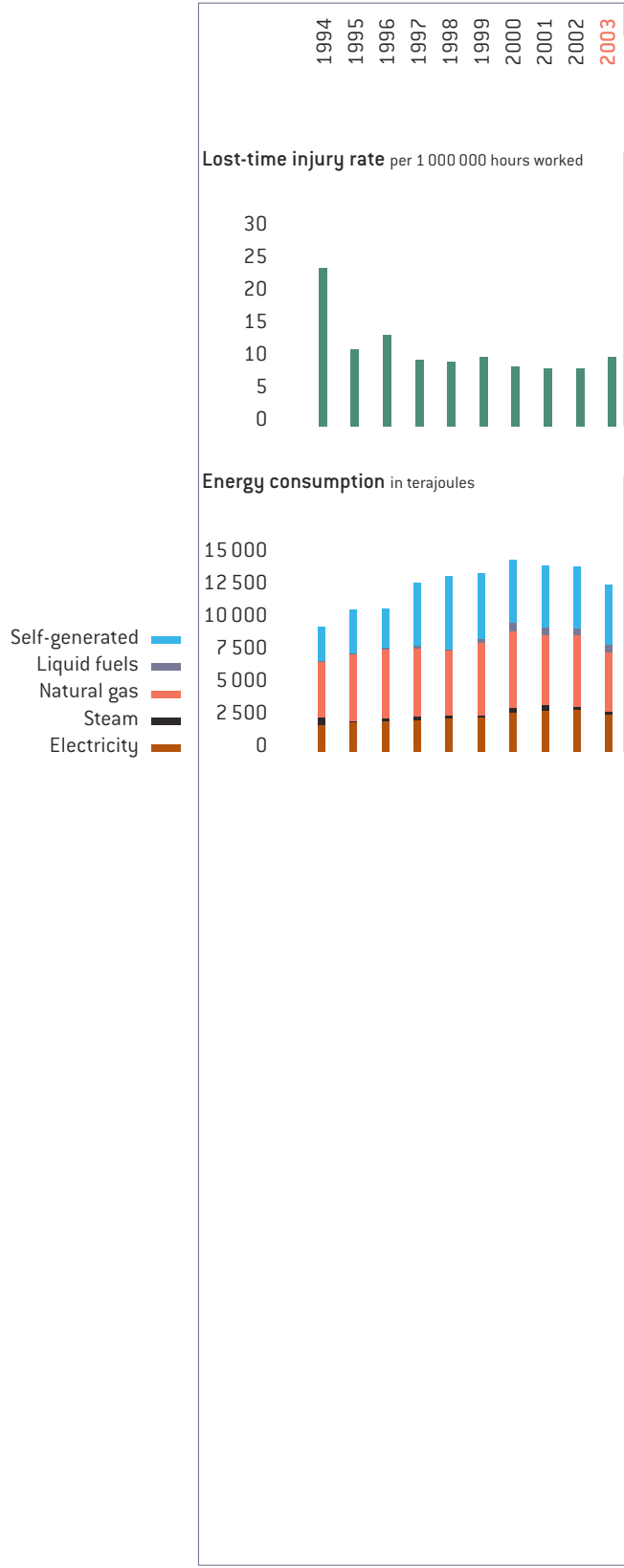
the options scheme for executives in key positions. These long-term incentive programs strengthen the alignment of employees' activities with the overall objectives of the company.

Responsibilities – Lonza is conscious of its social responsibilities as an employer. Owing to natural fluctuations, but above all to the difficult economic situation and the restructuring measures it necessitated, the headcount within the Group decreased by 9% in 2003. Employees affected by these measures received appropriate benefits packages. We work with local employee representatives and trade unions as social partners in such matters.

Worldwide, nearly 50% of our employees are unionized. There is also a European Works Council to which Swiss employees are affiliated.

Working environment – We conduct regular employee surveys in an effort to find out what our people think of their working conditions and the personal and organizational development initiatives, and to ascertain what progress has been achieved in these areas. The results of the surveys are discussed in workshops by small teams which formulate specific action plans for immediate implementation.

We aim to offer stimulating and demanding jobs. Talented, committed employees should have the chance to achieve their professional development goals and, by dint of their efforts and commitment, to gain the greatest possible satisfaction in their chosen careers.



Sustainability and SHE policy – Lonza is committed to the principle of sustainability. To run a business sustainably means that its commercial, ecological and social responsibilities as an economic entity must be met in such a way that business activities can be sustained in the long term, while the freedom of future generations to develop their potential and build a successful society is safeguarded. This part of the annual report concentrates on the fulfillment of our environmental responsibilities. Lonza bases its activities on the explicit Policy on Safety, Health and Environment (SHE), summed up in the following nine principles.

- 1 We actively manage SHE as an integral part of our business and operations practices, and apply comprehensive SHE management systems.
- 2 We require our regional and local managements to comply in their area of responsibility with the applicable laws and the internal and external SHE requirements.
- 3 We strive to minimize the environmental impact of our operations and business practices as well as to optimize the use of natural resources by our processes and products.
- 4 We will maintain a safe workplace environment for our employees and provide appropriate information and training to increase their skills and promote their safety, health and environmental awareness. All employees have a fundamental responsibility for SHE aspects at work.
- 5 We are committed to continuous improvement of our SHE performance and measure the progress by specific SHE performance indicators. We promote measures to increase the ecoefficiency of our investments and optimize our cost for SHE, while maintaining technological competitiveness.
- 6 We operate only processes, apply technologies and develop and handle products, which are assessed for their SHE risks. Safe handling and use of our products is to be guaranteed internally as well as communicated externally. New or modified processes and installations must be subjected to a systematic risk assessment prior to introduction.

7 We have emergency procedures in place and emergency response organizations at all our sites to control and to limit the impact of incidents and threats. All internal and external communication channels in case of an emergency are defined and operable.

8 We audit our operations, business and management practices at all our sites with regard to SHE performance and compliance through independent experts at least once every three years.

9 We openly communicate and provide information on our SHE performance to our employees, customers, shareholders and investors, governmental authorities and the public at large.

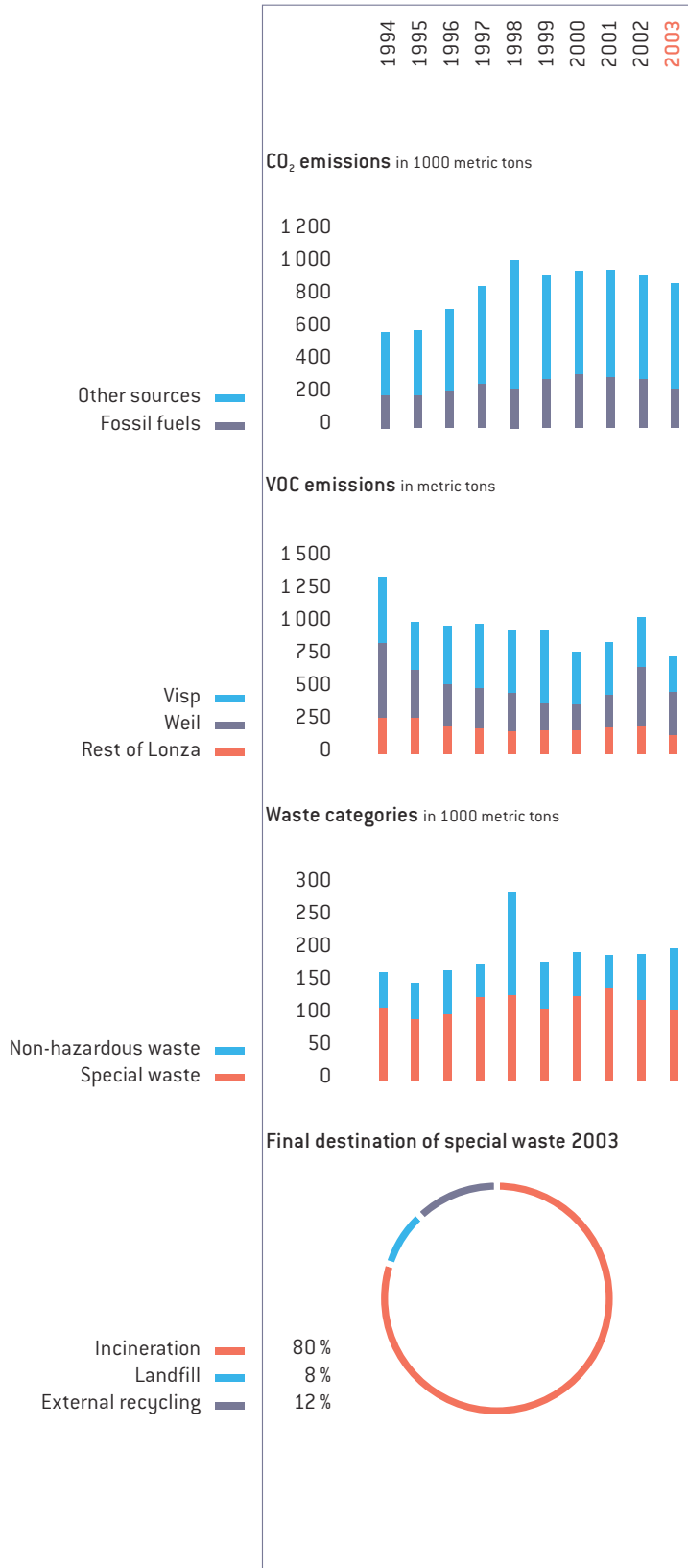
Lonza has nominated people on all levels of line management – from the Management Committee down – who are responsible for implementation of the Group's SHE policy, with support from specialists in the corporate functions. SHE awareness is an integral part of our activities, and SHE management systems guarantee that all projects and processes, across all our sites, are monitored by SHE specialists from the outset. Of the Group's more than 5 600 employees, a total of 180 work directly in the SHE area. In 2003, the operating expenses for SHE amounted to CHF 55.6 million, a fall of 11 % compared with the previous year. By contrast, SHE capital expenditure in 2003 rose by 53 % to CHF 40.5 million, which represents 1.8 % of net sales and 9.6 % of the Group's total investments in fixed assets.

SHE performance indicators – For the last ten years, Lonza has collected data on an annual basis for 45 SHE performance indicators. These are monitored at all sites, using a uniform, standardized schema, covering SHE costs and personnel, safety and accidents, energy and water consumption, air and water emissions, and waste. Details of the indicators, including definitions, are posted on the Group website www.lonza.com/group/en/company/activities/she/performance.html. In the following, we give a rundown of the key indicators for the Group. In keeping with our usual practice, we use the

absolute data for the consolidated Group figures, since the indexed figures in the form of efficiency indices are not particularly meaningful owing to the very heterogeneous mix of products and processes.

Safety – The downward trend observed over the last few years was not sustained. The Group-wide accident rate in 2003 was 10.8 accidents per million hours worked, representing an increase of 20 % compared with the previous year. However, this result does not reflect the wide variations among the different locations. It is to be welcomed that five of the 18 production sites reported no accidents in 2003. The US sites at Bayport and Mapleton were actually able to report seven and five years of accident-free operation respectively. All our facilities have accident-prevention programs in place, and all employees are trained in the safe handling of equipment and chemicals, safe process management and safety-conscious behavior. At the Visp site, particular attention is paid to a more intensive and specific compliance with occupational hygiene measures in production, necessitated by the increased use of pharmaceutical active substances. The substances handled are divided into four industrial hygiene categories, and a work instruction sets out binding guidelines for the appropriate technical, organizational and personal safety precautions. In the Group as a whole, no major incidents or breakdowns were reported which underlines the fact that the measures specified in the SHE policy and the safety management systems are being implemented and complied with. Nor were there any reported transportation accidents involving Lonza products.

Energy and water consumption – In energy-intensive chemical production, energy input is not only a significant cost factor, but it is also important that energy resources be used responsibly. The ongoing search for more efficient ways of utilizing energy and for an energy mix optimized for sustainability is a vital concern at all our sites, and in the year under review this yielded the desired results. For example, three



energy-conservation projects were developed at the Visp facility in 2003. One of these is ready for implementation and the other two are in the final stages of realization. They will bring considerable reductions in the consumption of steam and therefore also of natural gas. In 2003, two refrigeration plants were converted to work at condensation temperatures adapted to the temperature of the river water, thus contributing to a substantial reduction in electricity consumption. The first results of these measures confirm the anticipated energy-saving effects.

The Group's total energy requirement in the year under review was 12 356 terajoules, 10% lower than in 2002. Apart from the drive to improve energy efficiency, the slowdown in economic activity contributed to this decrease. The main energy sources used by Lonza are: utilization of waste (36%), natural gas (35%) and electricity (22%). Liquid fossil fuels account for only 5% of the overall energy consumption. Around 60% of the electrical energy used came from hydroelectric generation and therefore belongs in the category of renewable resources. The proportion of non-renewable fossil fuels is therefore around half the Group's total energy consumption.

Lonza's water requirements are divided into cooling water and process water. The cooling water systems are all closed-circuit and differ only in the method of heat removal. At most locations, cooling towers are used as heat exchangers, while at our biggest facility, Visp (CH) river water is used. Unlike cooling water, process water emerges as polluted effluent and must be treated before it can be fed back into a natural waterway. The process water requirements in 2003 were unchanged at 12 million cubic meters, almost the same level as the previous year. The largest single user is the production plant at Scanzorosciate (IT), which required 6.5 million cubic meters.

Air emissions – The lower energy requirements also brought a reduction of carbon dioxide (CO₂) emissions, further intensified by the realization of measures to increase energy efficiency. Com-

pared with the previous year, the total output of the greenhouse gas CO₂ dropped in 2003 by 5% to 856 000 metric tons, with the proportion of CO₂ produced by burning fossil fuels at 27% (previous year: 32%).

The specific energy-saving and waste-gas treatment measures at Visp and at our Weil site (DE) also had a positive influence on emissions of volatile organic compounds (VOC). Total VOC emissions for 2003 amounted to 719 metric tons which represents a 29% reduction in emissions compared with the previous year. The contribution of halogenated VOCs was 344 metric tons. Emissions of nitrogen oxides and sulfur dioxide remained constant around the previous year's levels; particulate matter emissions fell substantially [−25%].

Water emissions – The lead parameters for water pollution are total organic carbon (TOC), heavy metals, phosphorus and nitrogen. The overall level of contamination was low and relatively constant, demonstrating that the water treatment measures adopted are effective. Details on water emissions are published on our website.

Waste – Lonza has a specialized waste disposal concept at all its sites. Material flows are analysed and, as far as possible, waste is avoided or recycled. Where neither of these options is open, waste-specific disposal systems are instituted. Lonza ensures that the disposal of all waste materials, specifically the so-called special wastes, is conducted within the legal framework and respects environmental integrity. The total quantity of waste produced by Lonza in 2003 was 195 600 metric tons, of which 104 300 metric tons consisted of special (hazardous) wastes and 91 300 metric tons of non-hazardous household-type wastes or inert materials. The volume of waste produced in both categories is subject to substantial annual fluctuations and influenced in particular by investments in construction projects such as extensions and new buildings involving large-scale excavations or remediation of existing buildings and installations. In either case,

depending on the level of contamination, special wastes or non-hazardous wastes may be produced. The means of disposal for both categories are typically very diverse: in 2003, 92% of special waste materials were incinerated or recycled, while in the case of non-hazardous waste, the corresponding figure was only 58%.

Social integration and dialogue – At all its sites, Lonza maintains a good and balanced relationship with other stakeholders. For all our local managements, close contacts with the authorities and neighborhood are just as much a matter of course as involvement in local cultural and sporting activities. In the case of expansion or remediation projects, Lonza seeks to open lines of communication with the authorities as well as environmental and nature conservancy organizations, because their views and misgivings are important to us. Through active participation in national and international bodies (ACC, SSCI, CEFIC, OECD)¹ and commitment to the Responsible Care® programs of the chemical industry, Lonza is contributing to advances in the safe handling of chemical raw materials, products and waste substances as well as in the sustainable use of raw materials and lessening the impact on the environment. For example, as part of its involvement in the Associate Program of OPCW², Lonza provided four participants who compiled a risk study with further training in the field of chemical safety. The idea behind the program is to give participants from emerging and developing countries an insight into process safety at a modern chemical or pharmaceutical company through participation in a practical project. This contributes to so-called “capacity building” in the framework of the Chemical Weapons Convention. We firmly believe that such activities are important for society.

¹ ACC American Chemistry Council; SSCI Swiss Society of Chemical Industries; CEFIC European Chemical Industry Council; OECD Organisation for Economic Co-operation and Development

² OPCW Organization for the Prohibition of Chemical Weapons

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1. Group structure and shareholders

Operational Group structure 1.1

Modern corporate governance at Lonza – Lonza is fully committed to good corporate governance and complies with the corporate governance directive of the SWX Swiss Exchange. The principles and rules of Lonza Group Ltd are laid down in the Company's Articles of Association¹, the Regulations Governing Internal Organization and Board Committees, and the Code of Conduct¹.

Lonza is a life-sciences-driven company, headquartered in Basel, Switzerland, which operates 18 production and R & D facilities in eight countries. Its activities are organized in four business sectors. The business sectors function as profit centers and bear full responsibility for their business activities. Lonza is the leading custom manufacturer of active chemical ingredients, intermediates and biotechnology solutions for the pharmaceutical and agrochemical industries. It also offers organic intermediates for a wide range of applications, antimicrobial and associated products, as well as polymer intermediates and compounds. A detailed description of Lonza's worldwide activities is available on Lonza's website: www.lonza.com/group/en/company/overview.html.

Principal subsidiaries and affiliates – The companies belonging to Lonza Group are all non-listed entities. The principal subsidiaries and affiliates are shown on page 62 of this report and may also be downloaded from Lonza's website <http://www.lonza.com/group/en/company/corporate/principal.html>. They represent 97.6 % of the revenue of the Group.

Principal shareholders 1.2

The following table sets forth the identities of those Lonza Group Ltd shareholders and their respective shareholdings with more than 5 % of voting rights.

Number of shares at CHF 1 par value		31.12.2002		31.12.2003
		%		%
EMS-Chemie Holding AG, Domat/EMS (Switzerland)	5 727 042	11.35	11 359 047	22.52
Zurich Cantonal Bank, Zurich (Switzerland)	2 537 480	5.03	n.a.	n.a.

On 19 December 2003, EMS-Chemie Holding AG notified Lonza Group Ltd that it exceeded the threshold of 20 % of the voting rights of Lonza Group Ltd and holds 11 359 047 nominal shares representing 22.52 % of the voting rights. The changes are caused by the exercise of the put options issued and sold by EMS-Chemie Holding AG, which would have expired in December 2003.

On 29 December 2003 Zurich Cantonal Bank informed Lonza Group Ltd that its participation in the voting rights of Lonza Group Ltd fell below the threshold of 5 % as per 19 December 2003.

Lonza Group Ltd knows of no other shareholder that owned more than 5 % of the total share capital of Lonza Group Ltd as at 31 December 2003. To the best knowledge of Lonza Group Ltd, the above-mentioned shareholders are not linked by any shareholders' agreement or similar arrangement with respect to their shareholdings in Lonza Group Ltd or the exercise of shareholders' rights.

Changes that occurred between the balance sheet date and the date of the auditors' report are recorded on page 77.

Cross-shareholdings 1.3

Lonza Group Ltd has not entered into any cross-shareholdings.

¹ The specified documents may be downloaded from Lonza's website: www.lonza.com/group/en/company/corporate.html

2002

2003

The share capital as of 31 December 2003 amounting to CHF 50 450 000 comprised 50 450 000 registered shares with a par value of CHF 1 each.

Share capital
2.1

	Shareholders	Shares	Shareholders	Shares
	%	%	%	%
Switzerland	94.44	42.00	94.44	45.40
Great Britain	0.42	10.74	0.47	6.12
Germany	2.19	1.59	1.95	1.70
USA	0.39	0.14	0.56	4.36
Others	2.54	4.22	2.57	2.95
Shares in transit		35.21		33.38
Treasury shares without voting rights	0.02	6.10	0.01	6.09
Total	100.00	100.00	100.00	100.00
Total number of shares		50 450 000		50 450 000

As of 31 December 2003, Lonza Group Ltd had no authorized or conditional capital at its disposal.

Authorized and conditional capital
2.2

	Share capital	Registered shares	Par value/share	Changes in capital
31 December 2000	CHF 64 339 850	6 433 985	CHF 10	2.3
31 December 2001	CHF 55 260 070	5 526 007	CHF 10	
31 December 2002	CHF 50 450 000	50 450 000	CHF 1	
31 December 2003	CHF 50 450 000	50 450 000	CHF 1	

On 28 March 2001, the Ordinary Shareholders' Meeting approved the cancellation of 907 978 shares with a par value of CHF 10 each, repurchased at a gross price of CHF 940 per share.

On 27 March 2002, the Ordinary Shareholders' Meeting approved the following changes in the capital structure of Lonza Group Ltd:

1. Cancellation of 481 007 shares with a par value of CHF 10 each, purchased at an average price of CHF 997 per share.
2. Stock split in a ratio of 1:10, bringing the par value of Lonza Group Ltd shares to CHF 1 each.

million CHF	Reserves and retained earnings	Net income
31 December 2001	1 129	402
31 December 2002	964	221
31 December 2003	1 094	91

For additional information, please refer to the consolidated statement of shareholders' equity, displayed on page 54 of this report.

Lonza Group Ltd registered shares, with a par value of CHF 1, are listed on the SWX Swiss Exchange and included in the Swiss Market Index (SMI). They are traded on the virt-x, an electronic trading system in London.

Shares and participation
certificates
2.4

Lonza Group Ltd has not issued any participation certificates (non-voting shares).

Security number: 1 384 101 (valor), stock symbol: LONN (Telekurs)

Bonus certificates

2.5

Limitations on transferability and nominee registrations

2.6

Convertible bonds and options

2.7

On 31 December 2003, Lonza had a market capitalization of CHF 3 587 million (2002: CHF 4 238 million).

Lonza Group Ltd has not issued any non-voting equity security (Genussscheine, bonus certificates).

Purchasers of registered shares declaring that they have acquired these shares in their own name and for their own account will be entered without limitation as shareholders with voting rights in the share register. Persons who do not declare to have acquired the respective shares in their own name and for their own account are considered “nominees” and will be entered with voting rights in the share register up to a maximum of 2 % of the share capital unless the actually entitled persons are revealed. The details are set out in Art. 6 of the Company’s Articles of Association.

Convertible bond – In June 2002, Lonza Finance Limited, St. Helier, Jersey (GB), raised CHF 300 million via a convertible bond, due 2006, with a 2 % p.a. fixed interest rate. The bond is convertible into Lonza Group Ltd shares from 1 July 2002 up to and including 21 June 2006 at a conversion price of CHF 135 per share. Each bond of CHF 5 000 principal amount is convertible into initially 37.03704 shares with a par value of CHF 1. The purpose of the issuance of the convertible bond has been to purchase shares under the share repurchase program and for general corporate purposes. The usual risk with convertible bonds is the risk that the conversion will not be executed at the end of the conversion period.

In conjunction with this convertible bond, Lonza Finance Limited, St. Helier, Jersey (GB), purchased 2 222 222 shares in Lonza Group Ltd, with a par value of CHF 1 each, in the period from 12–25 June 2002. The average purchase price was CHF 118 net per registered share.

Options – Options granted to the Members of the Board of Directors and the Members of the Management Committee are mentioned under section 5.6 below. Disclosure of all options outstanding is provided in the notes to the consolidated financial statements (pages 73 and 74). No options or similar instruments have been issued by the Company or any of the Group entities.

The Board of Directors is made up of non-executive members and comprises four Swiss and two non-Swiss members.



Sergio Marchionne (1952), Canadian and Italian, Chairman of the Board of Directors and Member of the Compensation Committee
Licensed Barrister and Solicitor, Chartered Accountant and Certified General Accountant. Obtained a Bachelor of Laws from the Osgoode Hall Law School, York University, Toronto, and holds a Master of Business Administration from the University of Windsor, Canada

- Chairman of the Board of Directors of Lonza Group Ltd, Basel (since October 2002)
- Member of the Board of Directors of Lonza Group Ltd, Basel (since September 1999)
- Member of the Board of Directors of Société Générale de Surveillance Holding SA (since May 2001)
- Managing Director and Chief Executive Officer of Société Générale de Surveillance Holding SA, Geneva (since February 2002)
- Managing Director and Chief Executive Officer of Alusuisse Lonza Group Ltd, Zurich (1997–2000)
- Managing Director and Chief Executive Officer of Lonza Group Ltd, Basel (November 1999–January 2002)
- Member of the Board of Directors of Sero Ltd, Geneva (since May 2000)
- Member of the Board of Directors of Fiat SpA, Turin, Italy (since May 2003)

Activities and functions
3.2



Bernard Mach (1933), Swiss, Vice-Chairman of the Board of Directors and Member of the Compensation Committee
MD from the University of Geneva and PhD from Rockefeller University, New York. Until his retirement in 1998, Bernard Mach was Professor of Molecular Genetics and Chairman of the Department of Genetics and Microbiology at the University of Geneva Medical School

- Vice-Chairman of the Board of Directors of Lonza Group Ltd, Basel (since October 2002)
- Member of the Board of Directors of Lonza Group Ltd, Basel (since March 2001)
- Founder and former Board member of Biogen Inc., Geneva, then Boston
- Member of the Board of Directors of Sero Ltd, Geneva (since 1997)
- Founder and Chairman of the Scientific Board of Lombard Odier Immunology Fund, Geneva (since 1995)
- Founder and Chairman of NovImmune SA, Geneva (since 1998)
- Member of the Swiss Research Council (1969–1980)
- President of the Union of Swiss Societies for Experimental Biology (1990–1993)
- Member of the French Academy of Sciences (since 1995)



Peter Kalantzis (1945), Swiss and Greek, Member of the Board of Directors and Chairman of the Audit Committee
PhD in economics from the University of Basel. Industrial Consultant

- Member of the Board of Directors of Lonza Group Ltd, Basel (since September 1999)
- Executive Vice-President of Alusuisse Lonza Group Ltd, Zurich (1991–2000)
- Chairman of the Board of Directors of Mövenpick Holding, Cham (since 2001)
- Chairman of the Board of Directors of PrivatAir Holding SA, Geneva (since 2001)
- Acting President of the Swiss Society of Chemical Industries (2001–2002)
- Member of the Executive Board of economiesuisse (2001–2002)
- Member of the Board of Directors of Hansa AG, Basel (since 2003)



Rupert Gasser (1938), Swiss and Austrian, Member of the Board of Directors and Member of the Audit Committee

Graduated in Chemistry from the Technical Academy for Chemical Industry in Vienna, Austria

- Member of the Board of Directors of Lonza Group Ltd, Basel (since September 1999)
- Executive Vice-President, Nestlé SA (1992–2002)
- Member of the Board of Directors of Alusuisse Lonza Group Ltd, Zurich (1992–2000)
- Member of the Board of Directors of Alcan Aluminium Ltd, Montreal (2000–2001)
- Member of the Board of Syngenta Ltd, Basel (since 2002)
- President of Nestec Ltd, Vevey (since 2001)
- Member of Alcon Scientific Advisory Board, Fort Worth (since 2003)



Sir Richard Sykes (1942), British, Member of the Board of Directors and Chairman of the Compensation Committee

PhD in Microbial Biochemistry from Bristol University and DSc from the University of London. Fellow of The Royal Society. Member of a number of government and scientific committees. Holds a number of honorary degrees and awards from institutions both in the UK and overseas

- Member of the Board of Directors of Lonza Group Ltd, Basel (since March 2003)
- Rector of Imperial College, London (since January 2001)
- Served as President of the British Association for the Advancement of Science (1998–1999)
- Received his knighthood in the New Year Honours List for services to the pharmaceutical industry (1994)
- Chairman and Chief Executive of Glaxo Wellcome plc, London (1997–2002)
- Deputy Chairman and Chief Executive of Glaxo plc (1993–1997)
- Deputy Chief Executive of Glaxo Group Research Ltd, London, and Group Research and Development Director of Glaxo plc, London, and Chairman and Chief Executive of Glaxo Group Research Ltd (1987–1993)
- Vice-President, Infectious and Metabolic Diseases, Squibb Institute for Medical Research, Princeton, New Jersey (1983–1986)
- Director of Microbiology and Associate Director, Squibb Institute for Medical Research, Princeton, New Jersey (1979–1982)
- Head of the Antibiotic Research Unit of Glaxo Research Ltd, London (1972–1978)



Peter Matter (1941), Swiss, Member of the Board of Directors and Member of the Audit Committee
Education in banking

- Member of the Board of Directors of Lonza Group Ltd, Basel (since March 2003)
- Chairman of the Board of Directors of Swissfirst Asset Management Ltd, Zug (since 2000)
- Head of Portfolio Management and Group Treasurer of F. Hoffmann-La Roche Ltd (1969–1999)
- Member of the Board of Directors of EMS-Chemie Holding AG, Domat/Ems (since 2000)

None of the Members of the Board of Directors had any cross-involvement or important business connections with Lonza in the period under review. Sergio Marchionne was the only member of the Board of Directors to have served on the Management Committee of Lonza. He resigned as Chief Executive Officer (CEO) of Lonza on 1 February 2002.

Cross-involvement
3.3

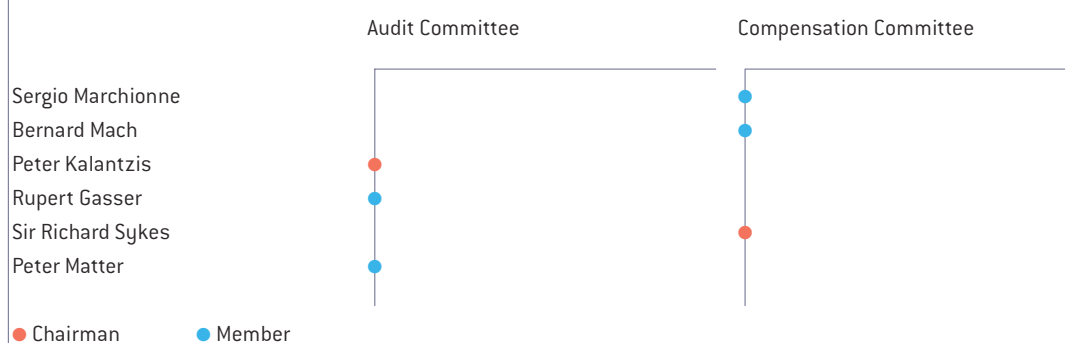
The members of the Board of Directors are elected by the Ordinary Shareholders' Meeting for a term of one year; re-election is possible. The Board constitutes itself and elects from amongst its members the Chairman and the Vice-Chairman.

Elections and terms of office
3.4

In accordance with the law and the Articles of Association, the Board of Directors is the supreme management body of the Group. It consists of the Chairman, the Vice-Chairman and the other members. In accordance with the Articles of Association the number of members must be at least three.

Internal organizational structure
3.5

The members of the Board of Directors sit on the following committees:



The Board of Directors is responsible for the tasks assigned to it according to Art.18 of the Company's Articles of Association and the Regulations Governing Internal Organization and Board Committees. It defines the strategic direction and is responsible for the ultimate management of Lonza and the supervision of the persons entrusted with Group management, especially with regard to compliance with the law, the Articles of Association, the regulations and the directives. The Board of Directors is entitled to issue the necessary instructions. In compliance with Swiss law and the Articles of Association, it has delegated the management of the Company to the Management Committee, with the exception of non-delegable and inalienable duties.

Definition of areas of responsibility
3.6

Organizational structures and control instruments – The Board of Directors continues to commit itself to maintaining the highest standards of integrity and transparency in its governance of Lonza. The Regulations Governing Internal Organization and Board Committees set out in detail the powers and responsibilities of the Board of Directors, its Committees and the Management Committee. The standing Board Committees in the areas of audit and compensation provide modern corporate governance guidance and support to the Board of Directors.

Broad supervisory and reviewing powers are held by the Board of Directors which is directly supported by Internal Auditing.

The Regulations Governing Internal Organization and Board Committees confer on the CEO the duty to inform the Management Committee and – together with the Chairman – the Board of Directors on

the business activities and all important business transactions including risk issues. The Board of Directors meets periodically with the Management Committee or its subcommittees for business updates and decisions on actions to be taken.

Audit Committee – The Audit Committee which currently includes three members of the Board of Directors, who are all independent of Lonza, meets and consults regularly with the Management Committee, the internal auditors and the independent auditors to review the scope and results of their work. The internal and independent auditors have full and free access to the Audit Committee. The Audit Committee reviews the systems of internal control and financial reporting.

Compensation Committee – Compensation matters have been delegated within the framework of the Board of Directors' competencies. The Compensation Committee takes decisions on the terms of employment of members of the Board of Directors and the Chief Executive Officer. The Compensation Committee and the Chief Executive Officer take decisions on the terms of employment of the members of the Management Committee.

Board meetings – During 2003, the Board of Directors met formally for full Board meetings on nine occasions. In addition, the Chairman and the Vice-Chairman supported the Management Committee through regular contacts.

Information and control instruments 3.7

Lonza maintains a system of internal financial and accounting policies, procedures and controls to provide a reasonable assurance, given the inherent limitations of all internal control systems, at appropriate cost, that transactions are executed in accordance with company authorization, that they are properly recorded and reported in the financial statements, and that assets are properly safeguarded. Lonza's internal auditors comprise two experts who continually evaluate the adequacy and effectiveness of this system of internal accounting policies, procedures and controls, and take appropriate action to correct deficiencies as they are identified. In 2003, they delivered 13 internal audit reports to the Audit Committee.

In addition to the documents required to pass resolutions, the Board of Directors receives the following reports at its regular meetings:

- Quarterly reports on the sales and earnings performance of the company with the relevant market information in the same period since the beginning of the year, structured by divisions/business sectors with the main sales areas and key product groups
- A quarterly report on the cash flows, debt and debt-equity ratio, plus other relevant key figures for the Group
- Regular qualitative assessments of the divisions/business sectors and major subsidiaries
- Audit reports prepared by the internal and Group auditors
- Regular analysis of the shareholder structure
- Annual overview of the Group's key staff benefit schemes including pension funds
- In cases involving extraordinary events of considerable commercial relevance, the Board of Directors receives direct, immediate information.

The Management Committee is appointed by the Board of Directors of Lonza Group Ltd. It performs the duties assigned to it by the Board of Directors, either under the terms of the Regulations Governing Internal Organization and Board Committees or additional tasks as delegated. It is responsible for leading Lonza, especially for developing and implementing the Lonza policy and strategy after approval by the Board of Directors. It supports and coordinates the activities of the business sectors and the corporate functions. It is also responsible for leadership development and succession planning.

At 31 December 2003, the Management Committee consisted of nine active members. Due to changed market conditions and the impact they had on Lonza's operations in 2003, the Management Committee was reduced to six members in January 2004.

Members of the Management Committee
(status February 2004)
4.1



Markus Gemuend (1958), Swiss, Chief Executive Officer
Holds a degree in law from the University of Basel, Switzerland

- Chief Executive Officer since February 2002
- Member of the Management Committee since August 2001
- Head of the Biologics business sector (August 2001–January 2004)
- Director of marketing and sales with responsibility for the Exclusive Synthesis business sector in the US (October 1998–July 2001)
- Counsel for Exclusive Synthesis and Biotechnology (1994–1998)
- Joined the legal department of Lonza Ltd, Basel, in 1988

Markus Gemuend advised the Board of Directors in January 2004 of his decision to step down from his position as CEO of Lonza Group Ltd. He will retain his responsibilities until a successor is appointed.

Activities and functions
4.2



Beat In-Albon (1952), Swiss, Head of Organic Fine and Performance Chemicals
Holds a PhD in economics from the University of Fribourg, Switzerland

- Member of the Management Committee since November 1999
- Head of Organic Fine and Performance Chemicals since June 2003
- Head of the Organic Fine Chemicals business sector (1998–May 2003)
- Joined Lonza in 1983 as assistant to the Head of the Agrochemical Department and subsequently held various managerial positions at Lonza Ltd, Basel (Switzerland)



Gerhard Klement (1952), German, Head of the Biopharmaceuticals business sector
Holds a PhD in Biotechnology from the University of Agriculture in Vienna, Austria

- Member of the Management Committee since July 2003
- Head of the Biopharmaceuticals business sector since February 2004
- Chief Operating Officer Biopharmaceuticals since June 2003
- Joined Lonza in January 2003 as Head of the Portsmouth, NH (USA), operations
- Worked in various functions for Centocor, Leiden (The Netherlands) and St. Louis, MO (USA), Laboratories Serono, Aubonne and Vevey (Switzerland) and Ares Serono, Geneva (Switzerland) and Boston (USA)



Lukas Utiger (1963), Swiss, Head of the Exclusive Synthesis business sector
Holds a PhD in chemical engineering from Imperial College, London, UK

- Member of the Management Committee since August 2001
- Head of the Exclusive Synthesis business sector since August 2001
- Head of Research and Development in the Exclusive Synthesis business sector (October 2000–July 2001)
- Joined Lonza as R&D chemist in 1992 and became R&D group leader for fine chemicals in 1998
- Acquired his business experience at ICI Chemicals & Polymers division in Runcorn (UK) from 1988–1992



Rosario Valido (1952), Italian, Head of Polymer Intermediates
Chartered accountant with degree from the University of Milan, Italy

- Member of the Management Committee and Head of Polymer Intermediates since July 2002
- Managing Director of Lonza SpA, Scanzorosciate (Italy), and Chairman of Lonza Compounds, Brembate and Lonza Composites, Scanzorosciate (Italy) since July 2002
- Deputy Head of the Polymer Intermediates business sector (2001–June 2002)
- General Manager of Anhydrides and Chemicals (1999–2001)
- General Manager of the Resins and Compounds business unit (1995–1999)
- General Manager of the Resins business unit and Site Manager at San Giovanni Valdarno (Italy) (1992–1995)
- Member of the Management Committee of Lonza Polymer Intermediates since 1992
- Joined Lonza in Italy in 1982 as Commercial Director of the Resins business unit



Roland Waibel (1958), Swiss, Chief Financial Officer
Graduated in economics from the University of Berne, Switzerland, with a PhD in Operations Research

- Member of the Management Committee since November 1999
- Chief Financial Officer since April 2003
- Group Controller (October 2001–March 2003)
- Responsible for Group IT since November 1999
- Head of Corporate Development since November 1999
- Director of Finance and Controlling of Lonza Ltd since 1997
- Joined Lonza in 1989 as Divisional Controller in the Plastics division and held several positions in Aluisse Lonza Services Ltd, Zurich (Switzerland) and Lonza Ltd in Basel and Visp (Switzerland)

Management contract
4.3

Lonza Group Ltd and its subsidiaries have not entered into management contracts with third parties.

The Compensation Committee administers the Lonza Executive Salary Plan, Incentive Plan and Stock Option Plan.

Lonza periodically retains outside compensation and benefits consultants to compare base salary and incentive compensation programs for its employees with those of other leading industrial companies. The Compensation Committee consults with the Head of Human Resources on general matters concerning compensation, pension and welfare benefit plans. The Lonza compensation programs consist of the Lonza Salary Plan, Incentive Plan and the Share Option Plan. The overriding objective of the Company's remuneration policy is to offer market- and performance-oriented remuneration and to motivate the employees to create shareholder value.

The Members of the Board of Directors may elect payment in cash and shares whereby the cash portion cannot exceed 40 %. The members of the Management Committee may receive the compensation in the form of cash (base salary) or share options (incentive). If they opt for share options, the cash portion is 50 %.

The Members of the Board of Directors are reimbursed for travel and other related expenses associated with the performance of their services for Lonza.

Payments to acting members of the Board of Directors of Lonza Group Ltd totaled CHF 1.837 million, 22.86 % or CHF 420 000 in the form of cash and 77.14 % in the form of shares (number of shares: 24 230). The compensation system for Board members allows them to choose either a payment in shares or a combination of cash and shares. Shares granted are valued at 80 % of the relevant market price as they are blocked for a period of three years. Access to these shares is only available in the fourth and later years.

None of the members of the Board of Directors gave up his function in the year under review.

The acting members of the Management Committee and those who gave up their functions in the year under review received – for their contributions and time served in 2003 – total compensation of CHF 4.578 million, which was paid in cash and cash equivalents.

In 2003, there were 14 members on the Management Committee. Five of these relinquished their functions in the year under review. The average number of Management Committee members during the year was 11.3 FTE (full-time equivalents).

The members of the Board of Directors and the Management Committee did not receive any credits or benefits in kind.

No severance payment was made to members of the Management Committee who gave up their functions in 2003.

Conflict of interest – No member of the Board of Directors benefits materially from any contract between a Lonza company and a third party.

No compensation was paid to former members of governing bodies.

In 2003, the members of the Board of Directors received shares as part of their total remuneration. There were no further share allotments except as stated in section 5.2 of this report.

Method of determining compensation and the shareholding programs
5.1

Compensation for acting members
5.2

Compensation for former members of governing bodies
5.3

Share allotment
5.4

Compensation, shareholdings and loans

Share ownership 5.5

Based on information available to Lonza Group Ltd, the members of the Board of Directors and parties closely associated with them¹ held 36 500 and the members of the Management Committee and parties closely associated with them¹ held 3 122 registered shares in Lonza Group Ltd at 31 December 2003.

Options 5.6

Under the various option schemes, the following options were granted to the members of the Board of Directors and the members of the Management Committee:

	Issue 2000	Issue 2001	Issue 2002	Issue 2003	Total issued
Board of Directors ²	0	1 142 850	1 614 872	0	2 757 722
Management Committee ²	338 750	207 850	522 500	302 370	1 371 470

The options vest after three years from grant date and become exercisable thereafter for a period of two years. After the exercise period, the options lapse.

Details on the development of the Lonza Option Plan are published on pages 73 and 74 of this report.

Additional remuneration 5.7

During the year under review, none of the members of the Board of Directors or the Management Committee or parties closely linked to such persons has billed honoraria or other remunerations to Lonza Group Ltd or any subsidiaries for additional services performed.

Loans granted by governing bodies 5.8

No loans were granted, nor are there any loans outstanding from previous years.

Highest total compensation 5.9

The highest compensation conferred on a member of the Board of Directors in 2003 was CHF 525 000, all in form of Lonza shares (number of shares: 9 326; see section 5.2).

¹Spouse, children below age 18, any legal entities that they own or otherwise control, or any legal natural person who is acting as their fiduciary

²Acting members

The shareholders' participation rights are described in the Company's Articles of Association.

Only persons with valid entries in the share register are recognized as shareholders or usufructuaries. A shareholder may only be represented at the Shareholders' Meeting by a legal representative or – by way of written proxy – by another shareholder entitled to vote, the appointed representative of the corporate body, the independent proxy or an assignee of proxy votes for deposited shares. Each share has the right to one vote.

The shares held by Lonza Group Ltd are not entitled to vote at the Shareholders' Meeting and bear no dividend.

Except as otherwise stipulated by law, an absolute majority of the votes represented at the Shareholders' Meeting is required for resolutions and elections.

Ordinary Shareholders' Meetings are called in accordance with the law and the Company's Articles of Association. Extraordinary Shareholders' Meetings must be called upon resolution of a Shareholders' Meeting or if demanded by one or more shareholders representing at least 10 % of the share capital.

One or more shareholders representing together shares with a par value of CHF 1 million may request an item to be included in the agenda. The request to include an item must be submitted in writing at least forty days before the meeting, stating the item to be included and the motions.

Purchasers of Lonza Group Ltd shares may submit a request to be entered, without limitation, as shareholders with voting rights in the share register, provided they expressly declare that they have acquired these shares in their own name and on their own account. Special rules exist for persons who do not expressly declare in the entry application that they hold the shares on their own account (nominees).

There are no special statutory rules concerning a deadline for entry in the share register. The share register is regularly closed three working days before the Annual Shareholders' Meeting.

Voting-rights restrictions
and representation
6.1

Statutory quorums
6.2

Convocation of the Annual
General Meeting
6.3

Agenda
6.4

Entry in the share register
6.5

7. Changes of control and defense measures

An offer to acquire all shares must be made in accordance with Art. 32 SESTA if the threshold of 33 $\frac{1}{3}$ of the voting rights is exceeded. No special opting-out or opting-up dispositions are contained in the Company's Articles of Association.

Clauses on changes of control are not part of any employment agreements or benefit plans.

Duty to make an offer
7.1

Clauses on changes of control
7.2

8. Auditors

Duration of the mandate and term of office of the head auditor
8.1

Since 1999, KPMG Fides Peat, Badenerstrasse 172, CH-8026 Zurich 4, Switzerland, has held the mandate as the independent statutory auditors of Lonza Group Ltd and the Group. The auditing company is elected for a term of one year. Thomas Schmid from KPMG Fides Peat has been the auditor in charge since 1 January 2003.

Head of Internal Auditing of Lonza: Ed O'Donnell (until June 2003), Brian Hamel (since July 2003)

Auditing honorarium
8.2

Lonza Group paid KPMG CHF 1.459 million (2002: CHF 1.338 million) for professional services rendered in connection with the audit of the Group's annual financial statements and other audit-related activities.

Additional honorarium
8.3

KPMG received a total fee of CHF 81 000 (2002: CHF 190 000) for other services rendered to Lonza.

Supervisory and control instruments vis-à-vis the auditors
8.4

The Audit Committee of the Board of Directors is responsible for evaluating the external auditors on behalf of the Board of Directors. In the reporting year, there was one joint meeting with the representatives of the external auditors.

The Audit Committee reviews Lonza's financial reporting process on behalf of the Board of Directors. Management is responsible for the financial statements and the reporting process, including the system of internal controls. The independent statutory auditor, KPMG Fides Peat, is responsible for expressing an opinion on the accounting records and the financial statements prepared in accordance with Swiss law and the Company's Articles of Association. As independent group auditors, KPMG Fides Peat, is responsible for expressing an opinion on the consolidated financial statements (balance sheet, income statement, cash flow statement, statement of changes in equity and notes) prepared in accordance with the International Financial Reporting Standards (IFRS), issued by the International Accounting Standards Board (IASB), and Swiss law. The Audit Committee is responsible for overseeing the conduct of these activities by Lonza management and the independent auditors.

Lonza pursues a proactive, integrated and professional communication policy¹. Lonza Group Ltd publishes price-sensitive information in accordance with the obligation to disclose price-sensitive facts as required by the SWX Swiss Exchange.

Corporate Communications and Investor Relations report directly to the CEO. On basic matters of general corporate policy, Corporate Communications receives its guidelines from the Management Committee.

Lonza Group Ltd provides all shareholders entered in the share register with an annual and semi-annual report. The company's website www.lonza.com is regularly updated and provides relevant information such as share price development, news releases and presentations.

Press conferences and analyst meetings take place at the Company's headquarters or by conference call.

Anticipated key reporting dates

Ordinary Shareholders' Meeting for the financial year 2003

31 March 2004, 2.30 pm

Convention Center Basel

Half Year Results 2004

21 July 2004

Full Year Report 2004

26 January 2005

Ordinary Shareholders' Meeting for the financial year 2004

23 March 2005

Dividend transfer to banks

As a rule, Lonza Group pays the dividend to its shareholders on the fourth business day following the Ordinary Shareholders' Meeting.

¹ www.lonza.com/group/en/company/corporate/policies.html

Publications

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Consolidated balance sheet

	million CHF	Note ²	2002	2003
Assets¹				
Fixed assets				
Property, plant and equipment	4	3 695		4 110
Accumulated depreciation	4	(1 945)	1 750	(2 205)
Intangible assets	4		21	17
Goodwill	4		60	53
Other non-current assets	4		39	8
Deferred tax assets	4,23		164	166
Investments	4		20	22
Long-term loans and advances	4		5	3
Total fixed assets			2 059	2 174
Current assets				
Inventories	6	547		516
Value adjustments	6	(31)	516	(35)
Trade receivables, net	7	527		447
Other receivables, prepaid expenses and accrued income	8	92		125
Short-term advances and other financial assets	12	23	642	40
Cash and cash equivalents	9,12		55	45
Total current assets			1 213	1 138
Total assets			3 272	3 312

¹ At 31 December

² See the accompanying notes to the consolidated financial statements

million CHF	Note ²	2002		2003	
Total shareholders' equity	see page 54	1 235	I	1 235	I Liabilities and shareholders' equity¹
Minority interests		0	I	0	I
Liabilities					
Long-term tax provisions	11, 23	429		438	
Long-term other provisions	11	140		139	
Long-term debt	12	317		687	
Total long-term liabilities and provisions		886		1 264	
Other liabilities and deferred items	13	185		196	
Current tax payables		82		33	
Trade payables	14	249		205	
Short-term debt:					
Due to bank and other financial institutions	12	635		379	
Total current liabilities and deferred items		1 151		813	
Total liabilities		2 037		2 077	
Total liabilities and shareholders' equity		3 272	I	3 312	I

¹ At 31 December

² See the accompanying notes to the consolidated financial statements

Consolidated income statement

million CHF	Note ¹	2002	2003
Net sales (see segment information)	pages 79–81	2 536	2 242
Cost of goods sold		(1 816)	(1 680)
Gross profit		720	562
Marketing and distribution		(86)	(76)
Research and development	24	(81)	(69)
Administration and general overheads	19	(148)	(124)
Other operating income/(expenses)		14	9
Operating income		419	302
Non-recurring items:			
Assets taken out of production/depreciation	20	(72)	(100)
Restructuring and other provisions	20	(112)	(58)
Amortization of goodwill		(5)	(5)
EBIT – earnings before interest and taxes		302	139
Other financial income and expenses	21,22	(19)	(24)
Income before income taxes		283	115
Income taxes	23	(62)	(24)
Net income before minorities		221	91
(Gain)/loss attributable to minorities		0	0
Net income (loss)		221	91
		CHF	CHF
Basic earnings per share before non-recurring items	28	6.12 ²	4.18 ³
Basic earnings per share	28	4.55	1.92
Diluted earnings per share before non-recurring items ⁴	28	5.96 ²	4.12 ³
Diluted earnings per share ⁴	28	4.46	2.00

¹ See the accompanying notes to the consolidated financial statements

² Excluding net loss after tax from non-recurring items of CHF (76) million

³ Excluding net loss after tax from non-recurring items of CHF (107) million

⁴ Diluted earnings per share for 2002 have been restated by the weighted average number of shares taking the shares for the employee benefit programs into account.

million CHF	2002	2003
Net income/(loss)	221	91
Adjustments for non-cash items:		
Minority interests	0	0
Income taxes	62	24
Other financial (income) and expenses	19	24
Depreciation of property, plant and equipment	146	147
Amortization of intangibles	10	7
Amortization of goodwill	5	5
(Decrease)/increase of provisions	(15)	44
(Gain)/loss on disposal of assets	52	29
Income taxes paid	(81)	(75)
Interest paid	(51)	(32)
Cash flow before change in working capital	368	264
(Increase)/decrease inventories	48	35
(Increase)/decrease trade receivables	(9)	78
Increase/(decrease) trade payables	42	(50)
(Increase)/decrease other net working capital	(43)	(17)
Increase/(decrease) of other payables net	(92)	(19)
Net cash (used for) provided by operating activities	314	291
Purchase of property, plant and equipment	(348)	(420)
Purchase of intangible assets	(2)	(4)
Proceeds from sale of tangible and intangible assets	48	36
(Purchase)/proceeds from sale of investments	2	(3)
(Acquisition)/divestment of subsidiary (net of cash)	0	0
(Purchase)/proceeds from sale of other assets	(6)	2
(Decrease)/increase in other long-term liabilities	(13)	(11)
Decrease/(increase) in loans and advances	(6)	(15)
Interests received	24	20
Dividends received	16	3
Net cash (used for)/provided by investing activities	(285)	(392)
(Decrease)/increase of capital	(485)	1
(Decrease)/increase in debt	49	181
Changes in minority interests	(2)	0
Dividends paid	(95)	(90)
Net cash (used for) provided by financing activities	(533)	92
Effect of currency translation on cash	(6)	(1)
Net (decrease)/increase in cash and cash equivalents	(510)	(10)
Cash and cash equivalents at 1 January	565	55
Cash and cash equivalents at 31 December	55	45

Consolidated statement of shareholders' equity

million CHF	Share capital	Premium	Retained earnings	Other comprehensive income	Translation differences	Treasury shares	Total equity
At 31 December 2001	55	622	1 190	(131)	129	(279)	1 586
Dividend	0	0	(95)	0	0	0	(95)
Buy-back of own shares	0	0	0	0	0	(538)	(538)
Capital reduction	(5)	(475)	0	0	0	480	0
Net (loss)/gain on hedge of net investments in foreign entities	0	0	0	91	0	0	91
Net (loss)/gain on cash flow hedges	0	0	0	(2)	0	0	(2)
Impact of convertible bond	0	0	0	17	0	0	17
Translation differences	0	0	0	0	(45)	0	(45)
Net income	0	0	221	0	0	0	221
At 31 December 2002	50	147	1 316	(25)	84	(337)	1 235
Dividend	0	0	(90)	0	0	0	(90)
Net (loss)/gain on cash flow hedges	0	0	0	1	0	0	1
Translation differences	0	0	0	0	(2)	0	(2)
Net income	0	0	91	0	0	0	91
At 31 December 2003	50	147	1 317	(24)	82	(337)	1 235

The share capital on 31 December 2003 comprised 50 450 000 registered shares with a par value of CHF 1 each (2002: 50 450 000 registered shares with a par value of CHF 1 each) amounting to CHF 50 450 000 (2002: CHF 50 450 000).

Reserves in the amount of CHF 25 225 000 cannot be distributed.

Basis of preparation – The consolidated financial statements for 2002 and 2003 are reported in Swiss francs (CHF) and are based on the annual accounts of the individual subsidiaries at 31 December which have been drawn up according to uniform Group accounting principles. The consolidated accounts are prepared in accordance with the International Financial Reporting Standards (IFRS) as adopted by the International Accounting Standards Board (IASB). They are prepared on the historical cost basis, except that derivative financial instruments are stated at their fair value.

Restatement – For comparative purposes, certain prior-year amounts have been reclassified to conform with the current-year presentation. The presentation of the consolidated income statement has been changed from a classification based on the nature of expenses to one based on their function. The prior year income statement has been restated accordingly.

Principles of consolidation – The consolidated financial statements represent the accounts for the year ended 31 December of Lonza Group Ltd and its subsidiaries. Subsidiaries acquired during the year are included in the consolidated accounts from the date of acquisition, while any subsidiaries sold are excluded from the accounts from the date of sale. Acquisitions are accounted for by the use of the purchase method of accounting. The full consolidation method is used, whereby the assets, liabilities, income and expenses are incorporated in full. The proportion of the net assets and net income attributable to minority shareholders is shown separately in the consolidated balance sheet and income statement.

Payables, receivables, income and expenses between Lonza consolidated companies are eliminated. Intercompany profits included in year-end inventories or goods produced within Lonza are eliminated. Transactions between subsidiaries are concluded under market conditions. Investments in subsidiaries are reflected in the balance sheet of the parent company using the cost method. Affiliates are valued in the consolidated financial statements using the equity method of accounting. Under this method, the investment is initially recorded at cost, and is increased or decreased by the proportionate share of the subsidiary's or affiliate's profits or losses after the date of acquisition, adjusted for any amortization of goodwill arising from acquisition and depreciation of fair market value increments/decrements recognized at that time. Dividends paid during the year reduce the carrying value of the investments. Investments are stated at cost, less any write-offs that are necessary. The significant subsidiaries and affiliates included in the financial statements are shown on page 62.

Definition of subsidiary and affiliates – Subsidiaries are those enterprises controlled by Lonza Group Ltd. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities.

Affiliates are those enterprises in which the Group has significant influence, but not control, over the financial and operating policies. The consolidated financial statements include the Group's share of the total recognized gains and losses of affiliates on an equity-accounted basis, from the date that significant influence commences until the date that significant influence ceases.

Definition of segments – The segment data are shown by the primary business segments and the secondary geographical segments. The business segments are structured by subsidiaries which operate within the same business activity and are the basis of the internal reporting system. The geographical segments are shown by the major continents.

Revenue recognition – Sales are recognized when the significant risks and rewards of ownership of the assets have been transferred to a third party and are reported net of sales taxes and rebates. Provisions for rebates to customers are recognized in the same period that the related sales are recorded.

Revenue from termination fees is recognized in the income statement in the period in which the termination occurs. The POC (percentage of completion) method is applied for development projects.

Foreign currencies – The consolidated financial statements of Lonza are expressed in Swiss francs (CHF). In the financial statements of the consolidated companies, assets and liabilities are translated at the rate on the balance sheet date. Transactions are recorded using the exchange rate at the time of the transaction. All resulting foreign exchange transaction gains and losses are recognized in the consolidated company's income statement. Income, expenses and cash flows of the foreign consolidated companies have been translated into CHF using the yearly average exchange rates. The balance sheets are translated using the year-end exchange rates. Exchange rate differences arising from the different exchange rates applied in balance sheets and income statements are allocated to reserves.

Straight bond – Interest-bearing borrowings are recognised initially at cost, less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortized cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective-interest basis.

Convertible bond – The convertible bond is separately shown in the balance sheet by the liability component and the equity component. The fair value of the liability component is determined on the basis of the present value of the principal plus the present value of the interest payable over the contractual period using a rate of interest applied by the market at the time. The value of the equity component results by deduction of the liability component from the total proceeds of the bond issue. The difference between the initial liability component and the notional amount is amortized over the contractual period of the bond and treated as a financial expense.

Derivative financial instruments and hedging – Derivative financial instruments are initially recognized in the balance sheet at cost and subsequently remeasured to their fair value. The method of recognizing the resulting gain or loss is dependent on whether the derivative contract is designed to hedge a specific risk and qualifies for hedge accounting. On the date a derivative contract is entered into, the Group designates derivatives which qualify as hedges for accounting purposes as either a hedge of the fair value of a recognized asset or liability (fair value hedge), a hedge of a forecasted transaction or firm commitment (cash flow hedge), or a hedge of a net investment in a foreign entity. Changes in the fair value of derivatives which are fair value hedges are recognized in the income statement, along with any changes in the fair value of the hedged asset or liability that is attributable to the hedged risk. Changes in the fair value of derivatives in cash flow hedges that are highly effective are recognized in equity. Where the forecasted transaction or firm commitment results in the recognition of an asset or liability, the gains and losses previously included in equity are included in the initial measurement of the asset or liability. Otherwise, amounts recorded in equity are transferred to the income statement and classified as revenue or expense in the same period in which the forecasted transaction affects the income statement. Hedges of net investments in foreign entities are accounted for similarly to cash flow hedges. The Group hedges certain net investments in foreign entities with currency forward contracts. All foreign exchange gains or losses arising on translation are recognized in equity and included in cumulative translation differences. Certain derivative instruments, while providing effective economic hedges under the Group's policies, do not qualify for hedge accounting. Changes in the fair value of any derivative instruments that do not qualify for hedge accounting are recognized immediately in the income statement. When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that

time remains in equity and is recognized in the income statement, when the committed or forecasted transaction is ultimately recognized in the income statement. However, if a forecasted or committed transaction is no longer expected to occur, the cumulative gain or loss that was recognized in equity is immediately transferred to the income statement.

The purpose of hedge accounting is to match the impact of the hedged item and the hedging instrument in the income statement. To qualify for hedge accounting, the hedging relationship must meet several strict conditions with respect to documentation, probability of occurrence, hedge effectiveness and reliability of measurement. At the inception of the transaction, the Group documents the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions.

This process includes linking all derivatives designated as hedges to specific assets and liabilities or to specific firm commitments or forecasted transactions. The Group also documents its assessment, both at the hedge inception and on an ongoing basis, as to whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

Fixed assets – Fixed assets (property, plant and equipment) are stated at cost less depreciation. The assets are depreciated over their estimated useful lives, which vary from 10 to 50 years for buildings and structures, and 5 to 18 years for production facilities, machinery, plant, equipment and vehicles. Fixed assets are depreciated using the straight-line method over their estimated useful lives.

Long-term leasing arrangements, which effectively constitute assets purchased with long-term financing, are carried as fixed assets at their purchase price and are written off over their estimated useful lives. The corresponding liabilities are included in long-term and short-term debt.

Subsequent expenditure: Expenditure incurred to replace a component of an item of property, plant and equipment that is accounted for separately, including major inspection and overhaul expenditure, is capitalized. Other subsequent expenditure is capitalized only when it increases the future economic benefits embodied in the item of property, plant and equipment. All other expenditure is recognized in the income statement as an expense as incurred.

Impairment – The carrying amounts of the Group's assets, other than inventories and deferred tax assets, are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement.

Calculation of recoverable amount – The recoverable amount of the Group's receivables is calculated as the present value of expected future cash flows, discounted at the original effective interest rate inherent in the asset. Receivables with a short duration are not discounted. The recoverable amount of other assets is the greater of their net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

Reversal of impairment – An impairment loss in respect of a receivable is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised. An impairment loss in respect of goodwill is not reversed unless the loss was caused by a specific external event of an exceptional nature that is not expected to recur, and the increase in recoverable amount relates clearly to the reversal of the effect of that specific event. In respect of other assets, an impairment loss is reversed if there has been a change in the estimates used to determine

the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Borrowing costs – Borrowing costs are capitalized for all assets that require a construction period to get them ready for the intended use. The interest is only capitalized for those projects with a capital outlay in excess of CHF 50 million and an investment/construction period greater than six months.

Intangible assets – Intangibles include software, licences, patents, trademarks and similar rights granted by third parties. These assets are amortized using the straight-line method over their estimated useful lives. Intangible assets are amortized over their useful lives, but not exceeding five years.

Goodwill – At the time of their initial recognition, the assets and liabilities of consolidated subsidiaries are recorded at their estimated fair value. Goodwill represents the difference between the purchase price and the fair value of the net assets acquired. Goodwill is capitalized and amortized on a straight-line basis over its estimated useful life not exceeding 20 years.

Inventories – Inventories are reported at the lower of cost (purchase price or production cost) or market value (realizable values). The cost of inventories is calculated using the weighted average method. Pro-rated production overheads are included in the valuation of inventories. Adjustments are made for inventories with a lower market value or which are slow moving. Unsaleable inventory is fully written off. Costs include all expenditures related directly to specific projects and an allocation of fixed and variable overheads incurred in the Group's contract activities based on normal operating capacity.

Receivables – Trade receivables as well as other receivables are disclosed at nominal values less expected economic adjustments at fair value.

Cash and cash equivalents – Cash includes cash in hand, in postal and bank accounts, as well as short-term deposits and highly liquid funds payable within 90 days at the latest.

Deferred taxes – Tax expense is calculated using the balance sheet liability method. Additional deferred taxes are provided wherever temporary differences exist between the tax base of an asset or liability and its carrying amount in the consolidated results for the year. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates in the respective jurisdictions in which Lonza operates that are expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. In assessing the recoverability of deferred tax assets, management considers whether it is probable that some portion or all of the deferred tax assets will not be realized. For transactions and other events recognized directly in equity, any related tax effects are also recognized directly in equity.

Retirement benefits – Most of Lonza's subsidiaries operate their own pension plans. Generally, they are funded by employees' and employers' contributions. A policy has been established whereby actuarial valuations are performed on a yearly basis. The cumulative effect from initial application of IAS 19 as of 1 January 1995 is included as a transitional amount and will be recognized as an asset or liability respectively, over a period not exceeding the expected remaining working lives of the participating em-

ployees. In the following years, the actuarial gains and losses are recognized over the same period as above if the accumulated gain and loss exceed the corridor of 10 % of the greater of plan assets and projected benefits obligation. Effective 1 January 1999, Lonza adopted the provisions of IAS 19 revised. This revised standard permits companies to elect to amortize or immediately recognize, any difference between the accumulated pension cost at transition and the funded status if that difference is an additional pension liability consistent with IAS 8, as a change in accounting policy. Lonza elected to immediately recognize the impact of the adoption of IAS 19 revised.

Provisions – A provision is recognized in the balance sheet when the Group has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. A provision for restructuring is recognized when the Group has approved a detailed and formal restructuring plan, and the restructuring has either commenced or has been announced publicly. Future operating costs are not provided for.

In accordance with the Group's published environmental policy and applicable legal requirements, a provision for site restoration in respect of contaminated land is recognized when the land is contaminated.

Option/share plans – Purchase and sale of own shares for the Lonza Share Option Plan (LOSOP) and Employee Share Purchase Plan (ESPP) are reflected in equity. For the Option Plan no personnel costs have been taken into account.

Research and development – Development costs are only capitalized when it is reasonably certain that the related product will be commercially marketed at a profit. Fixed assets (buildings, machinery, plant, equipment) used for research purposes are valued similarly to other fixed assets. Such assets are capitalized and depreciated over their estimated useful lives. Expenses for research and development include associated wages and salaries, material costs, depreciation on fixed assets, as well as overhead costs.

Net financing costs – Net financing costs comprise interest payable on borrowings calculated using the effective interest rate method, dividend income, foreign exchange gains and losses, and gains and losses on hedging instruments that are recognised in the income statement. Interest income (expense) is recognised in the income statement as it accrues, taking into account the effective yield of the asset or liability or an applicable floating rate. Dividend income is recognised in the income statement on the date that the dividend is declared. Interest income and expense includes the amortisation of any discount or premium or other differences between the initial carrying amount of an interest-bearing instrument and its amount at maturity calculated on an effective interest rate basis.

Use of estimates – The preparation of financial statements and related disclosures in conformity with International Financial Reporting Standards requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the period reported. Actual results could differ from those estimates. Estimates are used in accounting for allowances for uncollectible receivables, inventory obsolescence, depreciation, employee benefits, taxes, restructuring provisions and contingencies. Estimates and assumptions are reviewed periodically and the effects of revisions are reflected in the financial statements in the period they are determined to be necessary.

CHF	2002	2003	
The following exchange rates were used to translate the significant currencies used in Lonza:			
Balance sheet year-end rates			
EU	Euro	1.4530	1.5584
USA	Dollar	1.3862	1.2363
Great Britain	Pound sterling	2.2324	2.2035
Income statement year average rates			
EU	Euro	1.4676	1.5207
USA	Dollar	1.5608	1.3442
Great Britain	Pound sterling	2.3361	2.1972
<p>Risk management activities – Lonza is exposed to market risk from changes in currency exchange rates. To manage the volatility relating to these exposures, Lonza enters into various derivative transactions pursuant to Lonza's policies in areas such as counterparty exposure and hedging practices. Counterparties to these agreements are major international financial institutions. Positions are monitored using techniques such as market value and sensitivity analyses. There are no separable embedded derivatives.</p> <p>Interest rate management – Lonza's policy is to manage interest cost using a mix of fixed and variable rate debt. In order to manage this mix in a cost-efficient manner, Lonza enters into interest rate swaps, to exchange, at specified intervals, the difference between fixed and variable interest amounts calculated by reference to a corresponding notional principal amount.</p> <p>Foreign exchange management – In management of its exposure to fluctuation in foreign currency exchange rates, Lonza has entered into a variety of currency swaps, foreign exchange contracts and options. These agreements generally include the exchange of one currency for a second currency at a future date.</p> <p>To hedge currency risk, forward contracts are designated as hedges for net investments and cash flow hedges.</p> <p>The following table shows the contract or underlying principal amounts and fair value of derivative financial instruments by type of contract at 31 December 2003 and 2002. Contract or underlying principal amounts indicate the volume of business outstanding at the balance sheet date and do not represent amounts at risk. The fair values are determined by the mark-to-market valuation.</p>			

Exchange rates

1

Financial instruments

2

million CHF	2002	2003	2002	2003	2002	2003	2002	2003
		Contract or underlying principal amount		Positive fair values		Negative fair values		Total net fair values
Financial instruments								
Currency-related instruments								
Forward foreign exchange rate contracts	75	138	29	1	(5)	(1)	24	0
Currency swaps	608	603	0	19	0	(1)	0	18
Total currency-related instruments	683	741	29	20	(5)	(2)	24	18
Interest-related instruments								
Interest rate swap (straight bond)	0	375	0	3	0	0	0	3
Total financial instruments	683	1 116	29	23	(5)	(2)	24	21

The fair values of derivatives are included in the balance sheet caption "other receivables, prepaid expenses and accrued income".

Financial instruments by currency

Forward foreign exchange rate contracts and currency swaps			
USD		584	513
GBP		31	43
EUR		27	99
CZK		34	73
JPY		6	13
SGD		1	0
Total		683	741
Interest rate swap		0	375
Total financial instruments		683	1 116

	Contract or underlying principal amount		Fair values	
Financial instruments effective for hedge accounting purposes				
Fair value of cash flow hedges	69	0	(2)	0
Total	69	0	(2)	0

Fair value changes of cash flow hedges were recognized in shareholders' equity under other comprehensive income. No financial contracts have a duration of more than 12 months.

Notes to the consolidated financial statements

Changes in the scope of consolidation
3

Principal subsidiaries and affiliates¹ – Two new legal entities were established in 2003 (Lonza Guangzhou Nansha Ltd and Lonza (China) Investments Co. Ltd). Lonza Compounds SpA and Lonza Composites Srl, both in Scanzorosciate (IT), were merged into Lonza SpA. The principal subsidiaries and affiliates are shown below. With regard to divestiture see note 32.

	Registered office ²	Purpose	Currency ²	Share capital in 000	% Holding direct	% Holding indirect
European countries						
Lonza Ltd	Visp, CH	● ● ●	CHF	60 000	100	
Lonza Sales Ltd	Basel, CH	● ● ●	CHF	2 000	100	
Lonza Finance Limited	St Helier, Jersey, GB	● ● ●	CHF	12	100	
Lonza Biotec sro	Kourim, CZ	● ● ●	CZK	137 100		100
Lonza Compounds GmbH & Co. KG	Miehlen, DE	● ● ●	EUR	699		100
LOFO High Tech Film GmbH	Weil am Rhein, DE	● ● ●	EUR	7 671		100
Lonza GmbH	Weil am Rhein, DE	● ● ●	EUR	511		100
Lonza Group GmbH	Weil am Rhein, DE	● ● ●	EUR	25		100
Lonza Biologics plc	Slough, GB	● ● ●	GBP	4 500		100
Lonza Group UK Ltd	Slough, GB	● ● ●	GBP	17 000		100
Lonza SpA	Scanzorosciate, IT	● ● ●	EUR	51 600		100
Lonza Europe BV	Breda, NL	● ● ●	EUR	19		100
Other countries						
Lonza Guangzhou Ltd	Guangzhou, CN	● ● ●	USD	12 000		100
Lonza Guangzhou Nansha Ltd	Guangzhou, CN	● ● ●	USD	2 000	100	
Lonza (China) Investments Co. Ltd	Guangzhou, CN	● ● ●	USD	5 500	100	
Lonza Japan Ltd	Tokyo, JP	● ● ●	JPY	200 000	100	
Lonza Singapore Pte Ltd	Singapore, SG	● ● ●	SGD	45 500		100
Lonza America Inc.	Wilmington, DE, US	● ● ●	USD	8	100	
Lonza Inc.	Fair Lawn, NJ, US	● ● ●	USD	464		100
Lonza Biologics Inc.	Wilmington, DE, US	● ● ●	USD	1		100

● Research/Applications ● Production ● Sales ● Services/Financing

¹ All companies belonging to Lonza Group are non-listed entities

² Abbreviation of countries and currencies in accordance with ISO standards

million CHF	At 31 12 02	Currency translation differences	Change in the scope of consolidation	Additions	Disposals and adjustments	Transfers	At 31 12 03	Fixed assets net at 31 12 03	Insurance value at 31 12 03
At cost									
Land	54	1	0	0	5	0	60	46	
Buildings and structures	793	(7)	0	14	0	33	833	411	829
Production facilities, machinery, plant, equipment and vehicles	2 521	(48)	0	47	(21)	220	2 719	950	3 483
Construction in progress and advances for property, plant and equipment	327	(28)	0	359	0	(160)	498	498	161
Property, plant and equipment	3 695	(82)	0	420	(16)	93	4 110	1 905	4 473
Intangible assets	84	(3)	0	4	(3)	4	86	17	
Goodwill	90	(4)	0	0	0	0	86	53	
Other non-current assets and deferred items, net	203	(13)	0	0	(16)	0	174	174	
Investments	22	(1)	0	3	0	0	24	22	
Long-term loans and advances	5	(1)	0	0	(1)	0	3	3	
Total fixed assets	4 099	(104)	0	427	(36)	97	4 483	2 174	
Accumulated depreciation									
Land	(14)	0	0	0	0	0	(14)		
Buildings and structures	(401)	2	0	(25)	2	0	(422)		
Production facilities, machinery, plant, equipment and vehicles	(1 530)	25	0	(122)	(48)	(94)	(1 769)		
Property, plant and equipment	(1 945)	27	0	(147)	(46)	(94)	(2 205)		
Intangible assets	(63)	3	0	(7)	1	(3)	(69)		
Goodwill	(30)	2	0	(5)	0	0	(33)		
Investments	(2)	0	0	1	(1)	0	(2)		
Long-term loans and advances	0	0	0	0	0	0	0		
Total depreciation	(2 040)	32	0	(158)	(46)	(97)	(2 309)		
Total fixed assets net	2 059	(72)	0	269	(82)	0	2 174		

Commitments for capital expenditure in property, plant and equipment amount to CHF 64 million at year-end 2003 (2002: CHF 79 million).

Fixed assets under finance lease contracts at year-end 2003 amount to CHF 44 million (2002: CHF 32 million).

	million CHF	2002	2003
Leases			
5			
	Finance lease liabilities – minimum lease payments:		
	Not later than 1 year	2	2
	Later than 1 year and not later than 5 years	7	9
	Later than 5 years	10	9
	Total future minimum finance lease payments	19	20
	Present value of finance lease liabilities	(6)	(8)
	Present value of minimum finance lease payments	13	12
	The present value of finance lease liabilities is as follows:		
	Not later than 1 year	1	1
	Later than 1 year and not later than 5 years	4	5
	Later than 5 years	8	6
	Present value of minimum finance lease payments	13	12
	Operating lease liabilities – minimum lease payments:		
	Not later than 1 year	19	13
	Later than 1 year and not later than 5 years	71	47
	Later than 5 years	70	39
	Total future minimum operating lease payments	160	99
	Present value of operating lease liabilities	(17)	(10)
	Present value of minimum operating lease payments	143	89
	The present value of operating lease liabilities is as follows:		
	Not later than 1 year	17	12
	Later than 1 year and not later than 5 years	64	42
	Later than 5 years	62	35
	Present value of minimum operating lease payments	143	89

million CHF	2002		2003		
	%		%		
Raw materials	21	106	19	93	Inventories
Work in progress and finished goods	61	317	61	295	6
Others	18	93	20	93	
Total	100	516	100	481	
By division					
Exclusive Synthesis & Biotechnology	49	251	41	197	
Organic Fine & Performance Chemicals	28	143	32	153	
Polymer Intermediates	23	122	27	131	
Total	100	516	100	481	

The reported inventories are net of a total value adjustment amount of CHF 35 million (2002: CHF 31 million).

Receivables from customers	513	428	Trade receivables
Accounts receivable from unconsolidated affiliates	20	25	7
Value adjustments	(6)	(6)	
Total	527	447	

The credit risk is diversified due to the large number of entities comprising the Lonza customer base and the dispersion across many different industries and regions.

Other receivables	13	71	Other receivables, prepaid expenses and accrued income
Prepaid taxes and social security payments	18	17	8
Prepaid expenses and accrued income	25	37	
Accrued interest income	36	0	
Total	92	125	
Cash	55	45	Cash and cash equivalents
Time deposits	0	0	9
Total	55	45	

The assets pledged for security of own liabilities amount to CHF 1 million (2002: CHF 1 million).

Pledges and assets under reservation of ownership
10

Notes to the consolidated financial statements

Long-term provisions
11

million CHF	At 31.12.2002	Currency translation differences	Change in the scope of consolidation	Increase	Using	Reduction	At 31.12.2003
Deferred taxes	429	(1)	0	98	(47)	(41)	438
Retirement benefits	103	(4)	0	35	(18)	(31)	85
Others	37	0	0	26	(6)	(3)	54
Total	569	(5)	0	159	(71)	(75)	577

The provisions for retirement benefits primarily comprise the pension liability of Lonza's defined benefit pension plans as disclosed in note 25. Included in the above amounts are provisions for healthcare relating to Lonza's US subsidiaries.

Net debt
12

The net debt is composed of:

	2002		2003	
Long-term debt				
Bonds		0		375
Convertible		285		289
Due to banks and others:				
Banks	15		7	
Others	6	21	6	13
Leasing		11		10
Total		317		687
Breakdown by maturity (long-term debt excluding leasing)				
2004		13		0
2005		0		7
2006		285		664
2007		0		0
2008		0		0
Thereafter		8		6
Total long-term debt excluding leasing		306		677
Fair value comparison (long-term debt excluding leasing)				
		2002		2003
	Balance sheet	Fair value	Balance sheet	Fair value
Bond	0	0	375	379
Convertible bonds	285	283	289	291
Others	21	21	13	13
Total	306	304	677	683

Convertible bond – Amount: CHF 300 million, due 28 June 2006. Interest: 2 % p.a. payable on 28 June, for the first time on 28 June 2003. Conversion right: On or after 1 July 2002 up to and including 21 June 2006, each bond of CHF 5 000 principal amount is convertible into initially 37.03704 shares with a par value of CHF 1 (section 6 of the terms of the bond). Risk: The usual risk with the convertible bond is the risk that the conversion will not be executed at the end of the conversion period.

The fair values of the liability component and the equity conversion component were determined on the issue of the bond. The fair value of the liability component, included in long-term debt, was calculated using a market interest rate for an equivalent non convertible bond. The residual amount, representing the value of the equity conversion component, is included in shareholders' equity.

The convertible bond is recognized in the balance sheet as follows:

million CHF

Face value of convertible bond issued on 28 June 2002	300
Equity conversion component	17
Liability component on initial recognition	283
Interest expenses (2 % p.a.)	6
Amortisation of liability component	4

Straight bond – Amount: CHF 375 million, due 14 February 2006. Interest: 2 % p.a. payable on 14 February, for the first time on 14 February 2004. Subject to an interest rate swap that creates a liability at floating rates.

	2002 I	2003 I
Short-term debt		
Due to banks and other financial institutions	537	250
Others	98	129
Long-term debt due within one year	0	0
Total	635	379
Total debt	952	1 066
Loans and advances		
Long-term loans and advances	(5)	(3)
Short-term advances	(23)	(40)
Cash and cash equivalents	(55)	(45)
Total	(83)	(88)
Net debt	869	978

Loans and advances to affiliates amount to CHF 5 million (2002: CHF 5 million), whereas no debt is owed to them.

million CHF		2002		2003	
	Average interest rates		Average interest rates		
	%	%	%	%	
Breakdown of debt by currencies					
Swiss franc	2.13	81	773	1.60	79 839
Pound sterling	4.60	1	10	4.75	0 0
Euro	3.45	2	14	2.95	2 25
US dollar	1.73	15	146	1.73	17 186
Others	10.78	1	9	4.00	2 16
Total		100	952		100 1 066
Other liabilities and deferred items 13	Accrued liabilities and deferred items		123		136
	Capital tax payables		4		2
	Other interest-free liabilities		53		48
	Accrued interest payables		5		10
	Total		185		196
Trade payables 14	Payable to third parties		240		195
	Payable to affiliates		9		10
	Total		249		205
Contingent liabilities 15	Various lawsuits and claims arising from the ordinary business of Lonza are pending against companies of Lonza Group Ltd. In the opinion of management, and based on currently available information, the handling and settlement of these lawsuits and claims will have no adverse material effect upon the consolidated financial position or operations of Lonza. In the last two years, most of the numerous (individual and class) actions filed by purchasers and consumers of vitamins in the aftermath of the 1998 vitamin antitrust investigations in the USA (and elsewhere) against Lonza companies have been settled. With regard to the outcome of the few proceedings still pending, no firm predictions can be made at present. Management is monitoring the progress of these proceedings to assess any potential exposure and is making appropriate provisions on the basis of its assessment.				
Material and energy costs 16	Material costs		959		927
	Energy costs		102		104
	Total		1 061		1 031
Personnel expenses 17	Wages and salaries		484		445
	Pensions		45		49
	Other social security contributions		82		62
	Other personnel expenses		16		11
	Total personnel cost		627		567

million CHF	2002	2003	
Property, plant and equipment	146	147	Depreciation and amortization
Intangible assets	10	7	18
Total	156	154	
Amortization of goodwill	5	5	
<p>The line item "other operating income/(expenses)" of the consolidated income statement include in 2003 "other income" of CHF 49 million (2002: CHF 20 million) and "other expenses" of CHF 40 million (2002: CHF 6 million).</p>			Other operating income/(expenses) 19
<p>The consolidated income statement is charged with impairment costs for assets taken out of production of CHF 100 million (2002: CHF 72 million) and restructuring costs of CHF 58 million (2002: CHF 40 million). Due to overcapacity and the persistence of difficult market conditions, Lonza has decided to decommission fine chemicals production assets in both the USA and Europe.</p>			Impairment and restructuring 20
Interest income	25	20	Interest and other financial income
Other financial income	0	1	21a
Total	25	21	
Interest expenses	(51)	(37)	Interest and other financial
Other financial expenses	(6)	(9)	expenses
Total	(57)	(46)	21b
<p>Other financial expenses are primarily composed of financing costs for the convertible bond.</p>			
Dividend earned	11	0	Income from investments
Income from application of the equity method	2	1	22
Total	13	1	
Major components of tax expenses			Income taxes
Current taxes	(68)	(18)	23
Deferred tax expense relating to the origination and reversal of temporary differences	25	(5)	
Deferred tax expense/(income) resulting from tax rate changes	(19)	(1)	
Total	(62)	(24)	

Lonza Group Ltd and the operating company Lonza Ltd are domiciled in Switzerland. The maximum rate of all income taxes on companies domiciled in Switzerland is 8 % for holding companies and 25 % for operating companies (2002: same rates).

Since the Group operates across the world, it is subject to income taxes in many different tax jurisdictions. Lonza calculates the average tax rates as a weighted average of the rates applying in the tax jurisdictions in which it operates. The average tax rate for 2003 is 21 %.

million CHF	2002	2003
Reconciliation of tax expenses		
Tax at the domestic rates applicable to the profits earned in the country concerned	37	25
Tax effect of expenses that are not deductible for tax purposes	15	2
Tax-exempt capital gain	0	1
Tax credits and other incentives earned	(2)	(2)
Tax benefits from previously unrecognized tax losses	0	(4)
Deferred tax benefit from tax rate changes	(19)	(1)
Others	31	3
Total	62	24
Deferred tax expenses charged/(credited) directly to equity	(3)	(2)

Capital taxes of CHF 6 million (2002: CHF 8 million) are contained in other operating expenses. The deferred tax benefit from tax rate changes is the result of decreased income tax rates applicable in Germany.

	Assets	Liabilities	Assets	Liabilities
Components of deferred income tax balances				
Short-term operating provisions	57	101	54	79
Long-term operating provisions	49	125	31	122
Property, plant and equipment	0	201	45	237
Pension benefits	0	2	0	0
Tax loss carry-forwards	89	0	76	0
Subtotal	195	429	206	438
Valuation allowance	(31)	0	(40)	0
Deferred income taxes	164	429	166	438

These amounts are included in the following captions in the balance sheet:

Deferred tax assets	164	166
Long-term tax provisions	(429)	(438)
Net deferred tax liability	(265)	(272)

Research and development costs include all primary costs directly related to this function as well as internal services and imputed depreciations. These costs are incurred for:

- development of new products and services
- improvement of existing products and services
- development of new production processes
- improvement of existing production processes
- costs for patents
- purchase price for product and process know-how as far as it has not been capitalized

These costs amounted to CHF 82 million (2002: CHF 102 million) and represent the full R & D activity. In contrast to the consolidated income statement, research and development costs of CHF 69 million (2002: CHF 81 million) are incurred, representing the unabsorbed R & D overhead.

million CHF 2002 | 2003

Lonza sponsors defined benefit pension plans according to the regulations of the countries in which it operates. There are no significant defined contribution plans. The benefits are primarily based on years of service and the employees' compensation during the last years of employment.

During 2003, actuarial valuations were performed for all significant defined benefit plans using the Projected Unit Credit Valuation Method. The principal assumptions, expressed as a weighted average for Lonza, are the result of the underlying national economic conditions of the respective countries. In 2003, the pension benefits in Italy and the UK are disclosed for the first time. For comparison purposes, the 2002 results are modified to reflect this change.

Pension benefits
25

	%	%
Discount rate	4.4	4.3
Expected long-term rate of return on plan assets	5.9	5.7
Future salary increases	2.2	2.2
Future pension increases	0.5	0.5

The funded status of the defined benefit pension plans is as follows:

Present value of unfunded obligations	43	45
Present value of funded obligations	1318	1417
Plan assets at fair value	(1 146)	(1 232)
Funded status	215	230
Unrecognized transition amount	1	1
Unrecognised actuarial gains/(losses)	(176)	(214)
Unrecognised prior service costs	(2)	(1)
Limitation on recognition of surplus due to uncertainty of obtaining future benefits	0	9
Net liability recognized in the balance sheet	38	25

Pension assets of CHF 20 million (2002: CHF 17 million) and liabilities of CHF 45 million (2002: CHF 55 million) are included in the financial statements as financial receivables and liabilities respectively. Pension plan surpluses are only accounted for in the consolidated balance sheet if a future economic benefit for the Group is expected. In Switzerland, the pension fund was changed from a defined benefit pension plan to a defined contribution plan as of 1 January 2004. This change is already reflected in the 2003 calculation.

The plan assets include Lonza Group Ltd shares with a fair value of CHF 0.1 million.

Movement in the net liability recognized in the balance sheet:

Net liability at 1 January	66	38
Impact of exchange rate changes	(6)	1
Extraordinary adjustment	0	(12)
Contributions paid	(35)	(35)
Expense recognized in the income statement	23	25
Curtailment impact	(10)	(1)
Limitation on recognition of surplus due to uncertainty of obtaining future benefits	0	9
Net liability at 31 December	38	25

million CHF	2002	2003
The net periodic pension costs for Lonza's significant benefit plans consist of the following:		
Current service cost	27	28
Interest cost	66	59
Expected return on plan assets	(71)	(66)
Actuarial gains and (losses) recognized	1	4
Past service cost	0	0
Amortization of transition obligation	0	0
Total pension costs	23	25
Pension costs are recognized in personnel expenses (see note 17).		
Actual return on plan assets:		
Expected return on plan assets	71	66
Actuarial gain/(loss) on plan assets	(83)	62
Actual return on plan assets	(12)	128
Other post-retirement benefits – Lonza's post-employment benefits other than pensions are not funded. They mainly consist of post-retirement healthcare benefits in the United States which are provided under a defined benefit plan.		
The principal assumptions are as follows:		
	%	%
Discount rate	6.75	6.25
Medical-cost trend rate	6.00	8.00
The funded status of the post-retirement benefit plans is as follows:		
Present value of unfunded benefit obligations	48	49
Unrecognized transition amount	0	0
Unrecognized actuarial gains/(losses)	(7)	(7)
Unrecognized prior service costs	2	1
Liability recognized in the balance sheet	43	43
Movement in the liability recognized in the balance sheet:		
Liability as of 1 January	50	43
Impact of exchange rate changes	(9)	(1)
Expenses recognized in income statement	4	4
Benefits paid	(2)	(3)
Liability as of 31 December	43	43

million CHF	2002	2003
Net periodic costs for the post-retirement benefit plans are the following:		
Service cost	1	1
Interest cost	3	3
Actuarial (gains) and losses recognized	0	0
Past service cost	0	0
Amortization of transition obligation	0	0
Total post-retirement costs	4	4

These expenses are recognized in personnel expenses (see note 17)

Options (LOSOP) – In 2000, the Board of Directors of Lonza Group Ltd implemented a Share Option Plan entitling holders of options to purchase a fixed number of Lonza shares. The exercise of these options is subject to a holding period. Under the various option schemes (Board of Directors, Management Committee and key employees) the following options were granted:

Employee benefits
26

Year	Number of options	Strike price	Exercise ratio	Vesting/Expiry date
2000	2 175 500	CHF 97.00	10:1	03.05.03/03.05.05
2001	2 220 650	CHF 104.50	10:1	02.04.04/03.04.06
2002	4 353 718	CHF 113.00	10:1	08.04.05/06.04.07
2003	1 204 700	CHF 77.00	10:1	19.03.06/19.03.08

The options vest after three years from the grant date and become exercisable thereafter for a period of two years. After the exercise period, the options lapse.

Participants

	Issue 2000	Issue 2001	Issue 2002	Issue 2003
Board of Directors ¹	0	1 237 800	2 588 718	0
Management Committee ¹	881 600	207 850	562 500	315 940
Key employees	1 293 900	775 000	1 202 500	888 760
Total options granted	2 175 500	2 220 650	4 353 718	1 204 700

Development option plans

	Issued	Cancelled	Exercisable	Exercised	Total open
LOSOP 2000	2 175 500	281 600	1 893 900	0	1 893 900
LOSOP 2001	2 220 650	60 000	2 160 650	0	2 160 650
LOSOP 2002	4 353 718	203 910	4 149 808	0	4 149 808
LOSOP 2003	1 204 700	0	1 204 700	0	1 204 700
Total options	9 954 568	545 510	9 409 058	0	9 409 058

833 709 treasury shares with a par value of CHF 1 each (31 December 2002: 841 327 shares) are reserved for the option plans.

¹ Acting and former members

Fair value at the vesting date	CHF	Vesting date
LOSOP 2000	2 701 101	03.05.03
LOSOP 2001	2 627 917	02.04.04
LOSOP 2002	3 294 023	08.04.05
LOSOP 2003	1 028 332	19.03.06

Employee Share Purchase Plan (ESPP) – In keeping with our vision and culture, Lonza introduced an ESPP for the first time in 2002. This plan is intended to give our employees the opportunity to become co-owners of Lonza. This opportunity is open to full-time and part-time employees. Under the present plan rules, these employees have the opportunity – but no obligation – to acquire shares in Lonza against payment of the full purchase price, in amounts ranging from CHF 1 500 to CHF 15 000. After a holding period of three years, Lonza will provide these employees with one additional share for every three shares purchased. The ESPP is not part of an incentive program. The plan is intended as a long-term share-savings scheme to provide employees with an incentive to strengthen teamwork and personal commitment.

Development share purchase plan

	Purchased	Ratio	Allocated	Exercised	Total open	Expiry date
ESPP 2002	35 010	3:1	11 670	567	11 103	25.10.05
ESPP 2003	12 954	3:1	4 318	0	4 318	19.12.06
Total shares			15 988	567	15 421	

15 421 treasury shares with a par value of CHF 1 each (31 December 2002: 12 375 shares) are reserved for the share purchase plans.

In order to satisfy the exercise of the Employee Share Purchase Plan 2003, Lonza has acquired 3 723 registered shares with a par value of CHF 1 each during 2003, at an average market value of CHF 63 (2002: 12 375 shares at an average market value of CHF 86).

Fair value at the expiry date	CHF
ESPP 2002	912 126
ESPP 2003	261 583

number of shares	31 Dec 2001 ¹	Change in Year	31 Dec 2002	Change in Year	31 Dec 2003	
Total number of shares	55 260 070	 (4 810 070)	 50 450 000	 0	 50 450 000	
Treasury shares						
Shares reserved for convertible bonds	0	2 222 222	2 222 222	0	2 222 222	
Shares reserved for share option plan (LOSOP)	700 000	141 327	841 327	(7 618)	833 709	
Shares reserved for share purchase plan (ESPP)	0	12 375	12 375	3 046	15 421	
Share buy-back program ²	2 374 960	(2 374 960)	0	0	0	
Total treasury shares	3 074 960	 964	 3 075 924	 (4 572)	 3 071 352	
Total shares ranking for dividend at 31 December	52 185 110	 (4 811 034)	 47 374 076	 4 572	 47 378 648	
Share buy-back program in February 2002 Transferred shares ESPP, March 2003	(2 435 110)		116			
Total shares ranking for dividend at date of dividend payment	49 750 000		47 374 192		n.a.	
Share capital movements						
Share capital	CHF	55 260 070	(4 810 070) ²	50 450 000	0	50 450 000

Changes in share and
share capital movements
27

¹ The number of shares has been restated to reflect the share split 1:10 approved by the Shareholders' Meeting on 27 March 2002.

² The amount of CHF 4 810 070 is a capital reduction approved by the Shareholders' Meeting and is based on the share buy-back of 2 374 960 shares in 2001 and 2 435 110 shares in 2002.

Notes to the consolidated financial statements

		2002	2003
million CHF			
Earnings per share 28	Basic earnings per share		
	Net income	221	91
	Non-recurring items	112	158
	Tax effect on non-recurring items	(36)	(51)
	Net income before non-recurring items	297	198
	Weighted average number of shares	48 558 988	47 374 733
	Basic earnings per share	CHF 4.55	1.92
	Basic earnings per share before non-recurring items	CHF 6.12	4.18
	Diluted earnings per share		
	Net income	221	91
	Net income before non-recurring items	297	198
	Elimination of interest expenses on convertible bond	3	6
	Reversing other convertible cost items	3	6
	minus tax effect on dilution costs	(1)	(2)
	Diluted net income	226	101
	Diluted net income before non-recurring items	302	208
	Weighted average number of shares	48 558 988	47 374 733
	Adjustment for assumed conversion of convertible debt	1 296 296	2 222 222
	Adjustments for share options	797 642	853 045
	Weighted average number of shares for diluted earnings per share	50 652 926	50 450 000
	Diluted earnings per share	CHF 4.46	2.00
	Diluted earnings per share before non-recurring items	CHF 5.96	4.12

million CHF	2002	2003
The following is a summary of the free cash flow using Lonza's definition. It includes earnings before interest, taxes and depreciation (EBITDA) and subtracts increase of operating net working capital and capital expenditures less disposal of fixed assets. It can be derived from the cash flow statement as follows:		
Net income/(loss)	221	91
Adjustments for:		
Income taxes	62	24
Other (financial income) and expenses	19	24
EBIT	302	139
Amortization of goodwill	5	5
Operating income (after non-recurring items)	307	144
Depreciation of property, plant and equipment	146	147
Amortization of intangible assets	10	7
(Gain)/loss on disposal of assets	52	29
(Increase)/decrease inventories	48	35
(Increase)/decrease trade receivables	(9)	78
Increase/(decrease) trade payables	42	(50)
(Increase)/decrease other net working capital	(43)	(17)
Change of operating net working capital	38	46
Purchase of property, plant and equipment	(348)	(420)
Purchase of intangible assets	(2)	(4)
Proceeds from sale of tangible and intangible assets	48	36
(Purchase)/proceeds from sale of other assets	(6)	2
(Decrease)/increase in other long-term liabilities	(13)	(11)
Operating investment net	(321)	(397)
Free cash flow	232	(24)

Free cash flow
29

On 8 January 2004, Harris Associates L.P., Chicago (USA), made it known that it held 2 525 950 Lonza Group Ltd shares, or 5.01 % of the voting rights.

Events after balance sheet date
30

On 12 January 2004, Zurich Cantonal Bank, Zurich, made it known that it held 5.3 % of the voting rights (0.2 % in the form of nominal shares and 5.1 % in the form of options).

In 2003, payments to acting members of the Board of Directors of Lonza Group Ltd totaled CHF 1.837 million, 77.2 % of which was received in the form of shares. The compensation system for Board members allows them to choose either a payment in shares or a combination of cash and shares. Shares are granted at 80 % of the relevant market price as they are blocked for a period of three years.

Board of Directors
31

The Group had intended to divest the Polymer Intermediates activities by end of 2005. Given the dilutive effect of cash and earnings of this divestiture and the efforts required during the rebasing of our business, the Board has decided not to divest the Polymer Intermediates business. These activities are now fully integrated in the continuing operations.

Divestiture
32

Statement of value added

million CHF		Note ¹	2002	2003	
			%	%	
Origin of value added	Income from production		2 565	2 315	
	Other income from investments	22	11	0	
	Total income		2 576	2 315	
			100.0	100.0	
	Services bought from third parties :				
	Material costs	16	(959)	(927)	
	Energy costs	16	(102)	(104)	
	Other operating expenses excl. capital taxes		(294)	(255)	
	Gross value added		1 221	1 029	
	Depreciation on property, plant and equipment as well as amortization on intangibles and goodwill	18	(161)	(159)	
Income from application of the equity method	22	2	1		
Total net value added		1 062	871		
Non-recurring items		(112)	(158)		
Total net value added Group		950	713		
			41.2	37.6	
			(4.3)	(6.8)	
			36.9	30.8	
Distribution of value added	To staff:				
	Wages and salaries	17	484	445	
	Pensions	17	45	49	
	Other social security contributions	17	82	62	
	Other personnel expenses	17	16	11	
	Total personnel cost		627	567	
				66.0	79.6
	To public authorities:				
	Income and capital taxes	23	70	30	
	To lenders:				
	Interest on net debt	21	32	25	
	To shareholders:				
	Dividends paid	pages 53, 54	95	90	
	To the company:				
	Net income including minorities		221	91	
(Dividends paid)	pages 53, 54	(95)	(90)		
Total		950	713		
			100.0	100.0	
Distribution of value added per employee			CHF	CHF	
	Wages and salaries		77 901	74 947	
	Pensions		7 243	8 253	
	Other social security contributions		13 198	10 442	
	Other personnel expenses		2 575	1 853	
Total per employee		100 917	95 495		

¹ See the accompanying notes to the consolidated financial statements

million CHF							
Primary reporting format – business segments before non-recurring items							
Year ended		Exclusive Synthesis & Biotechnology	Organic Fine & Performance Chemicals	Polymer Intermediates	Others	Consolidation	Total
31 December 2003							
Net sales		871	932	579	33	(173)	2 242
	%	39	42	26	1	(8)	100
Net sales to customers ¹		835	826	578	3	0	2 242
	%	37	37	26	0	0	100
Operating income		147	125	41	(11)	0	302
	%	49	41	14	(4)	0	100
Percentage return on sales	%	17.6	15.1	7.1	na	na	13.5
Assets ²		1 394	844	675	25	(19)	2 919
	%	48	29	23	1	(1)	100
Liabilities ³		(232)	(102)	(105)	(26)	19	(446)
	%	52	23	24	6	(5)	100
Net capital invested ⁴		1 162	742	570	(1)	0	2 473
	%	47	30	23	0	0	100
Return on net capital invested ⁵	%	12.8	16.5	7.2	na	na	12.2
Depreciation and amortization		70	48	35	1	0	154
	%	45	31	23	1	0	100
Research and development		45	28	9	0	0	82
	%	55	34	11	0	0	100
Investments in property, plant and equipment and intangibles ⁶		317	84	23	0	0	424
	%	75	20	5	0	0	100
Headcount		2 331	2 089	1 209	30	0	5 659
	%	41	37	21	1	0	100
Average headcount		2 522	2 141	1 242	34	0	5 938
	%	42	36	21	1	0	100

¹ Intersegment sales for 2003, which were based primarily on prevailing market prices have been eliminated

² Assets consist of property, plant and equipment, intangible assets, inventories and receivables

³ Liabilities comprise trade payables, other operating payables, other long-term liabilities, operating provisions and exclude taxation and interest-bearing debt

⁴ Net capital invested comprises all assets and liabilities committed to the segment operations at historical year-end rates

⁵ Calculated at historical yearly average rates

⁶ Investments calculated at average rates

million CHF							
Primary reporting format – business segments before non-recurring items							
Year ended		Exclusive Synthesis & Biotechnology	Organic Fine & Performance Chemicals	Polymer Intermediates	Others	Consolidation	Total
31 December 2002							
Net sales		1 014	1 051	599	37	(165)	2 536
	%	40	41	24	1	(6)	100
Net sales to customers ¹		978	957	598	3	0	2 536
	%	39	38	23	0	0	100
Operating income		211	166	48	(6)	0	419
	%	50	40	11	(1)	0	100
Percentage return on sales	%	21.6	17.3	8.0	na	na	16.5
Assets ²		1 399	865	673	38	(70)	2 905
	%	48	30	23	1	(2)	100
Liabilities ³		(235)	(106)	(127)	(77)	70	(475)
	%	49	22	27	16	(14)	100
Net capital invested ⁴		1 164	759	546	(39)	0	2 430
	%	48	31	22	(1)	0	100
Return on net capital invested ⁵	%	17.7	21.2	8.4	na	na	16.8
Depreciation and amortization		83	49	24	0	0	156
	%	53	31	16	0	0	100
Research and development		62	31	9	0	0	102
	%	61	30	9	0	0	100
Investments in property, plant and equipment and intangibles ⁶		242	66	42	0	0	350
	%	69	19	12	0	0	100
Headcount		2 712	2 192	1 275	37	0	6 216
	%	44	35	20	1	0	100
Average headcount		2 694	2 192	1 292	35	0	6 213
	%	43	35	21	1	0	100

¹ Intersegment sales for 2002, which were based primarily on prevailing market prices have been eliminated

² Assets consist of property, plant and equipment, intangible assets, inventories and receivables

³ Liabilities comprise trade payables, other operating payables, other long-term liabilities, operating provisions and exclude taxation and interest-bearing debt

⁴ Net capital invested comprises all assets and liabilities committed to the segment operations at historical year-end rates

⁵ Calculated at historical yearly average rates

⁶ Investments calculated at average rates

million CHF

Secondary reporting format – geographical segments

Year ended	Switzerland	EU	Rest of Europe	North America	Other areas	Consolidation	Total
31 December 2003							
Net sales by marketing area	228	980	45	673	316	0	2 242
%	10	44	2	30	14	0	100
Net sales by production area	1 317	906	50	529	114	(674)	2 242
%	59	40	2	24	5	(30)	100
Operating income	196	91	4	4	7	0	302
%	65	30	1	1	3	0	100
Percentage return on sales	21.8	10.3	na	1.1	7.6	na	13.5
Net capital invested	874	612	134	697	157	0	2 474
%	35	25	5	28	7	0	100
Investments in property, plant and equipment and intangibles ¹	134	32	56	194	8	0	424
%	32	8	13	46	1	0	100
Headcount	2 550	1 455	251	1 046	357	0	5 659
%	45	26	4	18	7	0	100
Year ended							
31 December 2002							
Net sales by marketing area	242	1 101	40	846	307	0	2 536
%	10	43	2	33	12	0	100
Net sales by production area	1 469	975	50	690	116	(764)	2 536
%	58	38	2	27	5	(30)	100
Operating income	394	88	10	(68)	(5)	0	419
%	94	21	2	(16)	(1)	0	100
Percentage return on sales	26.8	9.0	20.0	(9.9)	(4.3)	na	16.5
Net capital invested	985	513	88	678	166	0	2 430
%	41	21	4	28	6	0	100
Investments in property, plant and equipment and intangibles ¹	88	70	19	167	6	0	350
%	25	20	5	48	2	0	100
Headcount	2 632	1 655	264	1 322	343	0	6 216
%	42	27	4	21	6	0	100

¹ Investments calculated at average rates

As Group Auditors, we have audited the consolidated financial statements (balance sheet, income statement, cash flow statement, statement of shareholders' equity and notes on pages 49 to 81) of Lonza Group Ltd, Basel, and its subsidiaries for the year ended 31 December 2003.

These consolidated financial statements are the responsibility of the Board of Directors. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We confirm that we meet the legal requirements concerning professional qualification and independence.

Our audit was conducted in accordance with auditing standards promulgated by the Swiss profession and with the International Standards on Auditing (ISA), which require that an audit be planned and performed to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement. We have examined on a test basis evidence supporting the amounts and disclosures in the consolidated financial statements. We have also assessed the accounting principles used, significant estimates made and the overall consolidated financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements give a true and fair view of the financial position, the results of operations and the cash flows in accordance with the International Financial Reporting Standards (IFRS) and comply with Swiss law.

We recommend that the consolidated financial statements submitted to you be approved.

KPMG Fides Peat

Hanspeter Stocker
Swiss Certified Accountant

Thomas Schmid
Swiss Certified Accountant
Auditor in Charge

Zurich, 18 January 2004

Financial statements of Lonza Group Ltd

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Balance sheet – Holding

	CHF	2002	2003
Assets¹	Fixed assets		
	Property, plant and equipment	3	2
	Investments	881 146 497	873 258 297
	Long-term loans to subsidiaries	76 124 878	131 574 483
	Total fixed assets	957 271 378	1 004 832 782
	Current assets		
	Receivables:		
	From third parties	561 676	7 024
	From subsidiaries and affiliates	4 388 085	3 016 947
	Prepaid expenses:		
	Third parties	842 550	8 354 924
	Subsidiaries and affiliates	5 100 404	772 140
	Short-term advances:		
	Subsidiaries and affiliates	606 440 824	637 217 262
	Marketable securities:		
	Own shares	71 710 968	60 373 143
	Cash	4 616 240	1 706 870
	Total current assets	693 660 747	711 448 310
	Total assets	1 650 932 125	1 716 281 092

¹At 31 December

CHF	2002	2003	
Shareholders' equity			Liabilities and shareholders' equity¹
Share capital	50 450 000	50 450 000	
Legal reserve:			
General legal reserve	25 225 000	25 225 000	
Reserve for own shares	336 311 343	335 958 272	
Available earnings brought forward	309 557 096	425 147 194	
Net income for the year 2002 and 2003	205 247 993	311 915 066	
Total shareholders' equity	926 791 432	1 148 695 532	
Liabilities			
Long-term liabilities			
Long-term debts:			
Due to third parties	0	375 000 000	
Long-term provisions:			
Due to third parties	0	832 463	
Total long-term liabilities	0	375 832 463	
Current liabilities			
Payables and other liabilities:			
Due to third parties	1 469 273	6 131 143	
Due to subsidiaries and affiliates	446 272	2 896	
Accrued expenses:			
Due to third parties	4 975 243	11 648 105	
Short-term provisions:			
Due to third parties	497 540	669 641	
Short-term debts:			
Due to third parties	482 850 000	143 770 000	
Due to subsidiaries and affiliates	233 902 365	29 531 312	
Total current liabilities	724 140 693	191 753 097	
Total liabilities	724 140 693	567 585 560	
Total liabilities and shareholders' equity	1 650 932 125	1 716 281 092	
	%	%	
Shareholders' equity as a percentage of total assets	56.1	66.9	

¹At 31 December

Income statement – Holding

	CHF	2002	2003
Income			
Income from investments		263 361 363	308 253 554
Income from sale of investments		54 991 161	0
Income from sale of property		299 999	35 108 455
Interest income		48 648 815	35 001 141
Other financial income		0	13 933 963
Other income		3 973 259	4 904 448
Total income		371 274 597	397 201 561
Expenses			
Personnel expenses		8 334 157	7 686 415
Other administrative expenses		4 565 664	6 788 501
Interest expenses		42 532 501	30 716 888
Other financial expenses		7 351 724	11 013 718
Provision on loan		46 800 000	0
Taxes		888 510	9 844 445
Other expenses		2 374 966	1 294 528
Write-offs on investments		53 179 082	17 942 000
Total expenses		166 026 604	85 286 495
Net income for the year		205 247 993	311 915 066

<p>At 31 December 2003, indemnity liabilities, guarantees and pledges in favour of third parties totaled CHF 163 229 463 (31 December 2002: CHF 174 238 403). The company is a member of the Lonza Group value-added-tax group in Switzerland and is thereby jointly and severally liable to the federal tax authorities for value-added-tax debts of that group.</p>	<p>Contingent liabilities 1</p>
<p>31 December 2003: CHF 5 456 000 (31 December 2002: CHF 30 053 000)</p>	<p>Fire insurance values of property, plant and equipment 2</p>
<p>31 December 2003: CHF 598 034 (31 December 2002: CHF 70 000)</p>	<p>Liabilities to personnel welfare institutions 3</p>
<p>See list of Significant subsidiaries, page 62</p>	<p>Investments 4</p>
<p>Lonza was informed by EMS-Chemie Holding AG that it held 11 359 047 nominal shares representing 22.52 % of the voting rights as of 31 December 2003. Lonza is not aware of any other shareholder owning more than 5 % of its share capital as of the end of the year.</p>	<p>Major shareholders in accordance with Art. 663c of the Swiss Code of Obligations 5</p>
<p>At 31 December 2003, Lonza Group Ltd and one of its subsidiaries held 3 071 352 of its own registered shares with a par value of CHF 1 each (31 December 2002: 3 075 924), resulting in a reserve for own shares of CHF 335 958 272 (31 December 2002: CHF 336 311 343).</p>	<p>Own shares 6</p>
<p>In order to satisfy the exercise of the Share Option Plans for key employees and the Employee Share Purchase Plan, Lonza Group Ltd acquired 3 723 registered shares, with a par value of CHF 1 each during 2003, at an average market value of CHF 63. In 2003, Lonza Group Ltd provided 567 registered shares, at an average market value of CHF 73 and sold 7 728 registered shares at an average market value of CHF 70. 849 130 of the own registered shares with a par value of CHF 1 each (31 December 2002: 853 702) are reserved for the Share Option Plans and the Employee Share Purchase Plan. 2 222 222 registered shares with a par value of CHF 1 each are reserved for Lonza Finance Ltd's convertible bond, purchased in 2002 at an average market price of CHF 118.</p>	
<p>The total of registered shares not entitled to a dividend is therefore 3 071 352 with a par value of CHF 1 each (2002: 3 075 924).</p>	
<p>In February 2003, Lonza Group Ltd issued a 2 % bond of CHF 375 000 000, at an issue price of 100.69 %, with maturity date 14 February 2006.</p>	<p>Long-term debts 7</p>
<p>Exchange gains/losses – Other financial income includes in 2003 net realized exchange rate gains of CHF 9 163 962. (In 2002, exchange rate losses of CHF 5 338 498 were included in other financial expenses).</p>	<p>Additional notes 8</p>
<p>There were no other circumstances subject to the reporting requirements of Art. 663b CO.</p>	

Proposal of the Board of Directors concerning the appropriation of available earnings

CHF	2002	2003
Available earnings brought forward	309 557 096	425 147 194
Net income for the year	205 247 993	311 915 066
Available earnings at the disposal of the Shareholders' Meeting	514 805 089	737 062 260
Payment of a dividend of CHF 1.30 (2002: CHF 1.90 per share) on the share capital eligible for dividend of CHF 47 378 648 (2002: CHF 47 374 192)	90 010 965	61 592 242
Available earnings carry-forward	424 794 124	675 470 018
Dissolution reserve for own shares in the 2003 business year	353 070	
Available earnings brought forward after dissolution reserve	425 147 194	

If the Shareholders' Meeting approves the above proposal from the Board of Directors, the dividend of CHF 1.30 per registered share, less 35 % withholding tax, will be paid on 6 April 2004 at the offices designated in the publication organ of the company and in selected daily newspapers.

Basel, 18 January 2004

Sergio Marchionne
Chairman of the Board

Markus Gemuend
Chief Executive Officer

As Statutory Auditors, we have audited the accounting records and the financial statements (balance sheet, income statement and notes on pages 83 to 88) of Lonza Group Ltd, Basel, for the year ended 31 December 2003.

These financial statements are the responsibility of the Board of Directors. Our responsibility is to express an opinion on these financial statements based on our audit. We confirm that we meet the legal requirements concerning professional qualification and independence.

Our audit was conducted in accordance with auditing standards promulgated by the Swiss profession, which require that an audit be planned and performed to obtain reasonable assurance about whether the financial statements are free from material misstatement. We have examined on a test basis evidence supporting the amounts and disclosures in the financial statements. We have also assessed the accounting principles used, significant estimates made and the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the accounting records, financial statements and the proposed appropriation of available earnings comply with Swiss law and the Company's Articles of Association.

We recommend that the financial statements submitted to you be approved.

KPMG Fides Peat

Hanspeter Stocker
Swiss Certified Accountant

Thomas Schmid
Swiss Certified Accountant
Auditor in Charge

Zurich, 18 January 2004

Lonza Group Ltd shares are listed on the SWX Swiss Exchange and included in the Swiss Market Index (SMI). The shares are traded on the virt-x, an electronic trading system based in London. The nominal value of the Lonza Group Ltd share amounts to CHF 1.

In the first four months of 2003, the Lonza Group share price performed in line with the Swiss Performance Index and achieved the year high of CHF 85.55 after a short sharp rise from the end of April till the beginning of May. Following the disclosure about the revised outlook for 2003 due to difficult market conditions in most of Lonza's business lines, the Lonza Group Ltd share price decreased to CHF 66.50 on 19 May 2003. In the second half of the year, the share price moved mostly in a range between CHF 60 and CHF 70.

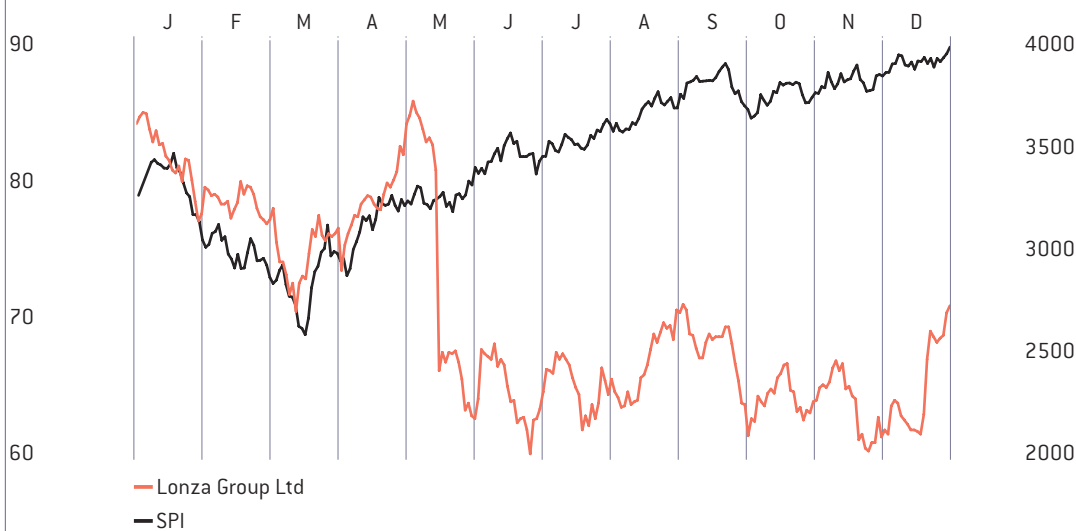
In December 2003, EMS-Chemie Holding AG as the major shareholder of Lonza Group Ltd increased its interest in Lonza Group Ltd nominal shares to 11 359 047 through the exercise of put-options and holds 22.52 % of the voting rights.

Daily trade volume was CHF 27.8 million or 394 460 shares on average.

Lonza Group Ltd

CHF

SPI Share price and index development



Information per security

		2002	2003
Registered shares			
Number of shares issued		50 450 000	50 450 000
Number of shares ranking for a dividend ¹		47 374 192	47 378 648
Par value per share	CHF	1	1
Net income	CHF million	221	91
Net income before non-recurring items	CHF million	297	198
Diluted net income	CHF million	226	101
Diluted net income before non-recurring items	CHF million	302	208
Ratios per security			
Weighted average number of shares		48 558 988	47 374 733
Diluted weighted average number of shares		50 652 926	50 450 000
Basic earnings per share	CHF	4.55	1.92
Basic earnings per share before non-recurring items	CHF	6.12 ²	4.18 ³
Diluted earnings per share ⁴	CHF	4.46	2.00
Diluted earnings per share before non-recurring items ⁴	CHF	5.96 ²	4.12 ³

¹ See note 26 on page 75

² Excluding net income after tax from non-recurring items of CHF 76 million

³ Excluding net loss after tax from non-recurring items of CHF (107) million

⁴ Diluted earnings per share for 2002 have been restated by the weighted average number of shares taking the shares for the employee benefit programs into account.

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Sales offices

This annual report is also available in German.
The English version prevails.

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Lonza

Anticipated key reporting dates

Ordinary Shareholders' Meeting
for the financial year 2003
31 March 2004, 2.30 pm
Convention Center Basel

Half Year Results 2004
21 July 2004

Full Year Report 2004
26 January 2005

Ordinary Shareholders' Meeting
for the financial year 2004
23 March 2005

Dividend transfer to banks

As a rule, Lonza Group Ltd pays the dividend to its shareholders on the fourth business day following the Ordinary Shareholders' Meeting.

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Stock exchange listing
SWX Swiss Exchange**Stock exchange trading**
virt-x**Common stock symbols**

Bloomberg LONN VX
Reuters LONZn.VX
Telekurs LONN

Security number

Valor 001384101
ISIN CH0013841017

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