evotec OAI

Leading innovation speed

Successful partnerships

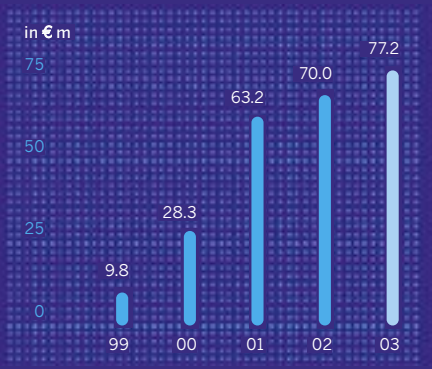
Commitment

Productivity

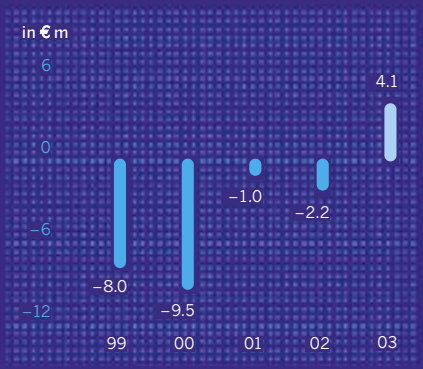
Trust

Evotec OAI AG	Page		2002	2003	Δ 03 | 02 in %
Results					
Revenue	22	T€	69,995	77,228	10.3
R&D expenses	23	T€	23,012	15,466	(32.8)
Operating loss*	23	T€	14,105	5,106	(63.8)
Net loss	24	T€	131,630	14,242	(89.2)
EBITDA	24	T€	(2,221)	4,086	284.0
Cash flow	24	T€	5,313	(1,333)	(125.1)
Balance sheet data					
Stockholders' equity	26	T€	195,407	172,101	(11.9)
Capital expenditure**	25	T€	7,327	14,204	93.9
Cash including marketable securities	25	T€	21,308	19,471	(8.6)
Balance sheet total	26	T€	241,042	220,919	(8.4)
Personnel data					
Employees as of 31 December	50		635	644	1.4
Per share					
Result	24	€	(3.71)	(0.40)	89.2

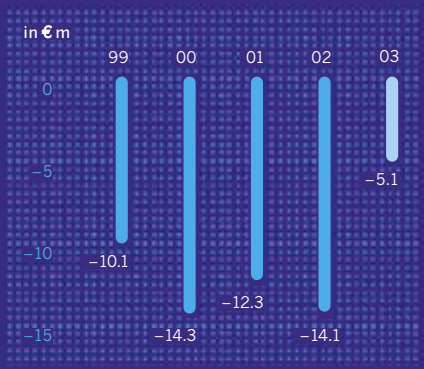
Revenue
Delivering on promises



EBITDA
Positive for the first time in company history



Operating result*
Planned cost reductions resulted in significant improvements



* before amortisation and impairment
** purchase of fixed and intangible assets, excluding capital leases

Synergistic partnerships

Throughout history, mankind has evolved by constantly creating and utilising new knowledge. Creating synergies has always been one of the most effective techniques to do so. At Evotec OAI, we therefore advocate and practise a **synergistic** approach to working with our customers. We endeavour to complement our customers' skills in order to create something new and different which neither we nor our partners could achieve alone.

At Evotec OAI, we know from experience that a synergistic relationship can only thrive when it is built on **partnership**. The term stems from the old French word "parçonier" which, in English, evolved through "parcener" to "partner", meaning that each has a "**part**" of the other, seeing things through each others eyes and thereby gaining a deeper understanding of the respective points of view. In fact, this is the only way we can assess the effect that we and our work have on our customers and their research. This insight enables us to take a share (or "**part**") of the responsibility for the results achieved, going far beyond merely delivering quality services. It is this sense of responsibility that breeds trust.

Our employees build on their combined experience of hundreds of years in collaborative research with customers to create this kind of **trusting relationship**. It is this bond of trust that enables us to communicate openly and thus to move on swiftly in research, thereby ultimately enhancing our customers' productivity. When they experience a partnership of this kind and when we fulfil their wishes, sometimes before they are even voiced, then we have created value and only then are we satisfied with what we have achieved.

Discovery and Development Services (DDS)

> Premier provider of integrated discovery + development solutions
> Top capabilities in assay development, screening and chemistry
> Portfolio expansion: structural biology, comp. chemistry, ADMET
> Strong and increasing base of repeat customers
> Significant deal flow despite challenging outsourcing environment
> +17% growth in local currencies, positive operating result**
> New discovery building in Oxford to support future expansion

Discovery Programs Division (DPD)

> Discovery of internal drug candidates for out-licensing
> Leveraging DDS' strong drug discovery + development engine
> Launch of research projects in CNS and Metabolic Diseases
> Strategic alliance with DeveloGen in Metabolic Diseases
> € 20 m contract with Takeda in Alzheimer's Disease
> ENS licensed in 5 CNS compounds from Roche
> ENS prepared for venture capital financing

Tools and Technologies (ET)

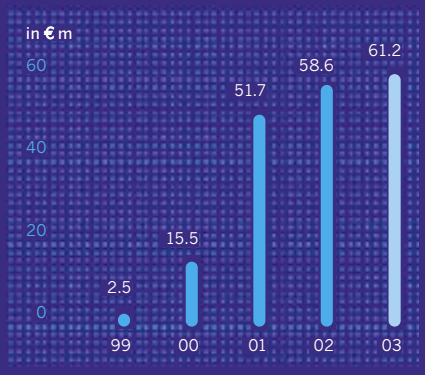
> Quality provider of life science tools and technologies
> Evotec Technologies: First full year as a stand alone company
> Two new bench-top devices launched: Elektra and Clarina II
> Successful collaborations with Pfizer and Olympus continued
> Large number of new customer relationships secured
> Outstanding top-line growth of 64%
> Pfizer became a 10% shareholder in Evotec Technologies

Condensed key figures DDS

		2002*	2003	Δ 03 | 02 in %
Revenue	T€	58,588	61,214	4.5
– Thereof 3rd party	T€	58,588	58,582	0.0
Gross margin	%	40.7	39.1	–
Operating result	T€	(133,373)	(10,422)	92.2
Operating result before amortisation				
and impairment	T€	(12,426)	9	–
R&D expenses	T€	15,213	8,112	(46.7)
Depreciation and allowances	T€	10,558	9,319	(11.7)
Number of employees as of 31 December				
without corporate overhead		458	440	(3.9)

* in 2002 DDS included DPD business
** before amortisation and impairment

Revenue

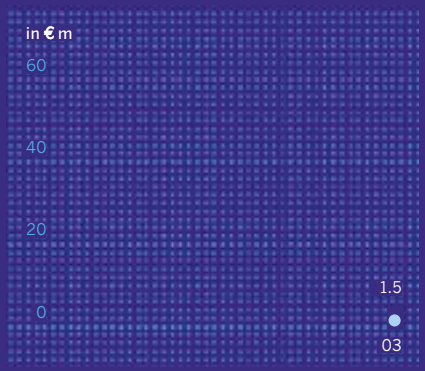


Condensed key figures DPD

		2002*	2003	Δ 03 | 02 in %
Revenue	T€	–	1,479	–
– Thereof 3rd party	T€	–	1,464	–
Gross margin	%	–	55.7	–
Operating result	T€	–	(5,356)	–
Operating result before amortisation				
and impairment	T€	–	(5,301)	–
R&D expenses**	T€	–	4,324	–
Depreciation	T€	–	425	–
Number of employees as of 31 December				
without corporate overhead		–	28	–

* in 2002 DDS included DPD business
** excluding € 1.4 m DeveloGen joint venture R&D expenses

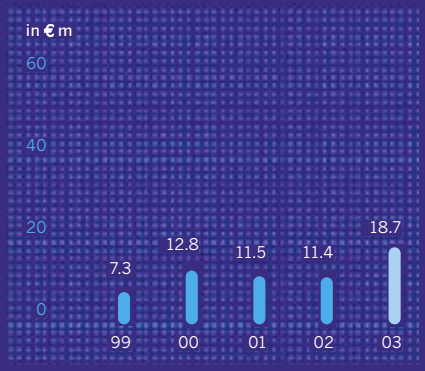
Revenue



Condensed key figures ET

		2002	2003	Δ 03 | 02 in %
Revenue	T€	11,407	18,668	63.7
– Thereof 3rd party	T€	11,407	17,197	50.7
Gross margin	%	67.0	43.7	–
Operating result	T€	(2,139)	(1,140)	46.7
Operating result before amortisation				
and impairment	T€	(1,678)	(161)	90.4
R&D expenses	T€	7,799	5,043	(35.3)
Depreciation and allowances	T€	547	1,030	88.3
Number of employees as of 31 December				
without corporate overhead		88	84	(4.5)

Revenue



Deal flow 2003

In 2003, we reinforced our position as the drug discovery and development partner of choice, announcing more agreemens than any of our competitors. Published new contracts are outlined below.

January

Oxagen
Evotec OAI will apply its fully integrated drug discovery process know-how to identify chemical compounds interacting with one of Oxagen's lead targets.

KeyNeurotek | Institute of Medical Technology Magdeburg (IMTM)
Evotec OAI announces drug discovery agreement to identify small molecule drug candidates to treat distinct CNS, autoimmune, allergic and dermatologic diseases.

Euroscreen
Euroscreen and Evotec OAI partner GPCR expertise.

Psychiatric Genomics
Psychiatric Genomics selects Evotec OAI as their strategic chemistry partner for drug discovery and development to treat psychiatric diseases. Three year agreement, using Evotec OAI's state-of-the-art medicinal chemistry skills and integrated ADMET profiling.

Dynogen
Evotec OAI enters into a three-year drug discovery and development services agreement with Dynogen. Dynogen will benefit from Evotec OAI's entire chemistry and biology capabilities to identify and advance neurological compounds to treat genitourinary and gastrointestinal disorders.

March

British Biotech
As part of their merger with RiboTargets, British Biotech transfers 17 research scientists and outsources medicinal chemistry and biology research activities for its anti-inflammatory and anti-bacterial drug discovery programmes to Evotec OAI.

April

Novartis
Evotec OAI and Novartis Pharma sign assay development and screening contract to identify drug candidates for several undisclosed Novartis targets.

May

Artesian Therapeutics
Evotec OAI and Artesian enter into a three-year drug discovery service agreement to optimise small molecule therapeutics for the treatment of congestive heart failure.

Axxima Pharmaceuticals
Evotec OAI signs medicinal chemistry agreement with Axxima Pharmaceuticals to design and synthesise small molecule lead structures for one of Axxima's leading kinase targets.

DeveloGen
Evotec OAI and DeveloGen announce a strategic drug discovery and development alliance for Metabolic Diseases. By sharing risks and rewards equally both parties are leveraging their complementary skills to rapidly produce potent and promising product candidates to fill their future partners' clinical pipelines.

June

August

Takeda Chemical Industries
Evotec Neurosciences (ENS) and Takeda announce a four-year collaboration to identify and validate novel targets relating to different aspects of the causes and progression of Alzheimer's disease, with the goal of developing innovative therapeutics. ENS will receive payments from Takeda of up to € 20 m and substantial additional milestone payments for the successful clinical development of compounds acting on selected targets.

September

October

Biofrontera
Evotec OAI and Biofrontera sign a co-marketing and distribution agreement to offer natural compounds for drug discovery services.

Roche
Evotec OAI and Roche expand their partnership through a medicinal chemistry collaboration to identify and develop a clinical lead candidate for one of Roche's cancer targets.

Content

12 DeveloGen
The joint venture with Evotec OAI allows DeveloGen to develop and exploit their pipeline of validated targets in Metabolic Diseases on an industrial scale and to the highest possible standards.

18 Curis
Curis' partnership with Evotec OAI has been very productive, resulting in an IND oncology drug candidate within 18 months which significantly contributed to their oncology agreement with Genentech in 2003.

28 Celgene
Evotec OAI has been Celgene's partner of choice for over 5 years, providing an excellent understanding of their projects and the technical, quality and regulatory processes needed to bring innovative pharmaceuticals to patients.

34 Elixir Pharmaceuticals
In just over a year Evotec OAI has delivered to Elixir a number of validated lead series and Elixir firmly believes that the partnership has saved them, overall, two years in their development.

40 GlaxoSmithKline
Evotec's EVOscreen® Mark III has become a key platform at GlaxoSmithKline for miniaturised screening in the low-microlitre range.

46 Novartis
Evotec OAI has delivered outstanding results for two challenging adherent cell assays, and Novartis scientists now benefit from this newly established uHTS process on their own EVOscreen® Mark III as a basis for accelerating their internal drug screening.

Joern Aldag
Chief Executive Officer and President

Dr Dirk H. Ehlers
Chief Financial Officer

To our shareholders

Evotec OAI had a successful 2003. Revenues grew by 10%, in constant currencies by 21%, and EBITDA was positive for the first time in the company history.

We are pleased to report that the Evotec OAI Group had a successful 2003 which we attribute to reliable and long-term partnerships. Throughout this annual report we highlight several relationships between Evotec OAI and our customers that illustrate our highly successful business model—resulting in an expanding market position. We also delivered on our operational plans in all our three divisions.

> We grew total Group revenues by 10% to € 77.2 m, delivering on our guidance for the year.
> We implemented tight cost controls on many of our operational activities, group-wide, to achieve EBITDA of € 4.1 m, reporting profitability, on an EBITDA level, for the first time in company history.
> We achieved positive operating income before amortisation in our Discovery and Development Services. Tools and Technologies were close to break-even.
> We delivered on our Discovery Programs strategy to expand our internal research activities through a strategic alliance with DeveloGen to develop drug candidates for Metabolic Diseases.
> We secured a € 20 m alliance with Takeda to expand research activities at our Evotec Neurosciences (ENS) subsidiary.

We believe that this performance and "delivery on promises" has also helped our stock price to recover from the low 2002 levels, increasing by 181% during the year.

Defying market trends. Our success in 2003 has defied world market and industry trends. Revenues grew despite a challenging outsourcing environment combined with a dramatic deterioration of the U.S. Dollar and the British Pound against the Euro. Contract research revenues for many of our competitors declined due to under-funded biotechnology companies and a reallocation of resources from discovery to development within the pharmaceutical industry.

Dr Ian M. Hunneyball
President, Services Devision

Bernard Questier
Chief Business Officer

Dr Timm-H. Jessen
Chief Scientific Officer

Our DDS division has matured to become a productive and solid drug discovery and development engine.

Discovery and Development Services (DDS) is core. Our DDS division has matured to become an industry standard as well as a productive and solid drug discovery and development engine for both our customers and our internal Discovery Programs Division. We can now focus on expanding the breadth of our service offerings and solutions to provide both our internal and external projects with new capabilities throughout the drug discovery and development processes. This year:

> We greatly enhanced our cell based assay and screening capabilities in medium and high throughput mode, increasing flexibility and data content.
> We added significant capabilities in computational and rational discovery approaches, notably computational chemistry, virtual screening, structural biology and early ADMET.
> We continued to build our target class expertise, in particular in ion channels and in G-Protein Coupled Receptors.

We are convinced that our combined breadth of services and focused expertise truly makes the drug discovery and development processes more efficient.

We delivered on our Discovery Programs strategy, expanding our internal discovery activities through alliances with DeveloGen, Roche and Takeda.

Discovery Programs Division (DPD) showing tremendous progress. We have made great progress in extracting higher value from our core capabilities through DPD. This division is focused on internal discovery programmes to fill the empty pipelines of our partners with drug candidates. We expanded our disease oriented capabilities through creative partnerships and utilised financing from partnerships to accelerate our exciting neurology programmes:

> Evotec Neurosciences (ENS) successfully closed a large pharma deal with Takeda valued at approx. € 20 m validating our target discovery technologies in our collaboration with the University of Zurich; we in-licensed 5 compounds at lead or drug candidate stage from Roche for the treatment of various neurodegenerative diseases, and in early 2004 we prepared a major financing with a strong group of financial investors to further develop ENS programmes with a minimal cash exposure to Evotec OAI.
> We established a landmark collaboration with DeveloGen AG, Göttingen, Germany, to build a speciality group in Metabolic Diseases; together we will develop drug candidates and proof-of concept drugs for a partner in the field of Metabolic Syndrome, Obesity and Diabetes Type II; we have already started four projects, three of which are in the 'hit to lead process', with one in screening. We are entertaining discussions with pharma companies to join into these promising research projects in order to be able to afford a significant expansion of the number of programmes we can run in parallel.

ET grew top-line by over 60%, launched two new products and continued being successful in collaborating with existing and a large number of new customers.

Strong year for Evotec Technologies (ET). ET was successfully spun out in 2002 and achieved all of its major objectives in 2003. The division has:
> Grown the top-line by over 60%;
> Streamlined operations and came close to positive operating result before amortisation;
> Launched two important new products;
> Continued successful collaborations with Pfizer and Olympus; and
> Secured a large number of new customer relationships.

The successful spinout of this division is a tremendous achievement and a great testament to our strategy of ET becoming a leading profitable provider of life science tools and technologies to the industry. More importantly, all of our divisions are major beneficiaries of this highly productive technology group.

We plan for 2004 to become a year of strong operational performance, EBITDA profitability, and strategy implementation.

Outlook for 2004. While we expect only a modest recovery in the contract research market in 2004, we expect to continue to grow. We have expanded our facilities in Oxford and laid the ground for a growing services business in parallel to building our internal programmes. We will continue to benefit from the partnering needs of the pharmaceutical and biotechnology industries to access our chemistry and core discovery capabilities. We plan for 2004 to become a year of strong operational performance, EBITDA profitability, and strategy implementation. We have one of the strongest brands in the industry, an unmatched customer base and highly motivated and competent people. Our powerful discovery and development engine and partnerships have positioned us as the premier provider of research solutions and intermediary products.

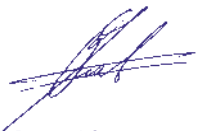
We thank our shareholders, customers and our staff for their loyalty, professionalism and collaborative spirit during the past year. Together, even in a difficult environment, we delivered on our challenging objectives and expanded our market share. And with this encouraging experience, we look forward to further progress in 2004.

Joern Aldag
Chief Executive Officer
and President

Dr Dirk H. Ehlers
Chief Financial Officer

Dr Ian M. Hunneyball
President, Services Devision

Dr Timm-H. Jessen
Chief Scientific Officer



Bernard Questier
Chief Business Officer

Our strategy

Evotec OAI is rapidly becoming a world leader in providing drug candidates—from target to proof-of-concept. We are discovering the next generation of novel drugs through both service partnerships and investments into our own internal programmes.

The pharmaceutical industry increasingly relies on biotechnology companies to increase their productivity in research—a great opportunity for Evotec OAI.

Industry needs strong discovery partners. The ever-consolidating pharmaceutical industry is clearly focused on top-line growth for economies of scale in product development, marketing and sales. In research this has made the pharmaceutical companies more dependent on the biotechnology industry and intermediary discovery companies to fuel their massive product development engines.

This environment presents great opportunities for dedicated R&D organisations such as Evotec OAI. Demand for compounds which have demonstrated proof-of-concept in man has clearly outpaced supply from internal programmes. This leads many pharmaceutical companies to increasingly rely on discovery outsourcing to strong and reliable suppliers. The pharmaceutical industry is also signing earlier deals to acquire pre-clinical development candidates to supplement their own pipelines of products. The purpose of this is to increase "shots on goal" and to benefit from the entrepreneurial spirit of the smaller biotech organisations.

Also disease-driven biotechnology companies need to partner. They often lack modern drug discovery expertise and critical mass to advance compounds into the clinic on their own.

At the same time, a great number of biotechnology firms have developed a thorough understanding of the molecular mechanisms underlying diseases. However, these firms often lack state-of-the-art drug discovery expertise, compound libraries, and critical mass and financial stability for advancing compounds into the clinic on their own. They need to partner with strong companies such as Evotec OAI in order to survive in a world of fierce competition for capital and novel drugs.

Evotec OAI is ideally positioned. In this environment a business focused on providing an industrial process, delivering high class proof-of-concept compounds has a great strategic opportunity and benefits at both ends: We have built one of the strongest discovery engines worldwide to meet the needs of both the pharmaceutical and biotechnology industries. We are industrial, yet entrepreneurial, operating with a passion to get things done fast, utilising the highest quality standards. The ingredients for our success are a universal discovery approach based on an integrated discovery platform complemented by strong target class and disease expertise and a broad customer network. Our biotechnology partners value the integration of our offering, our speed and our responsiveness. Our pharmaceutical partners value our dedication to results and our critical mass, helping them to greatly reduce the number of partners they need.

Many of our customers recognise the role we can play in bridging the gap between early stage research and the clinic.

Many of our established pharmaceutical and research driven biotech customers recognise our capabilities and the role we can play in bridging the gap between early stage discovery and the clinic.

DDS focuses on providing contract R&D support to our internal programmes at arm's length and to a strong network of partners who reward us with fees for services and success payments.

In DPD we develop drug candidates for out-licensing in partnerships which are outcome based and risk and benefit sharing in nature, including higher milestone payments and royalties.

In DPD we will create long-term value with our partners. However, we will not compete with our customers.

Strategy reflected in business structure. To maximise the value of our offerings we operate through two separate drug discovery divisions, DDS and DPD, complemented by Evotec Technologies:

> Our Discovery and Development Services (DDS) business focuses on providing contract research and development support to our customers and to our internal programmes, using the best platform of technologies, skills, experience and resources. Customers reward us with fees for services and success payments upon delivery of agreed-upon results and sometimes even clinical milestone payments and potential royalties. Our customers own the intellectual property on compounds generated during the collaboration. We extend and protect our property rights on the technology platform. This services business is where we have generated the vast majority of our revenues and have built our strong network of pharma and biotech partners.

> Our Discovery Programs Division (DPD), since 2003 a separate business segment, engages in selected proprietary discovery activities to develop compounds for out-licensing or joint discovery and early development with selected partners. This research relies on innovative disease biology from biotech or academic partners, or on highly validated, sometimes non-proprietary targets, where the key to success is high quality chemistry. For non-target-specific work DPD uses our DDS division on a subcontractor basis. Investing in R&D upfront DPD builds intellectual property and pre-clinical data, with the purpose to deliver higher value intermediaries to our customers. We will not, however, compete with the pharmaceutical industry. We intend to create partnerships which can be outcome based and risk and benefit sharing in nature, including higher milestones and royalties.

> Evotec Technologies (ET), spun out into a separate legal entity under separate management in 2002, comprises all instrument related business of the group. It is selling high value innovative instruments and related consumables, focusing on detection, automation and cell handling technologies that resolve bottlenecks in drug discovery and cell biology workflows. DDS and ET benefit from marketing and sales synergies, serving the same pharmaceutical partners, and from prototyping new technologies in DDS' discovery operations.

Growing internal programmes (DPD). While DDS and ET are established businesses today, DPD has built momentum in 2003: We closed a twenty million Euro deal with Takeda in the field of neurodegenerative diseases. We also established a landmark collaboration with DeveloGen AG, Göttingen, Germany, in Metabolic Diseases (Obesity and Diabetes Type II) and have started four programmes to find and optimise small molecule therapeutics against these indications.

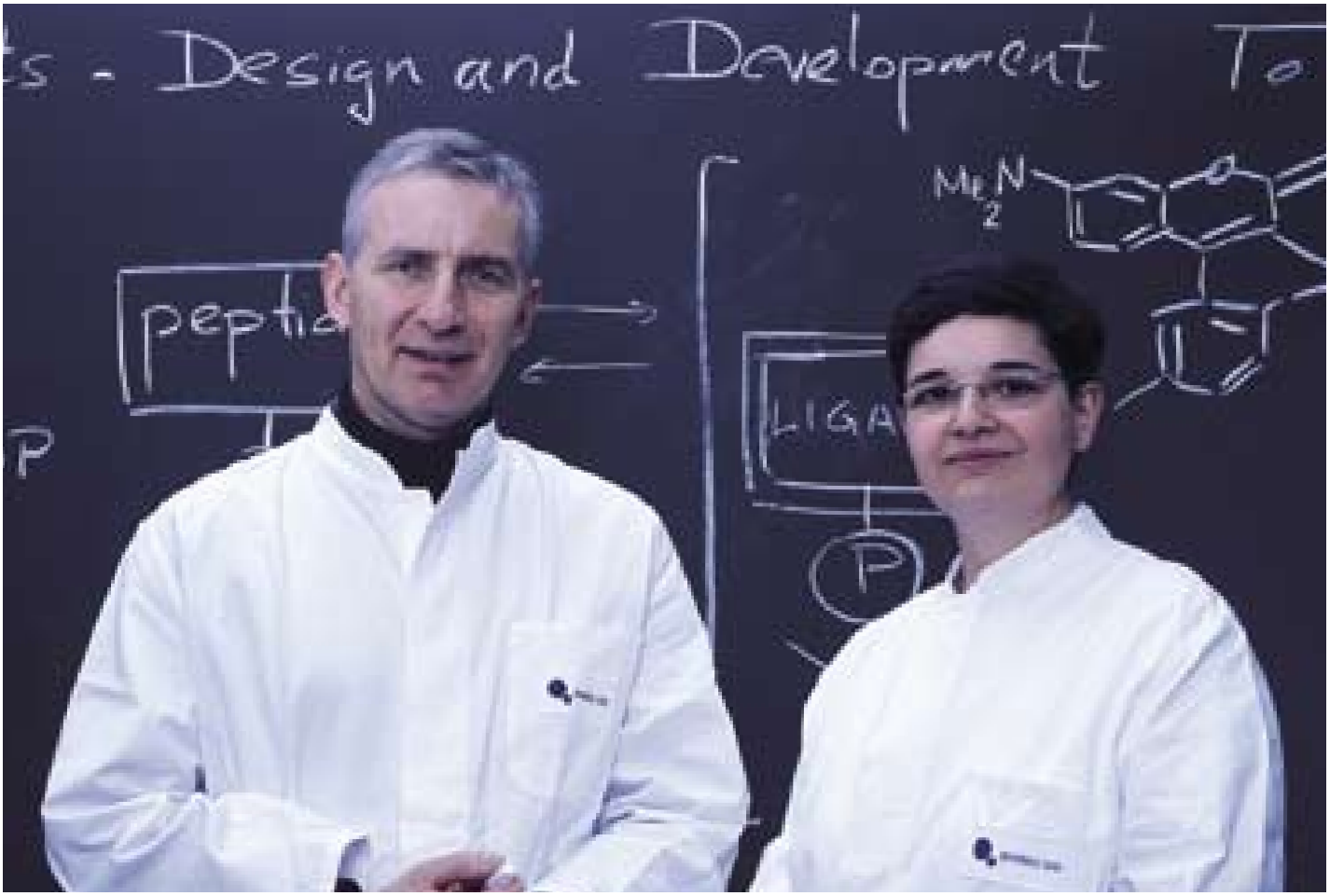
Future growth of DPD will depend primarily upon our financial resources. To meet our financial needs we are entertaining discussions with pharmaceutical companies to join into and co-fund such programmes. For our Evotec Neurosciences subsidiary we are actively pursuing venture financing to fund the development of new drug candidates.

Günter Karmann
DeveloGen AG
Chief Executive Officer

"The joint venture with Evotec OAI allows us to develop and exploit our pipeline of validated targets on an industrial scale and to the highest possible standards. With the collaboration, we bring our biology to the drug candidate stage which is where significant value is captured."

Dr Eloisa Lopez-Calle
Evotec OAI AG
Unit Head, Applied Biology and Chemistry

In September 2003 Evotec OAI and DeveloGen, a leader in the understanding of emerging mechanisms of Metabolic Diseases, entered into a strategic alliance to develop novel small molecule drugs in the fields of obesity and Type II diabetes. This partnership brings together top tier expertise and professional resources across the entire drug discovery process. A team of over 40 scientists is devoted to the joint programmes with four targets already in drug discovery. The progress in the JV is exceeding expectations.



Going forward we aim to further reinforce our position as the premier provider of research services and intermediary products and to capture a growing share of the tremendous value created by the pharmaceutical industry.

Capturing value in a difficult environment. Our key objectives in 2004 are to further reinforce our strategic position as the premier provider of research services and intermediary products. Our core assets are our comprehensive world-class platform, breadth of skills amongst our scientists and the many established partnerships with our customers. We now seek more creative, risk-sharing partnerships, leveraging complementary strengths, and ultimately capturing a growing share of the tremendous value that is created by the pharmaceutical industry.

Our partners

Synergistic partnerships exist in a scientific context by bonding biological targets with specific small molecules to create high quality and high value drug candidates to treat diseases, a process Evotec OAI help to create. Synergistic and long-term partnerships between our customers and Evotec OAI are the essence of our commercial success. In a trustful relationship we provide our partners with innovative solutions on time and to budget with a commitment to value, speed and customer service to ultimately enhance their productivity. Such synergistic and long-term partnerships are the essence of our commercial success.

Our company evolved in 2003 as one of the fastest growing solution providers and as the clear partner of choice (see "Deal flow", page 2 and 3) for drug discovery and development. Based on a strong and repetitive customer base ranging from big pharma to small biotech companies we have achieved an unmatched level of expertise and an outstanding track record for delivery. Going forward we strive to maximise value to our customers by providing world-class drug discovery and development solutions or by teaming up in risk and benefit sharing arrangements.

We grew repeat business from our existing customer base. Most notably, we significantly expanded our collaborations with Roche and Novartis.

Long-term relationships. Given the breadth of our integrated offering we are in a position to help our customers through more stages of drug discovery and development than any of our competitors. As a result, we had been able to grow repeat business from our existing customer base from about 50% in 2002 to over 60% in 2003. Most notably, we were able to significantly expand our existing collaborations with two major pharma companies, namely

> Roche expanded the relationship with us over and above our ongoing chemical library partnership by tapping into our medicinal chemistry expertise on a high profile oncology research compound

> Novartis, a long-term partner in the development of our EVOscreen® uHTS technology, has asked us to support their lead discovery efforts by adding our assay development and screening capabilities.

We also continued our successful collaboration with other leading pharma customers such as Astra Zeneca, GlaxoSmithKline, Merck and Pfizer, and with leading biotechnologies firms including Amgen, Biogen and Vertex. In addition, we grew collaborations with emerging biotechnology companies such as BioImage, Elixir Pharmaceuticals, Infinity, Oxigene and Prolysis in the areas of assay development, screening and medicinal chemistry. In development chemistry, we strengthened our relationships with Alizyme, Celgene, DuPont and Serono.

Evotec OAI secured deals with more than 30 new customers. A number of them will benefit from our full range of integrated capabilities.

New customers. Despite the continued difficult market environment, we were able to secure deals with more than 30 new customers in 2003. Most notably, we initiated collaborations with several pharmaceutical and biotechnology companies which will benefit from Evotec OAI's full range of integrated capabilities across the drug discovery and development value chain, namely Dynogen, Oxagen and Toray. In the U.S., following our innovative deal with the Boston based venture capital firm Oxford Bioscience Partners (OBP) in late 2002, we gained further business from their portfolio companies in addition to our partnership with Elixir. New customers include Artesian, Psychiatric Genomics and Rib-X in the areas of medicinal chemistry and ADMET services. In development chemistry, we added Anormed and Stiefel to our customer list. We also succeeded in significantly growing our business with new biotech customers in Europe, notably Axxima and Key Neurotek. Our dedicated business development efforts in Japan are increasingly bearing fruit with highlights including the integrated collaboration with Toray in medicinal chemistry, virtual screening and compound profiling and our CNS partnership with Takeda (see below).

Our innovative umbrella concept with OBP has proven to be very successful with Evotec OAI collaborating with seven of their portfolio companies already.

Setting new deal standards. Our recent umbrella contract with Oxford Bioscience Partners (OBP) established us as the premier solution provider for emerging biotech companies in their investment portfolio. This concept has proven to be very successful with Evotec OAI working for seven OBP portfolio companies already. We have now secured a similar deal with MPM Capital, a leading global Venture Capital firm, and are currently in negotiations with some of their portfolio companies concerning a potential collaboration.

Risk- and benefit-sharing research collaborations. In 2003, we achieved two major milestones with respect to our strategy to increasingly build indication-specific research programmes, to extract higher value from our core capabilities and to increase research productivity for our customers by building a pipeline of drug candidates.
Evotec Neurosciences (ENS) granted Takeda, a research-based global company with headquarters in Japan, access to its proprietary database of Alzheimer's Disease-related targets and further pursues the validation of selected target candidates for downstream drug discovery programmes. In addition, Evotec OAI and DeveloGen, a German-based disease biology-driven biotech company, formed a joint drug discovery and development partnership in the field of obesity and Type II diabetes. Both collaborations are explained in more detail in the Discovery Programs Division segment report (page 37).

We delivered outstanding results to our customers: more than 20 lead compounds, with three compounds in human clinical trials.

Track record. We have clearly demonstrated an outstanding track record for delivering innovative results and value to our customers. We have delivered more than 20 lead compounds of which 10 have entered pre-clinical development, with three compounds in human clinical trials. In early 2003, we received a milestone payment from Vertex related to the initiation of clinical trials, based on a collaboration which was originated in 1998.

Lee L. Rubin, Ph.D.
Curis Inc.
Senior Vice President, Research and
Chief Scientific Officer

"Our partnership with Evotec OAI has been very productive and has been a valuable component of Curis' drug discovery programmes. We have developed an IND oncology drug candidate within 18 months, contributing to the validation of our biology platform, ultimately resulting in an agreement with Genentech in June 2003."

Andy Boyd, Ph.D.
Evotec OAI Ltd
Department Manager, Discovery Chemistry

Since 1999 Evotec OAI has supported Curis in developing novel small molecule drug candidates involved in the modulation of the hedgehog pathway associated with the development of a variety of cancer types. Activities include hit-to-lead, lead optimisation, ADMET and PK evaluation, process R&D, scale-up and regulatory support. Evotec OAI has worked on various targets for Curis resulting in the discovery and scale-up of several drug candidates including CUR-61414, Curis' leading candidate for the treatment of basal cell carcinoma, the most common form of cancer in the U.S. This was one of the programmes covered by the cancer therapeutic agreement Curis signed with Genentech in 2003.

At Evotec OAI we believe scientific skills and customer service are two sides of the same coin.

Interactions with customers. At Evotec OAI we know that sustainable relationships with our partners require superior scientific performance in addition to excellent customer service skills. Ingredients of our successful partnering include outstanding project management, anticipation of and pro-active behaviour in unforeseen project situations, and the management of our partners' expectations. At Evotec OAI we believe scientific skills and customer service are two sides of the same coin.

Outlook. We are striving towards total customer satisfaction by delivering a value-enhancing solution to an unmet customer need in a both timely and cost-effective manner. In summary, we believe that we have all the necessary ingredients in place to significantly grow our business while maintaining our leadership as the preferred partner for pharma and biotech companies for drug discovery and development.

Management report

Status report 2003

For Evotec OAI, 2003 was a very successful year. We reached our key financial and commercial objectives despite a challenging economic climate and negative currency effects. We grew our top line by 21% in constant currencies and 10% in reported currencies to € 77.2 m and became EBITDA (€ 4.1 m) positive on an annual basis for the first time in our company history.

FDA approvals of NMEs per year:
1999 = 35 NMEs
2000 = 27 NMEs
2001 = 24 NMEs
2002 = 17 NMEs
2003 = 21 NMEs

Industry situation—continued pressure on contract research environment. 2003 was another demanding year for our industry. Many of our customers in the pharmaceutical and biotechnology industry were impacted by margin pressure, increasing generic competition and the need to maintain growth by getting new products to market and therefore changed their R&D priorities. The shortfall of new drugs in their pipelines has also driven these companies to resort to in-licensing more later-stage clinical candidates to speed up new product launches. These trends appear to be shifting resources from discovery into clinical development activities, resulting in cutbacks in pre-clinical R&D work and lower visibility in our Discovery and Development Services business.

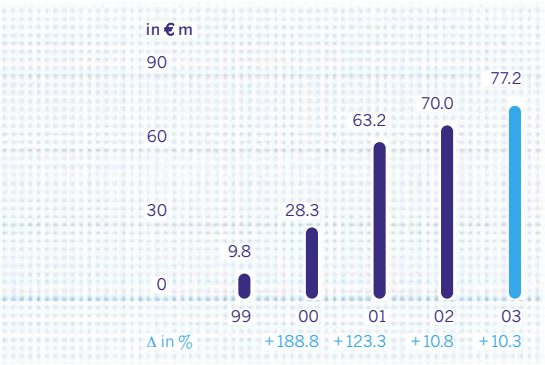
The biotechnology industry as a whole had a strong year with over $ 19.1 billion raised in the venture and equity markets. However, pressure from investors to realise quicker gains and reduce risk has directed most of this new funding to later-stage development programmes, with many companies completely dropping their discovery activities. We believe this trend is temporary as the industry may soon see a serious shortfall in pre-clinical compounds.

We achieved a growth rate of 21% based on constant year-on-year exchange rates—clearly outperforming our top-line guidance for 2003.

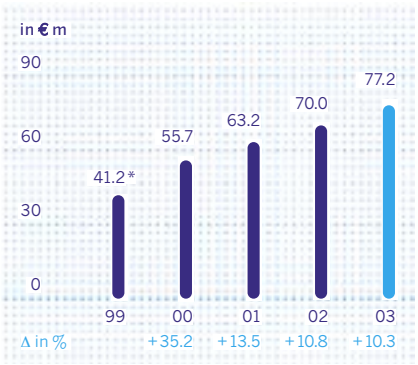
Revenues 2003—delivering on promised growth. Total group revenues increased by 10% to € 77.2 m (2002: € 70.0 m) meeting company guidance. At constant (last year's) exchange rates, revenue growth would have amounted to a very strong 21%. Our growth was supported by the sound performance of our core Discovery and Development Services (DDS) business and sizeable instrument deliveries by Evotec Technologies.

DDS managed to gain market share. The division maintained growth against the industry trend, despite adverse currency trends and cutbacks in pre-clinical R&D expenditures by some of our customers. Our diverse portfolio of capabilities has enabled us to reach total revenues of € 61.2 m, an increase of 4% (2002: € 58.6 m). With top-line growth of 64% to € 18.7 m (2002: € 11.4 m) Tools and Technologies has shown excellent performance. Success was driven by new product launches of the Opera confocal imaging reader as well as an extended collaboration with Pfizer Inc. We also recognised revenues of € 1.5 m in our newly established Discovery Programs Division (DPD) following an agreement between Evotec Neurosciences and Takeda signed in August 2003. With total revenues of € 35.4 m, the U.S. market continues to contribute substantially to our well balanced regional sales mix. Despite the U.S.-Dollar decline the proportion of our U.S. sales to total sales was reduced only slightly to 46% (2002: 47%).

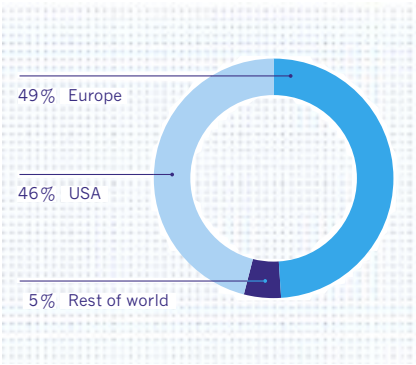
Revenue
Delivering on promises



Pro-forma revenue
Steady organic growth



Revenue by regions
Well balanced regional sales mix



*unaudited

Discovery and Development Services reached positive operating results, before amortisation, due to the effective implementation of cost control measures in 2003. Tools and Technologies was close to break-even.

2003 Operating result—significant progress. The Evotec OAI operating result improved to € (15.8) m (2002: € (135.5) m). No goodwill impairment impacted the operating result in 2003, despite reduced short-term growth in discovery chemistry and the continued under-utilisation of our pilot plant, while the 2002 operating loss was significantly affected by a € 109.4 m impairment charge. Excluding both goodwill and amortisation charges, the operating result still improved significantly with losses declining by 64% to € (5.1) m (2002: € (14.1) m). Discovery and Development Services reached positive operating results in 2003, before taking amortisation charges into account. Tools and Technologies was close to break-even.

Evotec OAI realised a gross margin of 40% (2002: 45%) with total cost of revenues of € 46.2 m (2002: € 38.5 m), an increase of 20% compared to last year. Gross margin performance was adversely effected by the U.S.-Dollar exchange rates as well as a less favourable sales mix in 2003.

We are focusing our research and development efforts more and more on internal drug discovery programmes, and less on traditional technology R&D activities.

R&D expenses amounted to € 15.5 m (2002: € 23.0 m), a planned cost reduction of 33%. As anticipated, tools and technology R&D has been reduced significantly by 35% to € 5.0 m, compared to the same period in 2002 (€ 7.8 m). R&D activities for drug discovery, Evotec OAI's core businesses (DDS, DPD), adding the 50:50 joint venture with DeveloGen (€ 1.4 m shown under non-operating expenses), remained at a comparable level to the previous year (€ 13.9 m, 2002: € 15.2 m). In addition to enhancements of our service platform, these R&D activities are increasingly directed towards internal projects in our Discovery Programs Division.

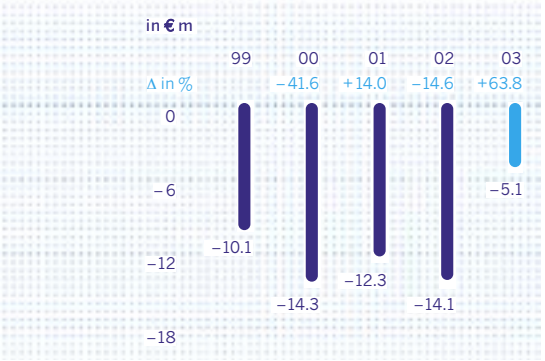
Even with our strong growth we have managed to keep selling, general and administration costs low. SG&A costs were reduced by 12% to € 17.9 m (2002: € 20.5 m), as a result of planned cost containment measures.

Currency effect on key numbers

		2003	2003 constant currencies*
Revenues	€ m	77.2	84.5
Growth over 2002	%	10.3	20.8
Revenues Discovery and Development Services	€ m	61.2	68.3
Growth Discovery and Development Services	%	4.5	16.6
Gross margin	%	40.2	41.7
EBITDA	€ m	4.1	6.6

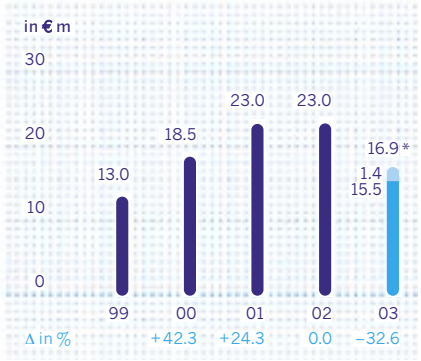
*currency adjustment using exchange rates of 2002

Operating result*
Planned cost reductions resulted in significant improvements



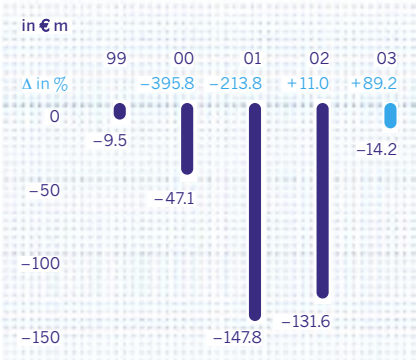
* before amortisation and impairment

R&D expenses
Steady R&D investment in discovery, reductions in technology R&D



* including € 1.4 m DeveloGen joint venture R&D expenses

Net income
Improvement supported by absence of goodwill impairment



We reduced our net loss by 89% as a result of improved operating performance, the absence of goodwill impairment and a negative impact of € 1.4 m from our DeveloGen joint venture.

2003 Net loss—improved by 89%. Net loss for the year amounted to € 14.2 m (2002: € 131.6 m). The sharp decline over 2002 is a result of an improved operating result and the absence of a goodwill impairment charge. Excluding the € 10.7 m amortisation charge, net loss improved to € 3.6 m (2002: € 10.2 m). R&D costs associated with our 50:50 DeveloGen joint venture, classified as "net loss from equity investments", have impacted the net loss by € 1.4 m. Our currency hedging policy contributed € 0.5 m to our non-operating income|loss. Evotec OAI realised total net tax benefits of € 2.8 m that included: current tax worldwide (€ 0.4 m) and deferred tax benefits (€ 3.1 m), mainly resulting from merger related amortisation.
The total net loss per share for Evotec OAI was € 0.40 (2002: € 3.71). The weighted average number of shares used in calculating basic earnings per share (EPS) increased by just 845 to 35,510,130 on 31 December 2003. The number of shares remained unchanged since 31 December 2002.

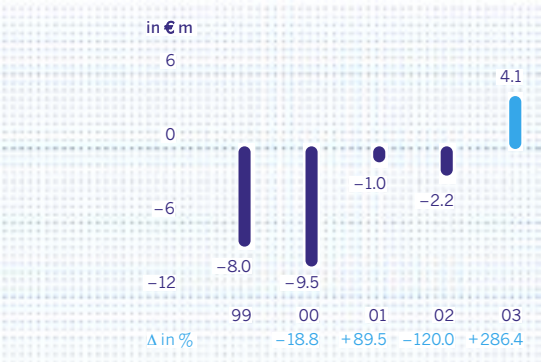
2003 EBITDA—positive for the first time in company history. The significant improvement in operating results combined with rigorous cost management translated into a positive € 4.1 m (2002: € (2.2) m) earnings before interest, tax, depreciation (including allowances) and amortisation (EBITDA), for the first time in our company history.

EBITDA calculation

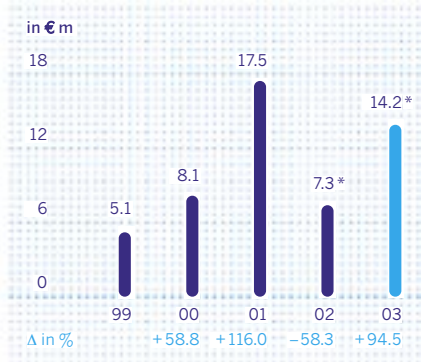
T€	2003	2002
Net income	(14,242)	(131,600)
– Interest income	540	700
+ Interest expense	714	300
– Tax benefits	2,825	2,700
+ Amortisation	10,671	12,000
+ Impairment	–	109,400
+ Depreciation and allowances	10,308	11,100
= EBITDA	4,086	(2,200)

2003 Cash flow—positive operating cash flow. Also for the first time, the group reached a positive cash flow, provided by operating activities, totalling € 7.8 m (2002: (1.0) m).

EBITDA
Positive for the first time in company history



Capital expenditures
Significant investment in new labs on top of regular capex



* excluding capital leases

We invested € 15.6 m into facilities and equipment for future growth. In 2004, capital expenditures will come back to regular levels. As of 31 December our liquidity amounted to € 19.5 m.

During the year we invested in new laboratory facilities in Oxford, laying the ground for growing drug discovery operations. Excluding these large investments, capital expenditure remained at average on prior year's level. In 2003, investments in tangible and intangible assets totalled € 15.6 m which were partially financed through a mixture of bank loans with different maturities. As a result bank loans increased by € 5.4 m to € 14.7 m. Financing activities in 2003 provided a total of € 7.2 m of cash, including Pfizer's equity investment in Evotec Technologies.
As of 31 December 2003, cash, cash equivalents and marketable securities totalled € 19.5 m (2002: € 21.3 m), giving us a solid starting point for 2004.

Condensed cash flow statement

T€	2003	2002
Net cash (used in) provided by operating activities	7,812	(970)
Net cash (used in) provided by investing activities	(16,371)	2,172
Net cash provided by financing activities	7,226	4,111
Net increase | decrease in cash and cash equivalents	**(1,333)**	**5,313**
Exchange rate difference	(1,212)	(2,656)
Cash and cash equivalents at beginning of year	21,308	18,651
Cash and cash equivalents at end of year	18,763	21,308
Cash and cash equivalents including marketable securities	19,471	21,308

2003 Balance sheet—solid asset and capital structure. As required by U.S. GAAP accounting, we conducted an extensive review on our intangibles in 2003. These reviews concluded, that no impairment charge was necessary in 2003, and therefore intangible assets only reduced by regular amortisation. Due to currency translation, our fixed tangible assets remained on last year's level despite higher continued investments in our anticipated growth compared with related depreciation.
Despite the growth related increase of inventories (+ 22 %, € 10.2 m) the group's working capital declined by 70 % to € 1.0 m due to reduced accounts receivables (– 24 %, € 7.7 m) and increased current liabilities (+ 5 %, € 22.5 m). Other non-current liabilities primarily include deferred tax liabilities of € 11.3 m (2002: € 15.5 m) as well as long-term bank loans and capital lease obligations of € 12.5 m (2002: € 7.9 m) mainly used for asset financing.

Total assets decreased by € 20.1 m to € 220.9 m (2002: € 241.0 m). No employee stock options were exercised and no share issuances occurred in the AG, resulting in an unchanged share capital of € 35,510,130.00. Our traditionally high equity ratio was 78% for 2003 (2002: 81%) emphasising our strong balance sheet.

Condensed balance sheet

T€	2003	2002
Cash, cash equivalents and securities	19,471	21,308
Inventories	10,225	8,408
Other current assets	13,296	16,316
Property, plant and equipment	62,051	61,951
Intangible assets	115,149	132,452
Other non-current assets	727	607
Total assets	**220,919**	**241,042**
Accruals	7,794	5,552
Other current liabilities	14,736	15,908
Long-term liabilities and minority interest	14,959	8,631
Deferred tax liabilities	11,329	15,544
Total stockholders' equity	172,101	195,407
Total liabilities and stockholders' equity	**220,919**	**241,042**

Our partner Pfizer has become an equity partner in Evotec Technologies and we are gearing up Evotec Neurosciences for a private financing.

Legal structure. In July 2003 we implemented the agreed capital increase of Evotec Technologies GmbH (ET) by Pfizer Inc., giving them a 10% stake in the company. ET also established a U.S. subsidiary for its U.S. sales and services activities in July.
In August, Evotec OAI entered into a joint drug discovery programme with DeveloGen, where both parties own 50% of the rights and responsibilities. The joint venture is not an incorporated legal entity at this time.
In December, we prepared Evotec Neurosciences (ENS) for a capital infusion through a venture capital financing. The restructuring included:
(i) selling 3% shares to Management and converting 2002 shareholder loans into equity (effectively keeping Evotec OAI's holding almost constant)
(ii) establishing ENS Holdings Inc. in the U.S., and
(iii) exchanging the shares in ENS against those in ENS Holdings. We believe that by effectively transferring the ENS corporate structure to the USA, we will be able to take advantage of the better financing environment there.

Production and procurement—very high value added. Evotec OAI's Discovery and Development Services business largely consists of contract research with a high percentage of costs going towards personnel and a respectively lower portion of costs going towards material usage. Only in our Tools and Technologies business do we have a lower value-added role, as all of the production activities beyond the prototype stage being outsourced to strategic suppliers. Overall, we are continuing the Company's policy to reduce the number of suppliers with emphasis on long-term partnerships. As part of the cost reduction measures last year, we successfully improved our procurement and long-term partnerships throughout the group.

Occupational safety and environmental protection—strong emphasis. We believe that we have an obligation to exceed statutory requirements in protecting our employees and the environment. Thanks to the continued commitment of our employees, our safety performance and environmentally sound working practices improve year-on-year. We are also committed to ensuring that we work in partnership with local communities and regulatory authorities.

Thanks to the continued commitment of our employees, 2003 was another successful year in terms of safe and environmentally sound working practices throughout Evotec OAI and its divisions.

At Abingdon, we increased management training in safety and risk assessment through e.g. a new company intranet, poster campaigns, laboratory "Toolbox Talks" and successfully implemented our annual Health and Safety plan, including increased monitoring and auditing of safety. We also invested heavily in efficient plant and controls in our new chemistry and biology facilities on the Abingdon site, reducing energy consumption by over 50% in some locations. We commissioned an Action Energy Survey and implemented many of the recommendations within six months. We also identified areas for improvement in waste generation by participating in a national survey by the Environment Agency. As a result, we introduced several schemes to reduce waste and increase recycling for items such as paper and glass containers.
In Hamburg, we continue to train our management and staff in environmental safety and to improve waste disposal. Looking for alternative waste disposal solutions, we have changed to a reusable waste disposal system. We have also improved and standardised operating procedures for facility management and adapted facility records to GLP standards. In addition, we have implemented occupational medicine programmes that ensure that employees working with biological materials are appropriately immunised.

We are confident that our internal control and risk management systems operate at an appropriate level for our business.

Risk management—comprehensive and reliable. We put high emphasis on risk management as an ongoing management task within the Evotec OAI Group. This also applies within Corporate Governance (see "Evotec OAI shares and Corporate Governance", page 51), where we continue to strive for maximum meaningful compliance with publicly established standards and codes of practice.
We are continuously reviewing our overall risk management system including regular commercial and R&D project reviews. We perform monthly financial reviews with a strong emphasis on cash and key performance drivers such as revenues, order book status and gross margins. Strict application of investment approval processes, legal contract review procedures, signing authorities, and currency management are also standardised operating procedures. Moreover, we continue to emphasise our IT security throughout the Group and review our insurance coverage regularly. In summary, we believe that our current internal control and risk management systems operate at an appropriate level for our business.

Given our quality reputation and multiple business offerings, we feel well prepared to face the current market challenges and positioned to expand our market share.

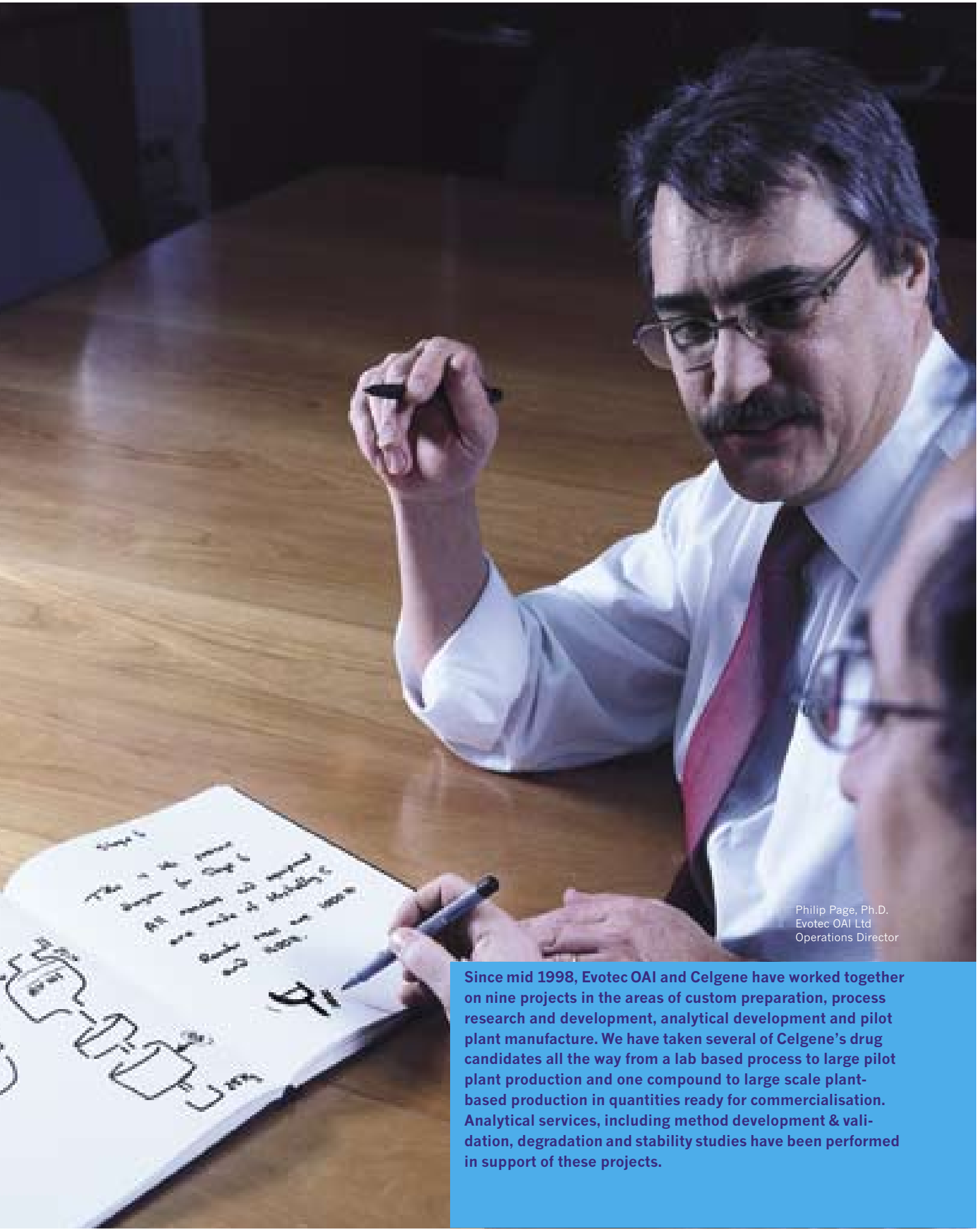
Business risks and future development—importance of market recovery and exchange rates.

> Our revenues depend to a large extent on out-sourced research and development projects by pharmaceutical and biotechnology customers. In the last two years the weak world-wide capital markets, as well as the general economic pressures in our industry, have in a number of cases altered the balance of R&D spending by our customers with an increased emphasis on later stage development programmes. Decreased discovery expenditures put pressure on our short-term growth expectations for our Discovery and Development Services business. We believe this shift in R&D expenditure to be temporary but while it remains there is an inevitable threat to growth and profitability.

> The business of Evotec Technologies (ET) is dependent upon significant capital expenditure by our customers. These capital expenditure budgets were generally reduced in 2002 and 2003 but there are some signs of recovery in instrument spending. Also, ET has been creative in constantly seeking innovative new products to provide solutions to research bottlenecks. Nevertheless, margin pressure and ongoing industry consolidation in the tools market could threaten ET's growth and profitability.

Andy Zeitlin
Celgene Corporation
Director, Pharmaceutical Development

"Evotec OAI's excellent understanding of process chemistry has made them our partner of choice for over 5 years. Their attention to quality and detail in combination with their seamless and straight communication have allowed us to work as a team in tackling some very challenging drug manufacturing and scale-up projects on time and to budget. They have a clear understanding of our projects and the technical, quality and regulatory processes needed to bring innovative pharmaceuticals to patients."



Philip Page, Ph.D.
Evotec OAI Ltd
Operations Director

Since mid 1998, Evotec OAI and Celgene have worked together on nine projects in the areas of custom preparation, process research and development, analytical development and pilot plant manufacture. We have taken several of Celgene's drug candidates all the way from a lab based process to large pilot plant production and one compound to large scale plant-based production in quantities ready for commercialisation. Analytical services, including method development & validation, degradation and stability studies have been performed in support of these projects.

> In our Discovery Programs Division we engage in selected discovery activities carrying some of the risk of these programmes ourselves. In this business, we are exposed to project attrition rates customary in the drug discovery industry. Even if we identify promising targets and compounds, it will take time before we could sell or license any drug candidates, if at all. Hence, expenditure on internal discovery programmes or related acquisitions of technologies or intellectual property could substantially reduce our short-term profitability. We intend to reduce part of the business risk through early partnering agreements.

We are also affected by usual business risks such as the general dependence on large pharmaceutical customers, the financing of investments and in particular foreign exchange rate fluctuations which we explain in more detail in the notes to the financial statements (No. 17). Despite our foreign exchange hedging, a continued strong weakening of the U.S.-Dollar, if not accompanied by a sizeable weakening of the GB Pound, constitutes a significant risk to our financial situation.

Overall, our success depends on our ability to retain our highly skilled staff and to adapt to changing technologies and market environments as well as customer expectations. If we fail to adapt to market needs, our ability to grow profitably could seriously suffer.

In summary, we expect to be able to create value and further strengthen our role in the industry. With positive operating cash flows from our Discovery and Development Services and Evotec Technologies businesses, firm cost man-

agement and flexibility in managing R&D spending, we feel well prepared to face the current market challenges. Given the high quality international reputation we have built in the individual areas of our offering, we are well positioned to deliver on our business plan.

Post-balance sheet events. Evotec Neurosciences anticipates to raise venture capital from leading investors in the biotech field in the first half of the year 2004. This financing is designed to allow ENS to broaden its pipeline of clinical and pre-clinical compounds prior to further pharma partnering.

Outlook

We plan for 2004 to become a year of good operational performance, EBITDA profitability in our two established divisions and advancements in our proprietary drug discovery programmes.

Sales—first signs of recovery. Based on industry trends, it seems that the market weakness caused by soft financing markets for biotechnology companies and budget cuts by pharmaceutical companies has bottomed out at the end of 2003. There are now signs of a recovery, particularly in the U.S. and Japan, with Europe following at some distance. Given the usual time lag between funding events and orders being placed, and the higher average exchange rate of the Euro against the Dollar in the first half of 2004 compared to the same period in 2003, we expect to see more significant revenue growth in the second half of 2004. For the full year, even at recent exchange rates, we expect to exceed 2003 revenues. Individual quarters could deviate from last year's performance as sizeable instrument deliveries to Pfizer boosted performance in the first and third quarters of 2003. As of the end of January, the order book for 2004 totalled approximately € 40 m.
With our diverse and sophisticated offerings, we are among the strongest brands in the industry and are therefore well positioned to benefit from an upswing in the contract research and outsourcing market. Based on our current order situation, ongoing negotiations with customers and a continuous expansion of our Discovery Programs Division we are optimistic about 2004 and expect to deliver good operational performance.

Results—EBITDA planned to remain positive. Assuming positive cash flows provided by operating activities in our Discovery and Development Services and our Tools and Technologies segments to be sufficient to fund our Discovery Programs Division, we plan for a continued positive EBITDA on a group level.

Capital investments—back to previous levels. Investments in 2003 were mainly characterised by the build up of capacity in Abingdon. Our 2004 capital expenditures will focus on technology updates for our services business. The level of investment is planned to be approximately the same as in 2002 (€ 8.7 m).

Ownership structure of subsidiaries. Pfizer Inc plans to slightly increase its holding in Evotec Technologies following a milestone achievement specified in the contract signed in October 2002. Our relative shareholdings in Evotec Neurosciences will decrease as tranches from venture capital financing are paid out.

Dividends. The payment of dividends in the future is dependent on our performance, our financial situation and liquidity requirements, the general market conditions, and statutory, tax and regulatory requirements. We currently intend to retain any profits generated from the development of our business and to use them to create further development and growth for our company. We do not expect Evotec OAI AG to have positive net income in 2004.

Segment report | Discovery and Development Services (DDS)

During 2003 DDS has expanded its offerings of research and development solutions, elevating our status as the partner of choice in the industry. The division has shown steady growth and achieved a positive operating result, before amortisation. DDS is well positioned for continued expansion in 2004.

Integration and evolution. Our DDS division provides unmatched capabilities in assay development, drug screening and chemistry to most of the top pharmaceutical and biotechnology companies. We strive to anticipate and respond to customer demands and stay at the forefront of scientific and technological advances.

Our biology and chemistry offerings within DDS work seamlessly together, providing fully-integrated solutions to a growing list of customers, such as Elixir Pharmaceuticals and Toray. The services of DDS also provide significant capabilities to our growing Discovery Programs Division including our joint programmes with Evotec Neurosciences and our new partner DeveloGen.

Our portfolio of services continues to evolve to offer the most optimised and targeted service and product offering to our customers' state-of-the-art drug discovery and development. We have expanded the capabilities of our DDS division including the enhancement of our ADMET capability, the acquisition of X-ray crystallography expertise (for lead optimisation and structure-based drug design) and the further development of our proprietary EVOseek knowledge management system. To increase the capabilities of our virtual screening and other computational chemistry activities we have installed a new, more powerful distributed computing grid that is regularly utilised within our customer projects.

We have seen outstanding growth in our assay development and screening services, and we were time and again selected as the medicinal chemistry partner of choice by our biotechnology and pharmaceutical customers.

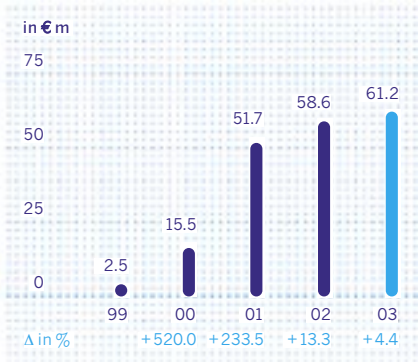
Comprehensive solutions. The comprehensiveness of our offering has allowed us to swiftly react to the changing needs of our customers during the year. We have witnessed a shift in investment from early stage research to later stage development as large pharma and biotech companies are facing pressure to show short-term progress in their new product programmes. As Evotec OAI has leading services for both the early stage research areas as well as later stage development stages, we were able to seamlessly serve as a partner to our customers within this phase of changing needs.

Despite this trend our Discovery Biology services have seen outstanding growth this year due primarily to recognition of our assay development skills. Several assay development and screening projects have been conducted for major pharma customers including Novartis.

For our Discovery Chemistry services we have increased the breadth of medicinal chemistry expertise through the acquisition of staff from British Biotech during its recent M&A activity, as well as other direct recruitments. We are time and again selected as the medicinal chemistry partner of choice for large pharma and biotech customers because of our proven strength in this area and are particularly pleased to have added Roche as a customer in this field in 2003.

In Development Chemistry the recent market changes towards later-stage development have been reflected in the recovery and steady growth in both

Revenue Discovery and Development Services
Continued growth in core business despite strong Euro



laboratory based projects and pilot plant work. This includes repeat business, contract extensions and several new customers. Our affiliate ProPharma, which provides formulation development and sterile manufacture of liquid and lyophilised clinical trial batches, demonstrated strong growth through 2003. Growth was particularly strong in clinical trials supplies manufacturing with many customers using our formulation services for the first time.

Our customers value our speed, quality of work, collaborative approach and responsiveness to expected or unexpected scientific developments.

Responsiveness and growth. In all our many and varied customer projects we emphasise the need for a collaborative approach. This makes us more responsive to expected or unexpected scientific developments within projects as well as changes within our customer's programmes and strategies during a project's term. Our existing customers value this responsiveness as well as our speed and quality of work, providing us with a high level of extended and repeat business.
We also provide the same high level of service to our new customers. The implementation of an innovative umbrella contract concept for the portfolio companies of specific venture capital firms has shown considerable success. Our umbrella concept with Oxford Bioscience Partners (OBP) alone has resulted in projects with seven OBP companies this year (Artesian, Cantata, Dynogen, Elixir, Enanta, Psychiatric Genomics and Rib-X). This is a good example of a synergistic partnership benefiting both Venture Capitalists and biotech companies as well as generating significant business for Evotec OAI. Other new customers this year include Axxima, Chroma, Oxagen and Novartis.

Financials. In 2003, total revenues in our DDS division amounted to € 61.2 m, up 4% over the previous year (2002: € 58.6 m). In local currencies, growth was even higher at 17%. Gross margin was approximately at last year's level (39%, 2002: 41%) despite the adverse impact of currency exchange rates. R&D

Condensed key figures Discovery and Development Services

		2003	2002	Δ 03|02 in %
Revenue	T€	61,214	58,588	4.5
– Thereof 3rd party	T€	58,582	58,588	0.0
Gross margin	%	39.1	40.7	–
Operating result	T€	(10,422)	(133,373)	92.2
Operating result adjusted for				
non-cash amortisation and impairment	T€	9	(12,426)	–
R&D expenses	T€	8,112	15,213	(46.7)
Depreciation and allowances	T€	9,319	10,558	(11.7)
Number of employees as of 31 December				
without corporate overhead		440	458	(3.9)

Jeff Naroian
Evotec OAI Inc
Vice President, Business Development North America

Elixir Pharmaceuticals was the first customer under Evotec OAI's innovative alliance with the VC firm Oxford Bioscience Partners (OBP). Elixir has decided to concentrate on their core disease expertise and, in drug discovery, continued to capitalise on our comprehensive, high-quality expertise to identify novel drug-like compounds for key targets that may some day change the way of treating the diseases of aging. In the first uHTS screen run by Evotec OAI, Elixir was able to identify potent and drug-like hit structures that have been progressed by Evotec OAI into medicinal chemistry programmes to optimise their potency, selectivity and pharmacokinetic profile.

Peter S. DiStefano. Ph.D.
Elixir Pharmaceuticals, Inc.
Vice President Research & Development
and Chief Scientific Officer

"Evotec OAI is much more than an outsourcing partner to us. Their understanding of drug discovery, biology processes and experienced consultancy complement our biology and understanding of the genetics of aging. In just over a year they have delivered a number of validated lead series and we firmly believe that the partnership has saved us overall two years in our development."

expenses declined when compared with 2002 (€ 8.1 m; 2002: € 15.2 m), largely due to R&D efforts directed towards our discovery programmes being shown for the first time within the separate division. In the previous year these R&D costs were part of DDS. The same applies to SG&A costs. These amounted to € 13.1 m (2002: € 18.9 m), reflecting careful spending throughout the year. The operating result before amortisation for the division was positive for the first time in the company's history with € 0.01 m (2002: € (12.4) m).

Our Discovery and Development Services division will grow operationally from increased demand from our Discovery Programs Division. Third-party revenues could be flat as a result of currency effects.

Outlook. Because of the current down-cycle in early drug discovery outsourcing, we are expecting a modest recovery in the contract research market not before the second half of 2004. This, in combination with a continued erosion of the U.S. Dollar, could result in flat third party revenue growth prospects for the year. However, we do plan to grow DDS operationally with increased demand from our Discovery Programmes Division developing candidate products in CNS and Metabolic Diseases, creating significant longer-term value to Evotec OAI.
To support our operational growth we have invested in the expansion of our facilities where needed. Our major investment in 2003 has been the fit-out of a new integrated discovery building in Abingdon, UK. Phased occupation commenced in December 2003 and the building, once fully fitted out, has capacity for up to 200 biology and chemistry scientists. This will not only provide increased capacity, but also enrich the knowledge base that Evotec OAI brings to each of its projects, customers and partnerships.

Segment report | Discovery Programs Division (DPD)

We are well underway in our quest to develop an internal portfolio of drug compounds for distinct disease indications by uniting our screening and chemistry skills with biology companies that understand the molecular causes of diseases. In 2003, we entered into our first 50:50 partnership with a disease-driven biotech company, DeveloGen. The pharma industry is in urgent need of novel drug candidates which we intend to provide through out-licensing from our Discovery Programs Division.

Evotec OAI is ideally set up to leverage its customer base and capabilities into true collaborative, multi target | compound based productivity partnerships that will generate multiple, high-value licensing opportunities.

Our Discovery Programs Division was established in 2003 to develop proprietary drug candidates to fill the clinical pipelines of pharma companies. Based on a thorough analysis of current and future market needs and on existing customer feedback, Evotec OAI has prepared for demand in this segment. We are convinced that the trend of early compound in-licensing will be further pursued and expanded by the pharma industry to enhance their productivity. Evotec OAI is ideally set up to leverage its customer base and capabilities into true collaborative, multi target | compound based partnerships that will generate multiple, high-value licensing opportunities.

The value of assuming higher R&D risk has been demonstrated this year through our € 20 m CNS deal with Takeda. We have now taken the next step to increase our indication specific visibility in Metabolic Diseases.

Investment highly rewarded at Evotec Neurosciences Central Nervous System (CNS) drug discovery. The value of assuming the higher risk associated with research on distinct target-disease relations has already been demonstrated this year through our affiliate Evotec Neurosciences (ENS). The € 20 m deal with Takeda, signed in August 2003 in the field of Alzheimer's Disease, highlights the rewards inherent in this kind of work. Throughout the year ENS has expanded its proprietary database on new and validated targets for Alzheimer's Disease and moved into assay development, screening and early chemistry with targets which undoubtedly are involved in neurodegenerative diseases and which ENS could put into a proprietary format for screening or compound testing. In December, ENS also in-licensed a group of late pre-clinical NMDA receptor subtype selective antagonists from Roche to be developed for CNS disorders including Alzheimer's Disease, neuropathic pain and Parkinson's Disease. ENS is on the way to becoming a strong player in the CNS field by aggressively establishing a balanced compound portfolio.

Broad venture established in Metabolic Diseases. We have now taken the next step to increase our indication specific capabilities: in September 2003 we combined our powerful discovery platform with the assets and capabilities of a leading Metabolic Diseases-driven biotech company, DeveloGen. The goal is to produce proprietary drug candidates (between Lead and Phase IIa stage) in the field of Diabetes and Obesity which in turn will be licensed out to the pharmaceutical industry to enhance the productivity of their respective pipelines. The risks and rewards are shared equally with our biotech partner, creating the critical mass to produce a number of different drug candidates over the years that will attract pharmaceutical partners.

The diabetes and obesity markets are very large, already comprising $ 12 billion of sales of pharmaceuticals (2002) and expanding rapidly. Market development, medical need and DeveloGen's proprietary approach to target identification and validation has convinced us to pool our efforts in this collaboration.

Our Discovery Programs Division has become a large contract customer for our services division with multiple programmes being run for our Metabolic Diseases joint venture and Evotec Neurosciences.

DPD as a customer of Discovery and Development Services (DDS). The Metabolic Diseases collaboration already has four programmes running within our DDS division, including novel targets as well as novel chemistries to existing targets. Some 40 scientists, half from Evotec OAI and half from DeveloGen, are pursuing these programmes through assay development, screening and lead optimisation. All collaborations in DPD are steered by a management separate from the DDS division to prevent any possible conflicts with customer work. In fact, ENS and the venture with DeveloGen are contract-based customers of DDS and receive the same professional treatment and attention as all our customers. This enables us to clearly separate our DPD activities and at the same time leverage the strength of the critical mass we have built in DDS.

First revenues. ENS has generated first revenues in DPD amounting to € 1.5 m. ENS related R&D expenses amounted to € 3.1 m and other DPD specific R&D expenses to € 1.2 m. Our pro rata R&D investment in the 50:50 joint venture with DeveloGen resulted in additional cost of € 1.4 m which are not allocated to the DPD division but shown in the group's non-operating result under "Net loss from equity investments" as a consequence of the "at equity" consolidation. We will initially fund our Metabolic Diseases venture internally from the operating cash flows of our DDS and Tools and Technologies units and will search for a partner as early as feasible to support this research. Our plan is to continue funding ENS through venture capital equity from 2004 onwards which based on the venture capital community's current interest in ENS seems highly plausible.

We intend to license out by the end of Phase IIa at the latest. We expect rewarding milestones and royalties once compounds are handed over to pharmaceutical partners.

Expanding productivity through in-licensing. We intend to complement our drug candidate portfolio with pre-clinical in-licensing opportunities in order to arrive at a balanced portfolio which will continuously enrich the clinical pipeline of our future pharma partner over several years. We have no intentions to pursue fully fledged clinical programmes ourselves, but rather license out our proprietary drug candidates for late-stage clinical development at the latest at the stage of proof-of-concept-drug (Phase IIa), preferably earlier. In return, we expect to be rewarded by attractive milestone and royalty payments.

Future expansion. Depending on the success and the speed of progression with this new model we are set up to replicate this principle in other indication areas. Our DPD programme provides real opportunities to create value to the Evotec OAI group, its employees and our shareholders, but will be carefully balanced with the financial performance of the overall Company.

Condensed key figures Discovery Programs Division

		2003
Revenue	T€	1,479
– Thereof 3rd party	T€	1,464
Gross margin	%	55.7
Operating result	T€	(5,356)
Operating result adjusted for non-cash amortisation and impairment	T€	(5,301)
R&D expenses*	T€	4,324
Depreciation	T€	425
Number of employees as of 31 December without corporate overhead		28

* excluding € 1.4 m DeveloGen joint venture R&D expenses

Segment report | Tools and Technologies

Evotec Technologies (ET), Evotec OAI's instrumentation business for drug discovery, achieved a strong performance in 2003. In the first full year as a stand alone company ET delivered an outstanding 64% sales growth.

ET has established itself within the industry as a proven and reliable partner, offering high-end products for critical life sciences applications, providing solutions to scientific workflow bottlenecks.

ET little affected by weak market environment. Driven by pharma and biotech companies scaling back their R&D budgets, most of the market for life science equipment continued to be weak. Evotec Technologies, however, reported strong growth as the company offers high-end products for critical life science applications and solutions to scientific or workflow bottlenecks. ET has established itself within the industry as a proven and reliable partner through innovation, automation and integrated solutions backed by highly specialised customer support teams that work in close relationship with its partners.

Strong product line. Evotec Technologies' solutions cover the whole range from high-throughput screening (HTS) to systems biology with a current emphasis on cell handling and analysis. **Opera**, ET's platform for automated high speed | high content imaging of cells combines the resolution of high performance confocal microscopes with the convenience of microplate readers and the speed necessary for HTS. Opera contributed significantly to sales growth in 2003 with six completed installations, and is one of our key products for future sales growth.

Elektra and Opera provide innovative solutions for cell handling and analysis and are key products for current and future sales growth.

Our **CellProcessor technology**, a platform for gentle, contact-free handling of single cells in micro-devices, permits individual cells to be examined in detail, to be treated or tested and to be recovered alive. In response to the urgent need to accelerate the process of cellular research, ET has launched the automated bench-top device **Elektra** in 2003. First orders have been placed and a distribution agreement has been signed to quickly access the Japanese market. In addition, feasibility studies are underway to adapt our technology for automated cell cloning, a very large and rapidly growing market.

EVOscreen® Mark III, ET's proven and now well established solution for miniaturised ultra high-throughput-screening (uHTS) has been installed at Pfizer in the UK and the U.S. with customer acceptance being achieved ahead of schedule. With the end of our exclusive agreement with Novartis, Pfizer and GlaxoSmithKline getting close, ET has started marketing EVOscreen® outside of the original consortium.

For bench-top instrumentation for FCS single molecule detection, ET continued its co-operation with Olympus, where ET is participating in the sales of each Olympus microplate MF reader. ET has extended this product line with the new **Clarina II** workstation, a fully automated device for assay development, screening applications and compound profiling in a medium-throughput format, and fully compatible with its larger brother EVOscreen®. Clarina II was launched in the U.S. in September and five systems have been already installed in customer labs.

Lars Oelerich
Evotec Technologies GmbH
Technology Support Engineer

Since 1996, GlaxoSmithKline (GSK) has co-actively participated in the development of the EVOscreen® platform as one of the partners of the consortium that Evotec OAI established with pharmaceutical companies. Mark III was installed and initiated operations in the HTS site of GSK at Tres Cantos, Spain in February 2002. Today Mark III is used at GSK in the screening of a broad range of target classes and has proven to be a reliable, efficient and competitive platform for uHTS which encompasses the advantages of miniaturisation and high quality data.

Julio Martin
GlaxoSmithKline plc
Manager, Molecular Screening

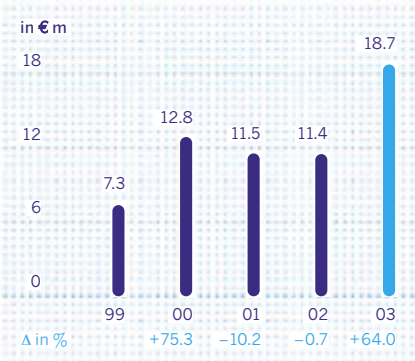
"EVOscreen® Mark III has become a key platform for miniaturised screening in the low-microlitre range at GSK. Evotec's engineers have worked closely with our scientists to build Mark III, incorporating single molecule detection and FCS⁺plus analysis into an uHTS set-up. The features of this platform in terms of sensitivity and multidimensional read-out provide us with highly informative data, in-well quality control and flagging of false signals."

All these instruments are supported by proprietary **software** for data management and analysis, ready-to-use reagent sets for bio assays as well as an extended portfolio of proprietary **consumables** such as NanoCarriers™, microplates, chips, kits, reagents and spare parts, all supporting flexible and easy application of our technology.

Drug discovery continues to be the largest customer segment for Evotec Technologies.

Staying close to our customers. Drug discovery continues to be the largest customer segment for Evotec Technologies due to Evotec OAI's history and longstanding relationships with key accounts from the pharmaceutical industry. In the context of the extended collaboration with ET signed in October 2002, Pfizer made an equity investment in ET in July 2003, with Pfizer becoming a 10% shareholder in the company.
In 2003, ET finalised service and maintenance contracts for most of the installed instrument base with its customers. We also established technology partnerships and joint development programmes which are leading to real innovations in R&D: joint fast prototyping, direct sales of customised research platforms, pre-series products as well as instrument oriented research cooperations.

Revenue Tools and Technologies
Strong growth supported by sizeable instrument deliveries to Pfizer



Delivered on all financial goals. Evotec Technologies has achieved outstanding growth in 2003. Sales increased by 64% to € 18.7 m (2002: € 11.4 m) with contributions from all product lines, on top of the strong impact from the extended Pfizer collaboration. Third party revenues amounted to € 17.2 m. In 2003, ET increased the relative share of total sales in the U.S. from 14% to 47% (Europe: 45%, Japan 8%). R&D expenses were reduced by 35% to a sustainable level of € 5.0 m (2002: € 7.8 m) as result of modular R&D approaches and customer funded R&D projects. Revenue growth in concert with an improved cost base has laid the grounds for Evotec Technologies GmbH achieving positive operating results before amortisation. Including allocation of corporate overheads, the segment came close to break-even (€ (0.2) m; 2002: € (1.7) m).

Looking forward we anticipate an increasing demand for automated cell-based analysis. To fully capture this potential we plan to expand our marketing and sales efforts in this area.

Good prospects for 2004. Success and productivity in the drug discovery industry will continue to be driven by increased efficiency in the research process and evolution towards more automated, integrated, high-throughput, miniaturised and | or parallel approaches. In addition, we anticipate an increasing demand in particular for automated cell-based analysis. Thus, with our new product line and established strong brand recognition we are well positioned to benefit from these trends and expect continued growth for 2004.
To capture this potential Evotec Technologies plans to increase marketing, sales and demo activities and to establish and strengthen its U.S. site at the heart of our customer base on the east coast.

Condensed key figures Tools and Technologies

		2003	2002	Δ 03 | 02 in %
Revenue	T€	18,668	11,407	63.7
– Thereof 3rd party	T€	17,197	11,407	50.7
Gross margin	%	43.7	67.0	–
Operating result	T€	(1,140)	(2,139)	46.7
Operating result adjusted for				
non-cash amortisation and impairment	T€	(161)	(1,678)	90.4
R&D expenses	T€	5,043	7,799	(35.3)
Depreciation and allowances	T€	1,030	547	88.3
Number of employees as of 31 December				
without corporate overhead		84	88	(4.5)

R&D report

The technology and knowledge curve in the drug discovery industry moves extremely quickly. Evotec OAI's R&D activities pave the way towards superior knowledge-driven drug discovery processes, supporting both our proprietary and partnered programmes.

R&D activities have focused on the extension of our portfolio of discovery products and services and the further development of decision support tools.

Success in drug discovery and development is critically dependent upon operational excellence and effective decision making. This process requires experimental results of the highest quality coupled with the most efficient technological solutions. Outside the Discovery Programs Division, R&D activities in 2003 have focused on the extension of Evotec OAI's portfolio of products and services and the further development of decision support tools that aid our scientists to successfully meet the objectives of our clients.

New ADMET assays handed over to operations. ADMET profiling is being used earlier and earlier in the drug discovery cycle within the pharmaceutical industry because of the well documented failure of clinical candidates due to inappropriate pharmacokinetics and toxicity. In 2003, we transferred new ADMET assays developed by R&D to Discovery and Development Services' routine operations, for the early measurement of absorption-related properties, solubility, metabolism, protein binding and cellular toxicity. We can now profile 'hit' compounds in these assays to identify inherent ADMET liabilities before medicinal chemistry optimisation.

We continue to develop our virtual screening capabilities to complement EVOscreen® and have built a database of over 5.5 million compound entries.

Integration of random and rational discovery progressed. We strongly believe that successful modern drug discovery is directly related to the effective integration of random and rational approaches. Thus we continue to develop our capabilities in virtual screening to complement EVOscreen®. The results of protein-ligand docking virtual screens conducted at Evotec OAI in 2003 have proved very exciting, providing new starting points for medicinal chemistry programmes. We have built a database of over 5.5 million entries containing screening compounds from over 40 suppliers which is updated on a regular basis. We use this database in virtual screening as a source of compounds for docking together with virtual libraries of compounds readily accessible by chemistry proven at Evotec OAI. After applying the same series of drug likeness filters that we use when selecting compounds for our uHTS screening library, we dock the compounds into the protein binding site. In 2003, we upgraded both our Linux cluster and distributed computing grid technology to add computing power to this virtual docking process. The final selection of compounds by our virtual screening process is dependent on the scores from up to eight scoring algorithms including one developed in-house.

Our new X-ray crystallography team enables us to offer high-quality X-ray structure determination of target proteins necessary to conduct virtual screening.

X-ray crystallography group added. Virtual docking based screening requires good quality structural data of the biological target of interest. Many of our clients are collaborating with us on novel proprietary targets for which the structure is not known. At the end of 2003 we initiated the establishment of an X-ray crystallography team by recruiting experienced personnel and purchasing X-ray equipment. This enables Evotec OAI to offer X-ray structure determination both for support of virtual screening and for iterative structure based design activities including target-lead co-crystallisation.

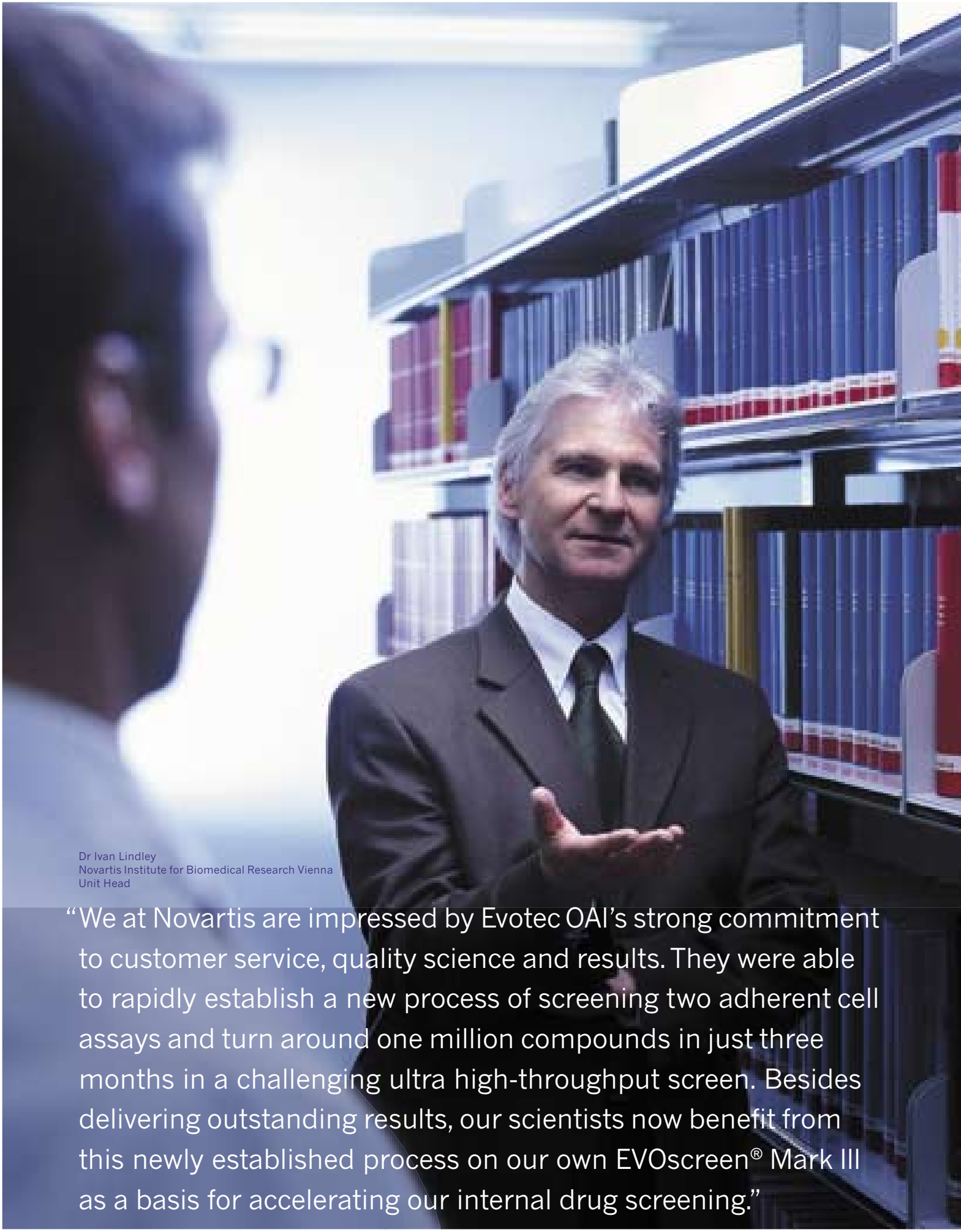
Informatics tools provide quick decisions. Computational Chemistry and Informatics tools are also helping with our hit discovery and lead optimisation. It is our philosophy to provide our combinatorial and medicinal chemists with state-of-the-art desktop decision tools—such as property calculations and computational rules—as an aid to the process of deciding which compounds to make next. Our tools allow chemists to evaluate properties such as LogP, polar surface area and Lipinski donor and acceptor counts. At the same time, the system assesses the compound against rules for oral absorption and bioavailability. Our chemists are also able to access on-line definitions of these rules and even the original papers so that they can make a judgement as to how relevant the rules are to their project. For more detailed studies of *in silico* ADMET, they are able to consult our computational chemistry team for access to more sophisticated predictions, including human intestinal absorption, serum albumin binding, blood-brain barrier penetration and aqueous solubility. The models can be used to predict the ADME properties of virtual libraries and help the chemist select R-group inputs that will give the lead compound or the library a better chance of having good physiological properties. Our EVOseek system is linked in with the desktop property calculator and can be used to store and retrieve assay results and display them in a way that allows the medicinal chemist to interpret hit lists and mine the Structure Activity Relationships.

We see increasing customer demand for cell-based analysis and related screening and assay development capabilities.

Cellular screening expanded. We are seeing increasing customer demand for cell based screens and thus expanded related assay capabilities. Cell based assays are required for signalling pathways and membrane bound proteins as the application of virtual screening approaches is limited to the soluble protein target classes for which structural information can be obtained. The performance of our proprietary uHTS platform EVOscreen® Mark III and our medium throughput screening system for cell based assays was further optimised and also the latter is now in regular use for client screening campaigns (e. g. Calcium flux, reporter and secretion assays). During the year, the assay portfolio utilising our Opera cell imaging reader has been further expanded and now includes bead based assays for the quantification of biomolecules at low concentration and dynamic assays within cells. These project specific developments have been made possible through the further development of the flexible cell imaging software iMacro developed by the Evotec Technologies software team in Tallinn.

Elektra launched for cell sorting. Elektra is the most recent product from Evotec Technologies (ET) and is used for single cell selection and recovery. Its unique features include the use of images from individual cells for the selection process instead of mere fluorescence intensity, providing much more information about the cell of interest, and the ability to deposit single cells safely and without contamination onto plates for growing clones.
Elektra thus complements ET's fast growing sector of cell handling and analysis products, which now comprise not only analysis technology (Opera reader), but also sample preparation technology. This is demonstrated by the use of the Elektra platform in drug discovery for cloning cell lines more rapidly and efficiently than previously possible.

Discovery Programs Division. Achievements in our R&D programmes on proprietary targets and compounds are described in the segment report on page 37.



Dr Ivan Lindley
Novartis Institute for Biomedical Research Vienna
Unit Head

"We at Novartis are impressed by Evotec OAI's strong commitment to customer service, quality science and results. They were able to rapidly establish a new process of screening two adherent cell assays and turn around one million compounds in just three months in a challenging ultra high-throughput screen. Besides delivering outstanding results, our scientists now benefit from this newly established process on our own EVOscreen® Mark III as a basis for accelerating our internal drug screening."

Dr Joachim Kraemer
Evotec OAI AG
Group Leader, Biochemical Assay Services
and Technologies

In April 2003, Novartis signed an assay development and screening contract with Evotec OAI and asked us to screen two adherent cell assays against 500,000 compounds from the Novartis' library. Being able to develop and run such challenging assays in under five months in a miniaturised uHTS format was a significant milestone in the HTS industry. To achieve their goals, the Novartis project team at Evotec OAI worked seven days a week and 16 hours a day—completing both screens with excellent performance six weeks ahead of schedule.

Intellectual property. Our state-of-the-art technologies are covered by strong and broad patent and know-how protection securing our competitive position. The Evotec OAI group holds 200 families of intellectual property rights, each of which protects one invention in different countries. Of these intellectual property rights, 16 German utility models are already registered and 33 German, 33 European, and 29 U.S. and one Japanese patents issued. Our patent position in the detection and cell-handling technology was recently strengthened through the issuance of several patents in Europe and the United States.

Distribution of families of protective rights by technologies at 31 December

Technology	Number of families of protective rights*	
	2003	2002
FCS and FCS+ plus detection technology	47	42
Assay development including cell-handling technologies	56	50
Microfluidics	21	19
Labelling strategies	8	8
Sample carriers	21	17
Molecule optimisation	4	4
Potential target genes (Alzheimer, anti-infective etc.)	39	35
Others	4	4

* these include our proprietary and in-licenced patent and utility model rights

Our people

Over the past years we have emphasized close partnerships with our employees. It is important that all of our 600+ employees believe that Evotec OAI is a special, challenging and rewarding place to work. This is inevitably translated into customer satisfaction and ultimately the success of our business.

We strive to build an organisation that promotes the engagement and responsiveness of our employees to maximise retention—ultimately building a more productive and successful business.

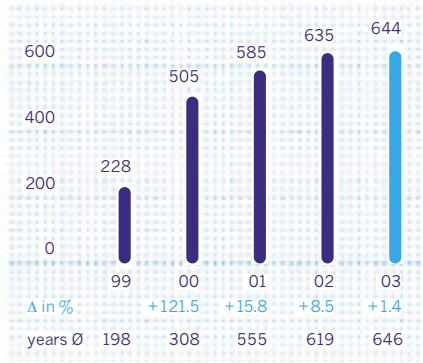
In 2002 we set out an HR Strategy to increase retention of talent, offer greater career development opportunities and improve communication with employees. We are striving to build an organisation where we consciously augment the engagement and responsiveness of our employees. This does not just mean improved employee satisfaction and therefore increased retention of key staff, but ultimately a more productive and successful business. Our goal is to work in partnership with our employees to develop their potential, provide satisfying and challenging work and enable them to be part of a successful and growing company.

Benefits and flexibility. We have responded to the needs of our UK employees to reflect the importance of family with a workplace nursery initiative which provides a highly cost effective solution for employees with small children who wish to return to work. In Hamburg and Oxford we have increased the number of people working on flexible work patterns as well as from home to meet modern work|life balance issues. Also, as a consequence of the Pension Reform Act in Germany, the company launched different programmes ("Unterstützungskasse", "Pensionskasse") allowing employees to add their own contributions to pension and other benefit plans.

Communication. We introduced a new quarterly company wide magazine "Infocus" that provides updates on our business and highlights employee achievements. We also continue to hold quarterly meetings between the senior management and our employees at our major sites. New canteens were opened in Abingdon and Hamburg and are very popular meeting places for staff.
In order to better integrate families of our staff, we organised an open house at our Hamburg headquarters, inviting all the families to a summer party to experience and discover the workplace of their relatives.
In the UK we have supported a number of our employees who have taken part in a variety of charitable events for good causes and deserve a great deal of praise for their efforts.

Measurable results. In order to monitor the success of our approach, we carried out an Employee Attitude Survey in Germany in 2003, following on from the successful similar exercise in the UK in 2002. A participation level of 92% and many of the positive comments from staff showed their real interest and desire to become even more involved in the Company. Through the survey we have a much better understanding of the issues that influence employee engagement.

Employees as of 31 December
Our continued hirings in discovery mask the restructuring in Evotec Technologies



The result of our initiatives in 2003 has been a measurable improvement in the retention rate as labour turnover in the UK is now half the corresponding figure for 2002 and at a historic low in Germany. This improved retention of knowledge and expertise in the business allows us to make significant improvements in productivity and research effectiveness.
The number of Evotec OAI employees increased slightly (+1.5%) during 2003 to 644 at the end of the year.

The past and the future. In December we had an opportunity to look back and assess our successes, as we celebrated the 10th Anniversary of the Company. In Abingdon, we combined this with the official opening of a new state-of-the-art laboratory facility for our integrated discovery services.
In 2004 we will continue to seek ways to better understand and improve the factors that affect levels of employee engagement as we believe that by working in partnership with our employees we can continue to develop an environment of excellence.

Headcount (average age: 34 years)

	Employees	Male	Female	Biologists and Biochemists	Chemists	Physicists	Engineers (R&D) and IT experts	Others
Discovery and Development Services	**440**	**290**	**150**	**17**	**287**	**3**	**11**	**122**
– Biology Services	62	28	34	13	8	2	7	32
– Discovery Chemistry	208	139	69	–	149	–	1	58
– Development Chemistry	117	94	23	–	98	–	–	19
– R&D	23	13	10	2	16	1	2	2
– ProPharma	30	16	14	2	16	–	1	11
Discovery Programs Division	**28**	**14**	**14**	**14**	**3**	**1**	**–**	**10**
– Discovery Programs	5	3	2	2	1	–	–	2
– Evotec Neurosciences	23	11	12	12	2	1	–	8
Tools and Technologies	**84**	**61**	**23**	**8**	**3**	**18**	**43**	**12**
Corporate overhead	**92**	**49**	**43**	**10**	**18**	**1**	**15**	**48**
Grand total	**644**	**414**	**230**	**49**	**311**	**23**	**69**	**192**

Evotec OAI shares and Corporate Governance

Evotec OAI's 2003 performance was rewarded by a 181% increase in share price to € 5.08 at year end. The Company delivered on its promises in 2003 despite challenging market conditions and the disadvantage of a strong Euro against the U.S. Dollar and GB Pound.

The year 2003 witnessed a revival of the trade in growth and technology stocks across the globe.

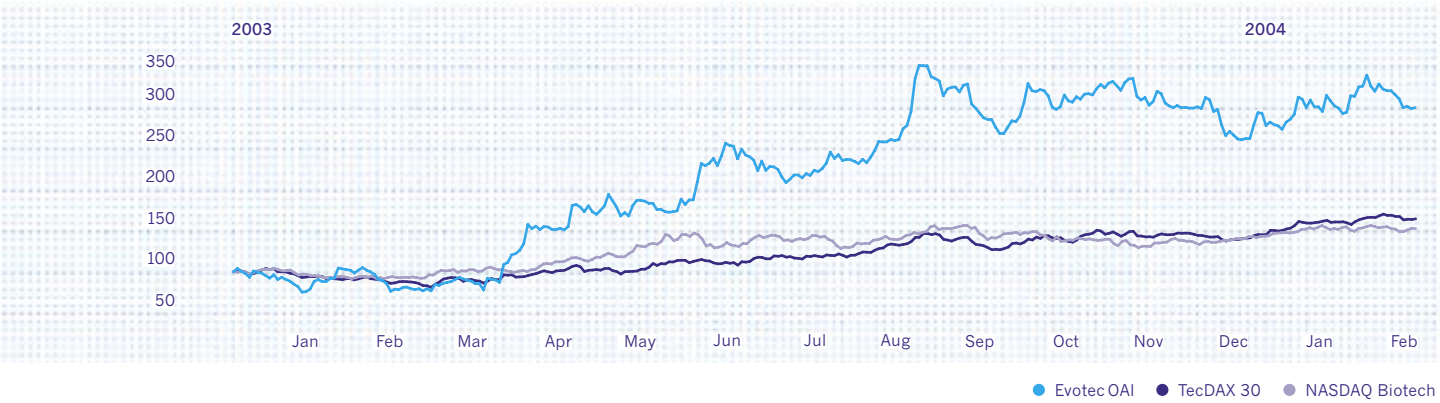
Capital markets are turning around. After declining three years in a row, most leading stock exchanges closed the year with substantial value gains. Stock markets started 2003 on a subdued note amid uncertainty over the Iraq war and worries over deflation. During the course of the year, however, sentiment improved thanks to all-time-low interest rates and extensive tax cuts in the United States, where hard economic data started catching up with the steady stream of upbeat leading indicators. This, in turn, improved corporate earnings prospects resulting in the Dow Jones index trading up 25%. The German DAX index did even better with a 37% gain for the year, recording the best performance of all important standard indexes worldwide (e.g. Dow Jones, STOXX 50, FTSE 100, Nikkei).

Evotec OAI shares 2003

1st quarter	High	€	2.03
	Low	€	1.45
2nd quarter	High	€	4.97
	Low	€	1.68
3rd quarter	High	€	6.81
	Low	€	4.04
4th quarter	High	€	6.50
	Low	€	5.05
2003	High	€	6.81
	Low	€	1.45
	Average share price	€	4.03
	Average daily trading volume	pcs.	156,473
	Price increase	%	181
	Closing price as at 31 December 2003 (Xetra)	€	5.08
	Market capitalisation as at 31 December 2003	€ m	180.4
	Number of shares as at 31 December 2003	pcs.	35,510,130
Key share data	Earnings	€	(0.40)
	Dividend	€	0.00

German securities identification number: 566480
Abbreviation: EVT

Development of Evotec OAI share price 2003 (indexed)



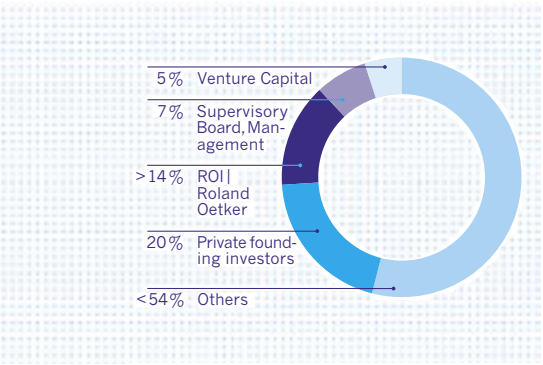
Investors returning to technology stocks also focused on biotech. 2003 witnessed a revival of the trade in German growth and technology stocks. Following the close-down of the Neuer Markt and the build-up of the German stock exchange's "new index world", many companies that fell out of grace during 2002 simply due to their affiliation with the Neuer Markt were in 2003 again looked at based on their fundamentals. They focused on building their businesses and many achieved considerable improvement in their stock prices. The new TecDAX 30 closed the year at 541.31, gaining 51%. The NASDAQ Biotech Index traded up 46%, outpacing all the broad standard indices, partly as a result of a number of significant product approvals.

Evotec OAI was one of the best performing stocks of the TecDAX 30, significantly outperforming its peer group.

Delivery on promises results in sound stock price performance. Evotec OAI stock price gained 181% year-over-year. Even with significant profit-taking around year-end, Evotec OAI closed the year at € 5.08—one of the best performing stocks in the TecDAX 30 and significantly outperforming its peer group. Starting from a very low base, Evotec OAI was rewarded for delivering on its financial and operational targets throughout 2003.

Stock option programmes to reward our employees' dedicated work. The Supervisory Board has acknowledged Evotec OAI's performance in 2003 and agreed that a limited number of stock options should be granted to our employees even though we did not achieve, in the relevant period, the stock price performance required by our stock option programmes for ordinary issuance. We issued a total of 523,400 options. The majority, totalling 437,400, was granted in November at an exercise price of € 5.99 and € 6.29. The remainder, 46,000 options in January 2003 (at an exercise price of € 1.66, € 1.93 and € 2.03) as well as 40,000 options in October (at an exercise price of € 5.50 and € 5.78) were mainly granted to Dr Ian Hunneyball and Bernard Questier as new members of the Management Board when they joined the Company. No options were exercised in 2003 from previous year grants. As of 31 December 2003, there are a total of 2,474,176 options issued that are available for future exercise, or approximately 7% of currently issued shares.

Shareholder structure



Source: Evotec OAI latest estimate 12 | 2003

Financial institutions which report on Evotec OAI

Bank Vontobel AG	ING Financial Markets
Bankgesellschaft Berlin AG	Landesbank Baden-Württemberg
Deutsche Bank AG	M. M. Warburg & Co.
DZ Bank AG	Sal. Oppenheim jr. & Cie.
Equinet Institutional Services GmbH	SES Research GmbH
Goldman Sachs Global Equity Research	SG Securities Ltd

Our IR activities have again laid the ground for transparency and liquidity of our stock.

Conveying our equity story through comprehensive investor relations. Evotec OAI's investor relations activities aim to ensure timely, comprehensive and reliable communication between the company and its shareholders and analysts. A continued dialogue with the financial community is particularly important to us in order to convey our business strategy, demonstrate progress and reliability and, ultimately, create shareholder value. Our Annual Shareholder Meeting in May was attended by approximately 270 participants and the representation of the Evotec OAI's share capital increased to 41% (2002: 31%). Over the course of 2003, senior management held approximately 100 one-to-one presentations at Evotec OAI in Hamburg, Germany, and Oxford, UK, and at 10 international investor conferences and several roadshows in key financial centres across Europe and the U.S. We observed increased investor interest with more investors actively approaching us and visiting us. Although we still suffer from financial institutions cutting back their biotech research resources, 12 financial analysts regularly follow the Company. The analysts play an important role in communicating our progress and key messages to the financial community. In summary, our IR activities in 2003 have again laid the ground for transparency and liquidity of our stock. Our work was rewarded by receipt of the Investor Relations Prize 2003 awarded by the German Capital Magazine and the DVFA (the German Society of Investment Analysts and Asset Managers) with Evotec OAI placed seventh of all companies listed on the TecDAX 30, up from 23rd in 2002.

Being committed to responsible and value-driven corporate management, Evotec OAI endeavours to comply with, and even exceed if possible, the legal external Corporate Governance requirements.

A commitment to good Corporate Governance. Evotec OAI has always been committed to responsible and value-driven corporate management. The Company endeavours to comply with, and even exceed if possible, the Corporate Governance (CG) requirements as defined by the German Corporate Governance Code. We are focused on the protection of shareholder rights, comply with comprehensive disclosure and transparency requirements, and strictly follow the criteria and public recommendations regarding reporting and auditing of financial statements as well as the tasks of the Management and Supervisory Board.

Since the German Corporate Governance Code was first issued in 2002, Evotec OAI has adopted its CG principles and thereby agreed to comply with recommendations of the new code and, in addition, has committed itself to voluntarily complying with most of the suggestions contained therein. We continue to commit to internationally recognised standards and principles of fair and responsible Corporate Governance.

Evotec OAI's Corporate Governance principles include:

> Compliance with high **reporting** standards, publishing financial results not later than 45 days after the end of the quarter and 90 days after the end of the fiscal year. All share price relevant information is available to the public on the Companies Website www.evotecoai.com. The Company conducts conference calls on quarterly financial results and makes these calls and other major events available on the internet for all shareholders.

> Enabling our shareholders to view substantial parts of our **Annual General Meeting** live on the Internet. In addition, we facilitate the exercise of voting rights by arranging representatives that vote on behalf of the individual shareholder in accordance with his instructions. These representatives may also be contacted during the meeting.

> Reporting specific and individualised Management Board and the Supervisory Board **compensation** in the annual financial statements.

> Monthly interactions between Management and Supervisory Board. The internal **rules of procedures** of both bodies have been amended on the basis of the new CG Code. A separate Charter of the Audit Committee, which handles accounting and risk management issues and ensures the independence of Evotec OAI's auditors, has been established.

> Publication of our committed **Company Insider Trading Policy** on our website.

Evotec OAI will continuously update its principles to assure our shareholders that we are committed to very high transparency and the best standards of corporate control. We are also committed to meeting and exceeding both national and international CG standards as they are in existence today or may evolve tomorrow.

In December 2003, the Management Board and the Supervisory Board of Evotec OAI AG stated in accordance with § 161 German Stock Corporation Act:

"Evotec OAI AG has complied in 2003 and intends to comply in the future with the recommendations of the Government Commission's German Corporate Governance Code (revised version as of 21 May 2003) with the following two exceptions:
The stock option programmes in place are based on binding resolutions of several Annual General Meetings. While the exercise of these options requires an increase of the share price, the exercise is not related to other comparison parameters as recommended in the revised version of Section 4.2.3 of the Code. This new recommendation will be considered for relevant future proposals to the AGM.
With the current Supervisory Board Committee composition, non-chair members of such committees do not receive any additional compensation on top of the base Supervisory Board compensation. It is planned to recommend to the Annual General Meeting scheduled for 1 June 2004 to amend the Company's Articles to fully accommodate the recommendation as described in No. 5.4. of the Code."

Shareholdings of the Board of Evotec OAI AG

	Holdings 31 December 2002		Holdings 31 December 2003	
	Shares	Stock options	Shares	Stock options
Management Board				
Joern Aldag	281,000	132,600	286,556	159,600
Dr Dirk H. Ehlers	0	60,000	0	75,000
Dr Ian M. Hunneyball	–	–	0	55,000
Dr Timm-H. Jessen	136,172	83,232	136,172	98,232
Bernard Questier	–	–	0	40,000
Supervisory Board				
Prof Dr Heinz Riesenhuber	110,400	0	110,400	0
Peer Schatz	3,892	0	3,892	0
Dr Pol Bamelis	0	0	1,500	0
Dr Karsten Henco	1,306,356	26,732	1,306,356	26,732
Dr Edwin Moses	313,058	15,000	313,058	15,000
Michael Redmond	1,000	0	1,000	0

Consolidated financial statements according to U.S. GAAP

We have issued the audit opinion in German, which was translated as follows:

Auditors' Report

We have audited the consolidated financial statements, comprising the balance sheet, the income statement and the statements of changes in shareholder's equity and cash flow as well as the notes to the financial statements prepared by Evotec OAI AG, Hamburg, (hereinafter "Company" or "Group") for the business year from January 1 to December 31, 2003. The preparation and the content of the consolidated financial statements in accordance with Accounting Principles Generally Accepted in the United States of America (US-GAAP) are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit of the consolidated annual financial statements in accordance with German auditing regulations and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (IDW). Those standards require that we plan and perform the audit such that it can be assessed with reasonable assurance whether the consolidated financial statements are free of material misstatements. Knowledge of the business activities and the economic and legal environment of the Group and evaluations of possible misstatements are taken into account in the determination of audit procedures. The evidence supporting the amounts and disclosures in the consolidated financial statements are examined on a test basis within the framework of the audit. The audit includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. 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 net assets, financial position, results of operations and cash flows of the Group for the business year in accordance with Accounting Principles Generally Accepted in the United States of America.

Our audit, which also extends to the group management report prepared by the Company's management for the business year from January 1 to December 31, 2003, has not led to any reservations. In our opinion on the whole the group management report provides a suitable understanding of the Group's position and suitably presents the risks of future development. In addition, we confirm that the consolidated financial statements and the group management report for the business year from January 1 to December 31, 2003 satisfy the conditions required for the Company's exemption from its duty to prepare consolidated financial statements and the group management report in accordance with German law.

Hamburg, February 27, 2004

KPMG Deutsche Treuhand-Gesellschaft
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

Dr Erle
German Public Auditor
(Wirtschaftsprüfer)

Kniese
German Public Auditor
(Wirtschaftsprüfer)

If the consolidated financial statements (either with or without the Group management report) are published or made available to third parties in a version other than the one on which we have issued our audit opinion (including translations into other languages) it is necessary to obtain our written agreement, in such cases where our audit opinion is quoted or where a reference is made to our audit; we refer in particular to § 328 of the German Commercial Code.

Evotec OAI AG and Subsidiaries
Consolidated balance sheets according to U.S. GAAP as of 31 December

T€ except share data	Footnote reference	2003	2002	Δ 03|02 in %*
Assets				
Current assets:				
– Cash and cash equivalents		18,763	21,308	(11.94)
– Marketable securities	(4)	708	–	100.00
– Trade accounts receivable, net	(5)	7,714	10,166	(24.12)
– Accounts receivable due from related parties		506	244	107.38
– Inventories	(6)	10,225	8,408	21.61
– Deferred tax assets	(13)	76	45	68.89
– Current tax receivables		2,754	2,665	3.34
– Prepaid expenses and other current assets		2,246	3,196	(29.72)
Total current assets		42,992	**46,032**	(6.60)
Long-term investments	(7)	677	560	20.89
Property, plant and equipment, net	(8)	62,051	61,951	0.16
Intangible assets, excluding goodwill, net	(9)	18,731	29,601	(36.72)
Goodwill, net	(9)	96,418	102,851	(6.25)
Other non-current assets		50	47	6.38
Total assets		220,919	**241,042**	(8.35)

	Footnote reference	2003	2002	Δ 03|02 in %*
Liabilities and stockholders' equity				
Current liabilities:				
– Current maturities of long-term loans	(10)	1,590	1,067	49.02
– Current portion of capital lease obligations	(11)	615	386	59.33
– Trade accounts payable		5,510	4,565	20.70
– Accounts payable to related parties		18	8	125.00
– Advanced payments received		917	5,703	(83.92)
– Accrued liabilities	(12)	6,869	4,726	45.34
– Accrued vacation		925	826	11.99
– Deferred revenues		4,545	2,695	68.65
– Current tax payables		62	80	(22.50)
– Other current liabilities		1,479	1,404	5.34
Total current liabilities		22,530	**21,460**	4.99
Long-term loans	(10)	10,758	6,820	57.74
Long-term capital lease obligations	(11)	1,777	1,113	59.66
Deferred tax liabilities	(13)	11,329	15,544	(27.12)
Deferred revenues		1,661	–	100.00
Other non-current liabilities		98	53	84.91
Minority interests		665	645	3.10
Stockholders' equity:				
– Share capital**	(15)	35,510	35,510	0.00
– Additional paid-in capital		540,035	536,908	0.58
– Unearned compensation		(150)	(345)	(56.45)
– Other comprehensive loss		(40,046)	(27,660)	44.78
– Retained deficit		(363,248)	(349,006)	4.08
Total stockholders' equity		172,101	**195,407**	(11.93)
Total liabilities and stockholders' equity		220,919	**241,042**	(8.35)

* unaudited
** 53,210,130 and 53,210,130 shares, 1 € nominal amount, authorised at 31 December 2003 and 2002, respectively
35,510,130 and 35,510,130 shares issued and outstanding in 2003 and 2002, respectively

See accompanying notes to consolidated financial statements.

Evotec OAI AG and Subsidiaries
Consolidated statements of operations according to U.S. GAAP for the years ended 31 December

T€ except share data and per share data	Footnote reference	2003	2002	Δ 03|02 in %*
Revenue:				
– Drug discovery products & development of technologies		17,223	11,825	45.65
– Drug discovery services		60,005	58,170	3.15
Total revenue		77,228	**69,995**	10.33
Costs of revenue:				
– Drug discovery products & development of technologies		9,952	3,768	164.12
– Drug discovery services		36,241	34,763	4.25
Total costs of revenue		46,193	**38,531**	19.89
Gross profit		31,035	**31,464**	(1.36)
Operating costs and expenses:				
– Research and development expenses		15,466	23,012	(32.79)
– Selling, general and administrative expenses		17,924	20,467	(12.42)
– Amortisation of intangible assets	(9)	10,671	12,018	(11.21)
– Impairment of goodwill		–	109,389	(100.00)
– Other operating expenses		2,751	2,090	31.63
Total operating costs and expenses		46,812	**166,976**	(71.96)
Operating loss		(15,777)	**(135,512)**	(88.36)
Other non-operating income (expense)				
– Interest income		540	681	(20.70)
– Interest expense		(714)	(331)	115.71
– Net loss from equity investments	(7)	(1,568)	(62)	–
– Foreign currency exchange gain (loss), net		(327)	210	(255.71)
– Other non-operating income, net		713	615	15.93
Total non-operating income		(1,356)	**1,113**	(221.83)
Loss before taxes and minority interests		(17,133)	**(134,399)**	(87.25)
– Income tax benefit	(13)	2,825	2,755	2.54
– Minority interests		66	14	371.43
Net loss		(14,242)	**(131,630)**	(89.18)

Weighted average shares outstanding	35,510,130	**35,509,285**
Net loss per share	(0.40)	(3.71)

* unaudited

See accompanying notes to consolidated financial statements.

Evotec OAI AG and Subsidiaries
Consolidated statements of cash flows according to U.S. GAAP for the years ended 31 December

T€	2003	2002
Cash flows from operating activities:		
Net loss	(14,242)	(131,630)
Adjustments to reconcile net loss to net cash used in operating activities:		
– Depreciation of property, plant and equipment	9,835	11,105
– Amortisation of intangible assets	10,671	12,018
– Depreciation of current assets	473	–
– Impairment of goodwill	–	109,389
– Net loss from equity investments	1,568	62
– Stock compensation expense	271	324
– Gain on sale of marketable securities, net	–	(55)
– Loss on sale of long-term investments	–	20
– Loss on sale of property, plant and equipment, net	63	68
– Deferred tax benefit	(3,186)	(2,928)
– Minority interests	(66)	(14)
Decrease (increase) in:		
– Accounts receivable	1,727	1,602
– Inventories	(2,339)	(2,072)
– Other assets from sale of shares in subsidiaries	–	(5)
– Other assets	481	57
Increase (decrease) in:		
– Accounts payable	1,144	(912)
– Advanced payments received	(4,786)	4,113
– Deferred revenues	3,691	423
– Accrued liabilities	2,392	(1,603)
– Current taxes payable	(13)	80
– Other liabilities	128	(1,012)
Net cash provided by (used in) operating activities	7,812	**(970)**
Cash flows from investing activities:		
– Purchase of marketable securities	(4,230)	(1,923)
– Purchase of long-term investments	(1,524)	(11)
– Purchase of property, plant and equipment	(12,515)	(7,299)
– Purchase of intangible assets	(1,689)	(28)
– Proceeds from sale of property, plant and equipment	15	11
– Proceeds from sale of shares in long-term investments	–	443
– Proceeds from sale of shares in subsidiaries	–	1
– Proceeds from sale of marketable securities	3,572	10,978
Net cash provided by (used in) investing activities	(16,371)	**2,172**
Cash flows from financing activities:		
– Proceeds from capital increase	–	20
– Capital contributed by minorities	3,065	–
– Net proceeds from increase of loans	5,496	4,914
– Repayment of loans	(1,335)	(823)
Net cash provided by financing activities	7,226	**4,111**
Net increase (decrease) in cash and cash equivalents	(1,333)	5,313
Exchange rate difference	(1,212)	(2,656)
Cash and cash equivalents at beginning of year	21,308	**18,651**
Cash and cash equivalents at end of year	18,763	**21,308**

See accompanying notes to consolidated financial statements.

Evotec OAI AG and Subsidiaries
Supplemental disclosures of cash flow information for the years ended 31 December

T€	2003	2002
Cash paid during the year for:		
– Interest	690	331
– Taxes	401	1,018
Supplemental schedule of non-cash activities:		
– Acquisition of long-term investments	198	611
– Additions to capital leases	1,352	1,335
– Removal of embargo	–	(942)
– Change in embargo intangibles	–	(658)
– Acquisition adjustment of Evotec OAI Ltd	–	(1,432)

See accompanying notes to consolidated financial statements.

Evotec OAI AG and Subsidiaries
Consolidated fixed asset movement schedule according to U.S. GAAP

T€	Acquisition and manufacturing costs					
	01|01|2003	Foreign exchange	Additions	Disposals	Reclass	31|12|2003
I. Intangible assets						
1. Patents and licences	3,106	–	1,689	–	–	4,795
2. Goodwill	102,851***	(6,433)	–	–	–	96,418
3. Developed technology	31,662	(2,193)	–	–	–	29,469
4. Customer list	21,433	(1,599)	–	–	–	19,834
	159,052	**(10,225)**	**1,689**	**–**	**–**	**150,516**
II. Tangible fixed assets						
1. Buildings and leasehold improvements	24,781	(1,823)	74	–	3,924	26,956
2. Plant, machinery and equipment	47,306	(2,900)	2,370	621	7,116	53,271
3. Furniture and fixtures	10,471	(624)	1,528	117	6	11,264
4. Purchased software	1,196	–	24	1	–	1,219
5. Capital leases	2,148	(161)	1,476	–	(221)	3,242
6. Assets under construction	2,966	(171)	8,141	7	(10,825)	104
	88,868	**(5,679)**	**13,613**	**746**	**–**	**96,056**
III. Financial assets						
1. Long-term investments	560	(29)	1,722	1,568	–	685
2. Other financial assets	47	–	3	–	–	50
	607	**(29)**	**1,725**	**1,568**	**–**	**735**
	248,527	**(15,933)**	**17,027**	**2,314**	**–**	**247,307**

* calculated at the yearly average foreign exchange rate results in an increase of T€ 198
** calculated at the yearly average foreign exchange rate results in an increase of T€ 128
*** net of accumulated amortisation as of 31 December 2001 of T€ 162,195 and impairment as of 2002 of T€ 109,389

See accompanying notes to consolidated financial statements.

Evotec OAI AG and Subsidiaries
Consolidated statements of changes in stockholders' equity and comprehensive loss according to U.S. GAAP

T€ except share data	Share capital		Additional paid-in capital	Unearned compensation
	Shares	Amount		
Balance at 31 December 2001	**35,507,047**	**35,507**	**536,857**	**(635)**
Share capital increase	3,083	3	17	–
Stock option plan	–	–	34	290
Comprehensive loss:				
– Foreign currency translation	–	–	–	–
– Net unrealised holding losses on available-for-sale securities	–	–	–	–
– Net loss	–	–	–	–
Total comprehensive loss				
Balance at 31 December 2002	**35,510,130**	**35,510**	**536,908**	**(345)**
Stock option plan	–	–	76	195
Capital contributed by minorities	–	–	3,051	–
Comprehensive loss:				
– Foreign currency translation	–	–	–	–
– Net unrealised holding losses on available-for-sale securities	–	–	–	–
– Net loss	–	–	–	–
Total comprehensive loss				
Balance at 31 December 2003	**35,510,130**	**35,510**	**540,035**	**(150)**

See accompanying notes to consolidated financial statements.

Depreciation, amortisation and writedowns					Net book value	
01|01|2003	Foreign exchange	Additions	Disposals	31|12|2003	31|12|2003	31|12|2002
2,120	–	406	–	2,526	2,269	986
–	–	–	–	–	96,418	102,851
14,835	(986)	6,100	–	19,949	9,520	16,827
9,645	(720)	3,967	–	12,892	6,942	11,788
26,600	**(1,706)**	**10,473***	**–**	**35,367**	**115,149**	**132,452**
3,299	(336)	1,621	–	4,584	22,372	21,482
15,995	(1,150)	5,628	549	19,924	33,347	31,311
6,530	(448)	1,804	113	7,773	3,491	3,941
813	–	146	1	958	261	383
280	(21)	507	–	766	2,476	1,868
–	–	–	–	–	104	2,966
26,917	**(1,955)**	**9,706****	**663**	**34,005**	**62,051**	**61,951**
–	–	8	–	8	677	560
–	–	–	–	–	50	47
–	**–**	**8**	**–**	**8**	**727**	**607**
53,517	**(3,661)**	**20,187**	**663**	**69,380**	**177,927**	**195,010**

Other comprehensive loss	Unrealised gains (losses) on securities	Retained deficit	Total stockholders' equity
(6,914)	**152**	**(217,376)**	**347,591**
–	–	–	20
–	–	–	324
(20,746)	–	–	(20,746)
–	(152)	–	(152)
–	–	(131,630)	(131,630)
			(152,528)
(27,660)	**–**	**(349,006)**	**195,407**
–	–	–	271
–	–	–	3,051
(12,386)	–	–	(12,386)
–	–	–	–
–	–	(14,242)	(14,242)
			(26,628)
(40,046)	**–**	**(363,248)**	**172,101**

Evotec OAI and Subsidiaries
Notes to consolidated financial statements

(1) Business Description and Basis of Presentation

Evotec OAI AG and subsidiaries ("Evotec" or the "Company") is a biotechnology group serving the life science industry by designing and applying technologies for highly effective drug discovery. Evotec offers a comprehensive range of high-value added services and products required to increase the efficiency and at the same time reduce the risk in the identification of new drugs. By integrating proprietary state-of-the-art technologies and processes in biology, chemistry and screening, the Company has established a unique position for the critical elements in the drug discovery and development process—from target to clinical development.
The Company was founded on 8 December 1993 as EVOTEC BioSystems GmbH. Evotec had an initial public offering in Germany on 10 November 1999.
All amounts herein are shown in thousands of Euro ("T€"), unless indicated otherwise.

(2) Summary of Significant Accounting Policies

The following is a summary of significant accounting policies followed in the preparation of the accompanying consolidated financial statements.

Principles of Consolidation. The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") and include the accounts of Evotec OAI AG and all companies which are under its control. All intercompany transactions and balances have been eliminated in consolidation.
Investments where Evotec does not have a controlling interest but is in a position to influence the operating or capital decisions of the investee are carried at equity.

Cash and Cash Equivalents. The Company considers all highly liquid short-term investments with original maturities of three months or less to be cash equivalents.

Marketable Securities. The Company applies Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standards ("SFAS") No. 115, "Accounting for Certain Investments in Debt and Equity Securities". In accordance with SFAS No. 115, the Company has classified all of its debt and equity securities as available-for-sale and states them at fair value as determined by the most recently traded price of each security at the balance sheet date. Unrealised gains and losses are included in accumulated other comprehensive loss, a separate component of stockholders' equity. Unrealised losses deemed to be other than temporary are reported in other non-operating expense.
Realised gains and losses from the sale of available-for-sale securities are determined based on specific identification of the cost of securities sold and are reported in other non-operating income and expense.

Inventories. Inventories are valued at the lower of cost or market, cost being generally determined on the basis of an average method. Cost consists of purchased component costs and manufacturing costs, which are comprised of direct material and labour costs and certain indirect costs. Costs are removed to costs of revenue based on specific identification.

Property, Plant and Equipment. Property, plant and equipment acquisitions, including leasehold improvements, are recorded at cost less any vendor rebates. Amortisation of leasehold improvements is calculated using the straight-line method over the shorter of the related lease term or the estimated useful life. Leased property, plant and equipment meeting certain criteria are capitalised and the present value of the related lease payments is recorded as a liability. Depreciation of property, plant and equipment, which includes amortisation of assets under capital leases, is calculated using the straight-line method over the estimated useful lives of the assets as follows:

Buildings and leasehold improvements	11–35 years
Plant, machinery and equipment	3–20 years
Furniture and fixtures	3–10 years
Computer equipment and software	3–5 years

The costs included in property, plant and equipment related to assets under construction are not depreciated until the assets are placed into service by the Company. Upon sale or retirement, the costs and the related accumulated depreciation are removed from the respective accounts, and any gain or loss is included in other operating income and expense. Maintenance and repairs are expensed as incurred.

Intangible Assets, excluding Goodwill. Intangible assets, excluding goodwill, consist of separately identified intangible assets such as developed technologies, customer lists and patents which were acquired in business combinations, as well as purchased licenses and patents.
Intangible assets with definite useful lives are recorded at cost and are amortised using the straight-line method over the estimated useful lives of the assets:

Developed technologies	3–5 years
Customer list	5 years
Patents	10 years or shorter life

The weighted average years of amortisation for developed technology, customer list and patents are 4.9, 5.0 and 8.8 years, respectively.

Goodwill. The goodwill results from the acquisition of Oxford Asymmetry International plc. as of October 2000.

Revenue Recognition. Revenue under collaboration agreements is recognised when earned and realisable based upon the performance requirements of the respective agreements. Advance payments received in excess of amounts earned are recorded as deferred revenue. Revenue under these long-term collaborative agreements include but are not limited to the following:

1. Database Access Fees—Revenue from database access fees is recognised rateably over the related contract period.

2. Research Payments—Revenue from research payments finances both direct costs incurred in connection with the Company's ongoing research and development activities and indirect costs incurred as part of an allocation of certain other administrative expenses. Revenue from research payments is recognised rateably over the related forecasted research period as services are provided.

3. Success Payments—Revenue contingent upon the attainment of certain milestones is recognised in the period the milestone is successfully achieved. This usually occurs when the contract partner agrees that the requirements stipulated in the agreement have been met.

Revenues from the sale of systems, equipment and devices are recorded at the time of delivery, title transfer or upon final acceptance by the customer as required by agreement.

Product and chemical compound sales are recorded as revenue upon delivery if the Company has received a customer order, the price is determinable and collectibility is reasonably assured. The Company assesses collectibility based on a number of factors, including past transaction history with the customer and their creditworthiness.
Service revenues generated from contracted services are recognised as the services are rendered. Revenue from compound access fees is recognised rateably over the related forecasted service period. Payments for contracted services are generally paid in advance and recorded as deferred revenue until earned. Some contracted services are settled in part by non-monetary payments. Due to the relatively insignificant portion of the contract value which is represented by the non-monetary portion, revenues derived from these particular contracts are recognised on the same basis as that used in monetary transactions.
The Company has entered into multiple-element contracts and carefully determined whether the different revenue-generating elements are sufficiently separable and whether there exists sufficient evidence of their fair values to separately account for some or all of the individual elements of the contracts. Only if an element is considered to meet these criteria it represents a separate unit of accounting.
Under the terms of various contractual arrangements, Evotec receives royalty payments which are incremental to the other company's respective product sales. Royalty income of T€ 480 and T€ 474 is included in product revenue for 2003 and 2002, respectively.
In December 2003, the Staff of the Securities and Exchange Commission issued Staff Accounting Bulletin No. 104 (SAB 104). Purpose of SAB 104 is to revise or rescind portions of the interpretive guidance included in SAB 101 in order to make this interpretive guidance consistent with current authoritative accounting guidance and SEC rules and regulations. The adoption of SAB 104 in 2003 had no impact on our financial position or results of operations.

Advertising Costs. The company expenses advertising costs in the year incurred.

Derivative Policy. The Company does not engage in derivatives trading, market-making or other speculative activities. The Company enters from time to time into agreements to obtain foreign currencies at specified rates based on expected future cash flows for each currency. Changes in the value of derivative financial instruments are measured at the balance sheet date and recognised in current earnings.

Income Taxes. Under the asset and liability method, deferred tax assets and liabilities are recognised for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases as well as for tax loss carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognised in the period that includes the enactment date. In assessing the recoverability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realised.

Research and Development. Research and development costs are expensed as incurred. Costs to develop software internally which is used as an integral part of a product or process is capitalised when both the technological feasibility of the software component is established and the research and development activities relating to the hardware component have been successfully completed. These conditions are usually met shortly before the product or process is launched and as a result no development costs of software have been capitalised. The software included in property, plant and equipment consists only of purchased software.
The Company receives grants from government authorities for the support of specific research and development projects. The grants are requested when qualifying expenses have been incurred and are recognised as a reduction of research and development expense when they are received. The amounts recognised as a reduction of the Company's research and development expense were T€ 1,012 and T€ 1,071 in 2003 and 2002, respectively. Under the terms of the grants, the governmental agencies generally have the right to audit the submitted qualifying expenses of the Company.

Translation of Foreign Operations and Foreign Currency Denominated Transactions. The assets and liabilities of foreign subsidiaries with functional currencies other than the Euro are translated into Euro using period-end exchange rates, while the revenues and expenses of such subsidiaries are translated using average exchange rates during the period. Gains or losses resulting from translating foreign functional currency financial statements are included in other comprehensive loss and are reported as a separate component of stockholders' equity. Gains or losses resulting from foreign currency denominated transactions are included in other non-operating income and expense.

Impairment of Long-Lived Assets. The Company reviews long-lived assets in accordance with SFAS 144, excluding goodwill, for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to the undiscounted amount of estimated future cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment recognised is measured by the amount by which the carrying amount of the assets exceeds the discounted amount of estimated future cash flows. Considerable management judgement is necessary to estimate discounted future cash flows. Assets to be disposed of are reported at the lower of the carrying amount or the fair value less costs to sell and are not depreciated.

Impairment of Goodwill. According to SFAS 142, "Goodwill and Other Intangible Assets" we perform goodwill impairment tests on an annual basis and between annual tests, if economic weaknesses, unexpected declines in operating results of reporting units and non-temporary market capitalisation declines are indicative of goodwill impairment. The process of evaluating the potential impairment of goodwill requires significant judgement during the analysis. In a first step of the impairment test, the fair values of each reporting unit are estimated using the discounted amount of estimated future cash flows. The discount rates for each reporting unit reflect an assessment of all inherent reporting unit risks. If the fair value of a reporting unit is less than its book value, a second step is performed that compares the implied fair value of the reporting units goodwill to the carrying value of its goodwill. As required by SFAS 142, we performed our annual goodwill impairment test in the fourth quarter of 2003 (see Note (9)). No necessity for any adjustment of the values of the assets recognised in our balance sheet due to impairment was identified in 2003.
Any impairment is reported as a separate component of operating costs and expenses in the consolidated statement of operations.

Comprehensive Loss. Comprehensive loss consists of net loss, foreign currency translation adjustments, and unrealised gains (losses) on marketable securities and is presented in the consolidated statements of changes in stockholders' equity and comprehensive loss.

Stock Compensation. The Company has elected to apply the provisions of Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees" in accounting for options granted under its stock option plan. Compensation cost from the issuance of employee stock options is measured using the intrinsic value method and is charged to expense over the vesting period. The following table illustrates the effect on net loss and net loss per share if the Company had applied the fair value method provisions of SFAS No. 123, "Accounting for Stock-Based Compensation", amended by SFAS 148 "Accounting for Stock-Based Compensation—Transition and Disclosure":

T€	2003	2002
Net loss, as reported	(14,242)	(131,630)
Add compensation expense		
determined under APB 25	271	324
Less compensation expense		
determined under SFAS 123	(1,111)	(1,265)
Adjusted net loss	**(15,082)**	**(132,571)**
Net loss per share | As reported in €	(0.40)	(3.71)
Net loss per share | Adjusted in €	(0.42)	(3.73)

The adjusted amounts do not reflect any tax effects due to the 100% valuation allowance on the deferred tax assets in Germany. The adoption of SFAS 148 had no impact on our financial position or results of operations, because the Company has not applied SFAS 148.

Use of Estimates. The preparation of the accompanying consolidated financial statements requires management to make estimates and assumptions that affect both the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the financial statements as well as the reported amounts of revenues and expenses during the reporting period. Actual results could differ from Management's estimates. In addition, changes in the current economic conditions and other events could also have a significant effect on reported amounts.

Recent Pronouncements and Adoptions. In 2001, the Financial Accounting Standards Board (FASB) issued SFAS 143, Accounting for Asset Retirement Obligations. SFAS 143 requires companies to record the fair value of a liability for an asset retirement obligation in the period in which it is incurred, which is adjusted to its present value each subsequent period. In addition, companies must capitalise a corresponding amount by increasing the carrying amount of the related long-lived asset, which is depreciated over the useful life of the related long-lived asset. The adoption of SFAS 143 on 1 January 2003, had no material impact on our consolidated financial position or results of operations.

In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities". SFAS No. 149 amends and clarifies accounting and reporting for derivative instruments and hedging activities under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities". SFAS No. 149 is effective for derivative instruments and hedging activities entered into or modified after 30 June 2003, except for certain forward purchase and sale securities. For these forward purchase and sale securities, SFAS No. 149 is effective for both new and existing securities after 30 June 2003. The adoption of SFAS 149 had no impact on our financial position or results of operations.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity". SFAS No. 150 establishes standards for how an issuer classifies and measures in its statement of financial position certain financial instruments with characteristics of both liabilities and equity. In accordance with the standard, financial instruments that embody obligations for the issuer are required to be classified as liabilities. SFAS No. 150 will be effective for financial instruments entered into or modified after 31 May 2003 and otherwise will be effective at the beginning of the first interim period beginning after 15 June 2003. The Company has no outstanding preferred stock. However, if and when the Company issues such stock, the Company will reclassify its redeemable preferred stock as a liability accordingly. Management does not expect the adoption of SFAS No. 150 to have a material impact on the Company's statement of earnings, financial position, or cash flows.

In January 2003, the Financial Accounting Standards Board issued FASB Interpretation No. 46, "Consolidation of Variable Interest Entities" ("FIN 46"). FIN 46, as amended, requires that variable interest entities be consolidated by the primary beneficiary of the entity if certain criteria are met. FIN 46 is effective immediately for all variable interest entities created or acquired after 31 January 2003. For variable interest entities created or acquired prior to 1 February 2003, the provisions of FIN 46 become effective for the Company during the first quarter of 2004. In late December 2003, FASB has published a revision to Interpretation 46 ("46R") to clarify some of the provisions of FASB Interpretation No. 46, Consolidation of Variable Interest Entities. The additional guidance is being issued in response to input received from constituents regarding certain issues arising in implementing Interpretation 46. Application by public entities, other than small business issuers, for all other types of variable interest entities is required in financial statements for periods ending after 15 March 2004.

A variable interest entity is a corporation, partnership, trust, or any other legal structure used for business purposes that either (a) does not have equity investors with

voting rights, or (b) has equity investors that do not provide sufficient financial resources for the entity to support its activities. Historically, entities generally were not consolidated unless the entity was controlled through voting interests. FIN 46 changes that by requiring a variable interest entity to be consolidated by a company if that company is subject to a majority of the risk of loss from the variable interest entity's activities or entitled to receive a majority of the entity's residual returns or both. A company that consolidates a variable interest entity is called the "primary beneficiary" of that entity. FIN 46 also requires disclosures about variable interest entities that a company is not required to consolidate but in which it has a significant variable interest. The consolidation requirements of FIN 46 apply immediately to variable interest entities created after 31 January 2003. The consolidation requirements of FIN 46 apply to existing entities in the first fiscal year or interim period beginning after 15 December 2003, with early adoption permitted. Also, certain disclosure requirements apply to all financial statements issued after 31 January 2003, regardless of when the variable interest entity was established. The Company has concluded that only DIREVO Biotech AG falls under the VIE definition of FIN 46. However, as the Company is not subject to a majority of the risk of loss from DIREVO's activities or entitled to receive a majority of DIREVO's residual returns or both the Company is not regarded as a primary beneficiary and therefore not required to consolidate that company.
In December 2002, FASB's Emerging Issues Task Force (EITF) issued its Consensus on EITF Issue 00-21, "Revenue Arrangements with Multiple Deliverables". The Consensus mandates how to identify whether goods or services or both that are to be delivered separately in a bundled sales arrangement should be accounted for individually because they are unique units of accounting. The Consensus applies to all contractually-binding arrangements comprising more than one product or service. The guidance in EITF Issue 00-21 is effective for revenue arrangements entered into in fiscal periods beginning after 15 June 2003. The adoption of EITF 00-21 had no impact on our financial position or results of operations.

EBITDA. EBITDA stands for earnings before interest, taxes, depreciation (incl. allowance for accounts receivables and inventories) and amortisation.

(3) Use Restrictions on the Company's Technology

Evotec was subject to certain restrictions concerning technologies arising in the course of its cooperations with GlaxoSmithKline (GSK) and Novartis.

Under the terms of an amended contract with GSK, Evotec may use the results of a collaboration agreement for projects not related to pharmaceutical drug discovery, for internal projects in pharmaceutical drug discovery, or in "external target collaborations", i.e. cooperations which the Company enters into with third parties with respect to the screening of chemical or biological substances on a pharmaceutical target, provided that the number of molecular targets does not exceed certain restrictions. These restrictions lapsed in April 2003.
A fourth amendment to this agreement, signed in May 2001, allows Evotec to sell detection systems and liquid handling devices, which have a restricted throughput of compounds per day. As part of the amendment, GSK was entitled to receive a specific number of systems and devices under preferred conditions. The estimated future commitment was accrued in 2001 and resulted in the recognition of an intangible asset. The intangible asset is amortised over the remaining period of the original restriction, that being two years. In 2002, the Company delivered all of the systems and devices which GSK was entitled to under the previously mentioned amendment. The settlement of this obligation resulted in reducing the cost basis of the respective intangible asset at the Company. In addition, the amendment grants Evotec the right to enter into other collaborative agreements with two additional funding partners. In the case such agreements are established, GSK will receive a specified amount of credits against future goods depending on the number of additional funding partners. As of the balance sheet date, the Company has not entered into any additional funding partner collaborative agreements. Further more the sale of the biochemical Mark III to non-funding companies is restricted until the third anniversary of the Mark III delivery date, which is mid of December 2004. The sale of the cell upgrade on the Mark III is restricted until May 2005.
With regards to the "external target collaborations" under an agreement with Novartis, Evotec must pay royalties equal to 5% of qualifying revenue to Novartis for a period of ten years expiring on 16 March 2008. The Company has recorded royalty expenses of T€ 42 and T€ 20 in 2003 and 2002, respectively.
In December 2001, Evotec signed an amendment to the Novartis agreement which allows Evotec to sell detection systems and liquid handling devices which have a restricted throughput of compounds per day. As part of the amendment, Novartis was entitled to buy a specific number of systems and devices under preferred conditions and (or) participate in a share of the revenue on the sales of the equipment to third parties up to a limited amount. In consideration for the rights received in 2001, the Company accrued a liability and recognised an intangible asset, each in the amount of T€ 400. The intangible asset has been amortised over the remaining period of

the original restriction—that being two years. In 2002, the Company has fulfilled all its obligations under the previously mentioned amendment and settled its liability.

(4) Marketable Securities

All marketable securities in 2003 in the amount of T€ 708 consist of foreign corporate bonds which are publicly traded, are due within one year, are denominated in GBP and are considered as available for sale.
The unrealised gain on these securities amounted to T€ 0 as of 31 December 2003. Realised losses on the sale of corporate bonds amounted to T€ 0 and T€ 22 in 2003 and 2002, respectively. Realised gains on the sale of money market mutual funds and corporate bonds amounted to T€ 0 and T€ 0 in 2003, respectively, and to T€ 70 and T€ 7 in 2002, respectively.

(5) Trade Accounts Receivable

The Company has determined the non-payment risk of all trade accounts receivable which resulted in an allowance of T€ 126 and T€ 0 in 2003 and 2002, respectively.

(6) Inventories

Inventories consist of the following:

T€	31|12|2003	31|12|2002
Raw materials	4,647	4,816
Work-in-progress	4,234	3,231
Finished goods	1,344	361
Total inventories	**10,225**	**8,408**

Raw materials consist of biological materials and substances, chemicals and components of instruments. Work-in-progress in 2003 primarily consists of costs incurred on customer projects, an Evotec Mark III screening machine and laboratory equipment which were not completed at year end. Finished goods include finished laboratory equipment and customer projects which are ready for shipment. The Company carries an allowance on raw materials of T€ 205 and T€ 205, included in the amounts above, as of 31 December 2003 and 2002, respectively. Additionally, an allowance on work-in-progress and finished goods of T€ 115 and T€ 114, respectively is included in the amounts of 2003 above.

(7) Long-term Investments

Long-term investments (unconsolidated) consist of the following:

T€	31|12|2003	31|12|2002
Prolysis Ltd.	354	383
SiREEN AG	323	125
Vmax Ltd.	–	52
DIREVO Biotech AG	–	–
DeveloGen joint venture	–	–
Total long-term investments	**677**	**560**

Evotec acquired a 3.88% investment in 2002 in the common stock of Prolysis Ltd. as part of a three year drug discovery agreement where Evotec will earn additional shares by performing services for Prolysis. All shares have been acquired through non-monetary payments. The shares are held as a long-term investment at cost and are subject to a regular fair value impairment review, at least once a year. As of 31 December 2003 and 2002 the carrying amount of the investment is T€ 354 and T€ 383, respectively, which was earned in accordance with the above mentioned agreement.
Evotec acquired a 5.0% investment in the common stock of SiREEN AG ("Sireen"), during the foundation of the company in January 2002. This investment is accounted for at cost and is subject to a regular fair value impairment review, at least once a year. On 11 October 2002, Sireen issued to new investors 118,548 shares of voting redeemable preference stock. Due to the participation of Evotec in this capital increase, the investment increased from 5.0% to 6.36%. This investment is partly paid by services provided in a drug discovery agreement between Evotec and Sireen (2003: T€ 198; 2002: T€ 115).
Evotec acquired a 46.36% investment in the common stock of Vmax Ltd. ("Vmax") on 22 August 2002, which is accounted for under the equity method of accounting. Vmax specialises in the field of the discovery and development of small molecule antimicrobials. Through 31 December 2003 and 2002, Vmax had not generated any revenue. The Company's accumulated equity contributions and advances to Vmax amounted to T€ 196 and T€ 103 at 31 December 2003 and 2002, respectively. The Company's share of the net loss of Vmax amounted to T€ 137 and T€ 51 for 2003 and 2002, respectively. The amount by which Evotec's share of the loss of the investee exceeded the equity investment was set off against the advances. The remaining carrying amount of T€ 8, recorded in long-term investments has been written down to T€ 0 as of 31 December 2003.
Evotec has a 22.72% voting interest by virtue of a 65.0% investment in the common stock of DIREVO Biotech AG ("Direvo"), which is accounted for under the equity method of accounting. Direvo is involved in screening-based directed evolution and applies its integrated proprietary

technologies to the development of biopharmaceuticals, industrial enzymes, chemical biocatalysts and enzymes for food and feed. Due to the redeemable feature of the preferred shares, the Company reduced the investment in Direvo to zero in 2001. On 16 December 2002, at the annual general meeting, the shareholders of Direvo decided to issue 43,072 new shares of preference stock. Because of the voting rights held by the preferred stockholders, Evotec's proportionate voting interest of Direvo decreased from 32.5% to 22.72%.
The Company's share of the net loss of Direvo amounted to T€ 0 in 2003 and T€ 11 for 2002. For the year ended 31 December 2003, Direvo had generated revenues of T€ 271 and incurred a net loss of T€ 2,689. Our maximum exposure to loss as a result of our involvement with DIREVO Biotech AG is limited to the original investment in DIREVO AG in the amount of T€ 32.
The Company and DeveloGen AG formed a 50:50 joint venture in August 2003 to discover, develop and commercialise drug candidates in certain areas of Metabolic Diseases and to collaborate with pharmaceutical companies for defined projects in these areas. This joint venture is consolidated at equity in the financial statements. Evotec's total investment in 2003 amounted to T€ 0. Research and development expenses of the Company related to the joint venture in the amount of T€ 1,431 are shown under net loss from equity investments.
The long-term investments of Evotec continue to have losses and, therefore, do not have undistributed profits.
The Company has recorded revenues with the investments SiREEN AG and Prolysis Ltd. in the amount of T€ 704 and T€ 1,747 in 2003 as well as T€ 565 and T€ 1,018 in 2002, respectively. No further material transactions with investments of the Company were recorded.

(8) Property, Plant and Equipment

Property, plant and equipment consist of the following:

T€	31|12|2003	31|12|2002
Buildings and leasehold improvements	26,956	24,781
Plant, machinery and equipment	53,271	47,306
Furniture and fixtures	11,264	10,471
Purchased software	1,219	1,196
Capital leases	3,242	2,148
Assets under construction	104	2,966
Fixed assets, at cost	**96,056**	**88,868**
Less accumulated depreciation		
without software	33,047	26,104
Less accumulated amortisation		
of software	958	813
Total property, plant and equipment	**62,051**	**61,951**

The main additions in 2003 relate to the completion of a laboratory research facility in Abingdon, UK and several laboratory equipments in Hamburg. Upon completion of the assets under construction, costs are transferred into their respective fixed assets classification. Depreciation expense amounted to T€ 9,834 and T€ 11,105 in 2003 and 2002, respectively.
The net book values included in the fixed assets, which are held under capital leases, are plant and machinery as well as fixture and fittings of T€ 2,462 and T€ 14 as of 31 December 2003 and T€ 1,768 and T€ 100 as of 31 December 2002, respectively. The related depreciation amounts to T€ 540 and T€ 14 in 2003 and T€ 208 and T€ 29 in 2002, respectively.

(9) Other Intangible Assets and Goodwill

Intangible assets, excluding goodwill, consist of the following:

T€	31|12|2003	31|12|2002
Developed technologies	29,469	31,662
Customer list	19,834	21,433
Patents and licenses	4,795	3,106
Intangible assets, at cost	**54,098**	**56,201**
Less accumulated amortisation	35,367	26,600
Total intangible assets excluding goodwill	**18,731**	**29,601**

Amortisation expense of intangible assets amounted to T€ 10,671 and T€ 12,018 in 2003 and 2002, respectively. The estimated aggregate amount of amortisation of developed technologies and customer list is as follows:

T€	
2004	9,163
2005	6,873
2006	–
Thereafter	–
Total	**16,036**

All goodwill of the Company has been allocated to the discovery and development services segment. The Company has tested its discovery and development services segment for impairment on the annual designated test date of 31 October 2003. As a result of that test, the Company concluded that the carrying value of goodwill was not impaired, leaving a balance at 31 December 2003 of T€ 96,418. The fair values of the Company's reporting units Discovery Chemistry Services, Biology Services, Development Chemistry and the Pilot Plant, which all belong to the discovery and development services segment, were estimated using established valuation tech-

niques, specifically the discounting of estimated future cash flows. We also considered our market capitalisation on the dates of our impairment tests under SFAS 142 in determining the fair value of the respective businesses.

(10) Long-Term Loans

In February 1998, the Company entered into a T€ 5,113 loan agreement with a bank of which T€ 1,917 is still outstanding. This loan carries a fixed interest rate of 5% per annum and is repayable in semi-annual instalments of T€ 320 ending on 30 September 2006. This loan is secured by certain patents, receivables and equipment. In July 2002, the Company entered into a T€ 5,000 loan agreement with a bank of which T€ 4,700 is used and outstanding. This loan carries a fixed interest rate of 5.84% per annum, which is fixed until 30 June 2007 and is to be repaid in monthly instalments of T€ 96.5, starting one month from the day of full exercise of the loan. The first maturity date of the loan could be 30 June 2007. The repayment is included accordingly in the maturity table below. This loan is secured by certain fixed assets.
On 4 February 2003 the Company entered into a loan with another bank of T€ 2,937 secured by a charge on buildings and chattels in the UK of which T€ 2,622 is still outstanding. The loan is repayable in equal instalments over a period of five years. A further loan facility of T€ 5,667 was agreed on the same date secured on trade accounts receivable and funds deposited at the bank. An amount of T€ 2,479 had been drawn down from this facility as of 31 December 2003. This loan is repayable in full by 28 February 2006 or in instalments before that date and is subject to covenants being fulfilled. At the year end 2003 there were no restrictions of use over the funds on deposit as all the requirements of the loan covenants have been met. Failure to have met all the covenant requirements may place restrictions on funds deposited at the bank.
ProPharma Ltd., a subsidiary of the Company has debt of T€ 630. It is repayable in instalments through 2007 and secured by all of that subsidiary's assets. This agreement contains typical debt covenants which are related to government grants in the amount of T€ 44. The Company is in compliance with all debt covenants at 31 December 2003. Current year maturities include an overdraft in ProPharma of T€ 484. This overdraft is secured by a bond and floating charge over all of ProPharma's assets dated 20 January 2000, assignations of Zurich life assurance policies on the lives of two directors and a letter of security from a Bank, which is contingent upon a T€ 425 deposit at this bank.

The annual maturities of these debts are as follows:

T€	
2004	1,590
2005	1,106
2006	3,586
2007	5,124
2008	942
Thereafter	–
Total	**12,348**

The Company maintains lines of credit totalling T€ 5,900 to finance its short-term capital requirements, of which the entire balance is available as of 31 December 2003. These lines of credit provide for borrowings at various interest rates and have various expiration dates between 2004 and 2008 as well as no stated expiration date.

(11) Capital Lease Obligations

If leased assets are capitalised within fixed assets, the Company recognises the present value of the liabilities from the capital leases as financial obligations at lease inception.
The future minimum lease payments under capital leases are as follows:

T€	
2004	703
2005	605
2006	595
2007	533
2008	159
Less interest	(203)
Total principal payable on capital leases	**2,392**

(12) Accrued Liabilities

The accrued liabilities consist of the following:

T€	31|12|2003	31|12|2002
Accrued outstanding invoices	2,430	1,558
Bonus accruals	2,003	1,527
Other accrued liabilities	2,436	1,641
Total accrued liabilities	**6,869**	**4,726**

The change of accrued liabilities is primarily due to the inclusion of T€ 1,073 in respect of building retentions in Abingdon held at the year end. The associated costs in relation to these accruals have been included in the cost of fixed asset additions. Additionally an amount of T€ 198

was included for rent and rates following the occupation of new premises at Milton Park, Abingdon. Furthermore, the bonus accruals were increased due to the Management's decision to bring the variable component of compensation back to 2001 level.

(13) Income Taxes

Loss before income taxes, minority interests and net loss from equity investments is attributable to the following geographic regions for the years ended 31 December 2003 and 2002:

T€	2003	2002
Germany	(10,135)	(18,720)
Foreign	(5,430)	(115,617)
Total	**(15,565)**	**(134,337)**

Income tax benefit (expense) for the years ended 31 December 2003 and 2002 is as follows:

T€	2003	2002
Current taxes:		
– Germany	–	–
– Foreign	(361)	(173)
Total current taxes	**(361)**	**(173)**
Deferred taxes:		
– Germany	–	–
– Foreign	3,186	2,928
Total deferred taxes	**3,186**	**2,928**
Total income tax benefit	**2,825**	**2,755**

The tax rate in the UK for the years ended 31 December 2003 and 2002, amounted to 30%. For the years ended 31 December 2003 and 2002, the actual income tax benefit differed from the amounts determined using the combined German federal corporation income and trade tax rate of 40.38% (2002: 40.38%) as follows:

T€	2003	2002
Expected income tax benefit	6,624	54,245
Non-deductible goodwill impairment and amortisation	–	(44,171)
Other permanent differences	1,266	891
Foreign tax differential	(525)	(646)
Effect of tax rate change	(44)	–
Change in valuation allowance	(4,756)	(7,305)
Other	260	(259)
Actual income tax benefit	**2,825**	**2,755**

Deferred income tax assets and liabilities as of 31 December 2003 and 2002 relate to the following:

T€	2003	2002
Deferred tax assets:		
– Loss carry forward	43,297	37,146
– Intangible assets	1,957	2,277
– Other	245	129
Total	**45,499**	**39,552**
Valuation allowances on deferred tax assets	(36,645)	(31,889)
Total deferred tax assets	**8,854**	**7,663**
Deferred tax liabilities:		
– Property, plant and equipment	14,928	14,117
– Intangible assets	5,013	8,891
– Undistributed subsidiaries earnings	146	146
– Other	20	8
Total deferred tax liabilities	**20,107**	**23,162**
Deferred tax liability, net	**11,253**	**15,499**

In 2002, the Company recognised tax benefits in the amount of T€ 1,433 which were credited to goodwill because of a change in circumstances that caused a revaluation of the realisability of tax loss carry forwards for the subsidiaries of the Company, Evotec OAI Ltd and ProPharma Ltd.

Net deferred income tax assets and liabilities are presented in the accompanying balance sheets as of 31 December 2003 and 2002 as follows:

T€	2003	2002
Net deferred tax assets, current:		
– Germany	–	–
– Foreign	76	45
Net deferred tax liabilities, non-current:		
– Germany	–	–
– Foreign	(11,329)	(15,544)
Total	**(11,253)**	**(15,499)**

For the years ended 31 December 2003 and 2002, Evotec recorded additional valuation allowances with respect to tax benefits of tax loss carry forwards T€ 4,604 and T€ 4,883, respectively. The valuation allowances on the Company's deferred tax assets are not recorded to the extent it is considered more likely than not that such tax benefits would be realised in future years. These considerations include, but are not limited to, the ability under respective tax laws to carry forward incurred tax losses indefinitely and thereby offset taxable income in future years, tax planning strategies and estimates of future taxable income. Evotec has not generated taxable income in Germany since the start of operations and does not expect to in the foreseeable future. The rational be-

hind the valuation allowances is based on the potentially unlikely prospect of generating taxable income and, to a significant extent, the questionable nature, availability and benefit of the tax loss carry forwards generated prior to the completion of the initial public offering in 1999 and the acquisition of the UK subsidiaries in 2000. Tax loss carry forwards for Germany of T€ 85,815 and the UK of T€ 29,534 do not expire. Due to changes in the German tax law in 2003, the tax loss carry forwards can only be offset against an amount of 60% of future taxable income after exceeding a fully deductible amount of T€ 1,000 per year.

In determining the allowance, income tax expense for 2003 and 2002 was allocated entirely to continuing operations, with nothing allocated to accumulated other comprehensive loss on the basis that a valuation allowance is established on the net deferred tax asset positions in Germany.

(14) Stock-Based Compensation

The shareholders' meeting on 7 June 1999 established a stock option plan and authorised the granting of stock options for up to 1,466,600 shares. The plan is subject to certain restrictions regarding the number of stock awards that may be granted in a year and the allocation of the grants to members of the Management Board, other key management personnel and all other employees. In connection with the acquisition of OAI in 2000 and the increased number of employees, the shareholders approved an additional 949,000 shares which may be issued in connection with the granting of stock options. In 2001, the annual shareholders' meeting provided for the authorisation of an additional 1,129,600 stock options.

Under the terms of the plan, each option entitles the holder to purchase one share of the Company's stock within ten years of the grant date at a set strike price. For all options granted in 1999, the strike price was the price of the initial public offering of € 13.00 (€ 6.50 after stock split). Options granted in 2000 and thereafter can be exercised at a strike price equal to the closing price of the shares or at a strike price equal to the closing price of the shares plus 5% on the trading day before the option was granted. Options have a graded vesting: a maximum of one-third of which can be exercised at the earliest after two years, a maximum of two-thirds after three years and all remaining awarded options after four years. Options can only be exercised within certain specified two week periods starting on the third day after one of the following events:

(i) release of the quarterly results,
(ii) annual press conference on the financial statements, or
(iii) annual shareholders' meeting of the Company.

The options can only be exercised if the stock price exceeds the strike price by at least 5%.

The Company deems the 5% stock price increase probable at the grant date, thereby giving the variable plan a fixed character.

The terms of the stock option plan provides that for a further granting of options the price of the Company's stock should increase by at least 30% compared to the average closing price of the stock during the last quarter of the year preceding the year of the date of any subsequent grant. The Supervisory Board, however, has the authority to override this restriction and to authorise the granting of options to employees if such a decision is considered necessary for the interests of the Company.

A summary of the status of the plan as of 31 December 2003 and 2002, and the changes during the years then ended is presented as follows:

pcs. and € per share	2003		2002	
	Options	Weighted average exercise price	Options	Weighted average exercise price
Outstanding at beginning of the year	2,129,526	10.31	1,666,451	13.53
Options granted	523,400	5.84	616,868	2.27
Options exercised	–	–	(3,083)	6.50
Options forfeited	(113,750)	10.71	(150,710)	13.10
Options waived (re-issueable)	(65,000)	12.76	–	–
Outstanding at end of the year	2,474,176	9.30	2,129,526	10.31
Thereof exercisable	784,535	14.60	320,279	16.53

A summary of the stock options outstanding at 31 December 2003 is as follows:

	Outstanding in pcs.	Exercisable in pcs.	Weighted average remaining contractual life in years	Weighted average exercise price € per share
Exercise price 1.66 € – 2.31 € per share	617,688	–	8.91	2.24
Exercise price 5.50 € – 6.80 € per share	1,255,173	408,344	8.20	6.53
Exercise price 10.15 € –12.48 € per share	95,500	32,137	7.94	12.38
Exercise price 15.29 € per share	4,500	1,500	7.23	15.29
Exercise price 24.30 € per share	501,315	342,554	6.90	24.30

Evotec's stock option plan results in compensation expense when Evotec's stock price exceeds the strike price subsequent to the issuance of the options. Total compensation costs of T€ 76 and T€ 34 were determined at the measurement dates of the granted options in 2003 and 2002, respectively. These amounts were reflected in unearned compensation, a component of stockholders' equity. The Company recognised compensation expense in 2003 and 2002 for all options totalling T€ 271 and T€ 324, respectively, which was reflected as operating costs and expenses in the consolidated statements of operations.

The fair value of each option grant was estimated on the date of grant for the fiscal years ended 31 December 2003 and 2002 using a Black-Scholes option pricing model with the following weighted average assumptions:

	2003	2002
Risk-free interest rate	4.0%	4.2%
Volatility	75.6%	104.5%
Dividend yield	–	–
Average expected life	3 years	3 years
Options expected to be exercised	74.7%	70.0%

The weighted average fair value of each option granted during the year ended 31 December 2003 and 2002 was € 0.70 and € 0.37, respectively.

(15) Stockholders' Equity

On 31 December 2003, authorised but unissued shares consist of a conditional capital (bedingtes Kapital) of 3,487,218 shares available with respect to the stock option plan and an approved capital (genehmigtes Kapital), as decided upon at the annual general meeting in 2001, of 17,700,000 shares. On 31 December 2003, there are 35,510,130 shares issued and outstanding.

On 11 April 2002, the Company issued 3,083 new shares to its employees in connection with the exercise of stock options pursuant to the existing stock option plan. The price per share paid was € 6.50.

The annual shareholders' meeting on 18 June 2001 authorised the Management Board of the Company to issue up to 17,700,000 shares for cash or contributions in kind. Under German law, the shareholders of a stock corporation may empower the Management Board to issue shares in a specified aggregate nominal value not exceeding 50% of the issued share capital at the time of the shareholder vote, in the form of approved capital (genehmigtes Kapital). The authorisation expires five years after the date of the shareholders' resolution.

(16) Segment Information

The Company's operations include three reportable operating segments which are: (i) Tools and Technologies, (ii) Discovery and Development Services and (iii) Discovery Programs Division.

(i) The Tools and Technologies segment collaborates with pharmaceutical companies to develop its platform technology and to design, manufacture, assemble and deliver instruments and disposables for its drug discovery systems. Tools and Technologies conducts research and development activities with collaborative and strategic partners in the pharmaceutical or diagnostic industry to develop new technologies and enhance the screening systems resulting from those contracts.

(ii) The Discovery and Development Services segment enters into service contracts with third parties to provide screening, assay development, chemical compound optimisation and production and disease targets. The total business activities of the UK are included in this second segment.

(iii) The Discovery Programs Division segment is engaged in selected discovery activities to develop compounds for out-licensing. The strategic objective of this division is to generate proprietary intellectual property that can provide the Company with additional long-term upside through more significant milestones and royalties. Discovery Programs Division utilise group synergies by contracting its discovery research to the Discovery and Development Services segment at arms length.

The Company makes decisions about resources to be allocated to the segments and assesses their performance using revenues and gross profits. Evotec does not identify or allocate assets to the operating segments nor does the Company evaluate the segments on these criteria. Net sales and operating expenses in the segment's include both sales to customers and inter-segment transfers, which are priced to recover cost plus an appropriate profit margin according to the at arms length principle.

Revenues in the consolidated statements of operations are differentiated by products and by services. This definition is close to the definition used in the segment reporting. Differences between the revenue splits are mainly due to product deliveries from our service unit, which are reported in services in the segment reporting. The accounting policies of the segments are the same as those described in the summary of significant accounting policies (see note 2).

The following represents segment data, revenues and gross profit, for the years ended 31 December 2003 and 2002:

T€	2003	2002
Revenues:		
– Discovery and Development Services	61,214	58,588
– Tools and Technologies	18,668	11,407
– Discovery Programs Division	1,479	–
– Consolidation	(4,133)	–
Total revenues	**77,228**	**69,995**
Costs of revenue:		
– Discovery and Development Services	37,254	34,763
– Tools and Technologies	10,503	3,768
– Discovery Programs Division	655	–
– Consolidation	(2,219)	–
Total costs of revenue	**46,193**	**38,531**
Gross profit:		
– Discovery and Development Services	23,960	23,825
– Tools and Technologies	8,165	7,639
– Discovery Programs Division	824	–
– Consolidation	(1,914)	–
Total gross profit	**31,035**	**31,464**

The following represents segment data, revenues, gross profit and operating loss from continuing operations, for the year ended 31 December 2003:

T€	Discovery and Development Services	Tools and Technologies	Discovery Programs Division	Consolidation	Total 2003
Revenues:					
– Drug discovery products and Technologies	41	18,668	–	(1,486)	17,223
– Drug discovery services	61,173	-	1,479	(2,647)	60,005
Total revenues	**61,214**	**18,668**	**1,479**	**(4,133)**	**77,228**
Costs of revenue:					
– Drug discovery products and Technologies	–	10,503	–	(551)	9,952
– Drug discovery services	37,254	–	655	(1,668)	36,241
Total costs of revenue	**37,254**	**10,503**	**655**	**(2,219)**	**46,193**
Gross profit	23,960	8,165	824	(1,914)	31,035
Research and development expenses	8,112	5,043	4,324	(2,013)	15,466
Selling, general and administrative expenses	13,088	3,283	1,801	(248)	17,924
Amortisation of intangible assets	10,431	979	55	(794)	10,671
Impairment of goodwill	–	–	–	–	–
Other operating expenses	2,751	–	–	–	2,751
Operating loss	**10,422**	**1,140**	**5,356**	**(1,141)**	**15,777**

Depreciation including allowances, included in the operating loss of Discovery and Development Services, Tools and Technologies and Discovery Programs Division, amounts to T€ 9,319, T€ 1,030 and T€ 425, respectively. Revenues can be split into the following product and service lines:

T€	2003	2002
Biology Services	10,603	6,105
Chemical Discovery	31,666	33,894
Chemical Development	18,945	18,589
Discovery and Development Services	**61,214**	**58,588**
Discovery Programs Division	1,479	–
Technology development		
and transfer agreements	–	4,777
Evotec Technologies	18,668	6,630
Tools and Technologies	**18,668**	**11,407**
Consolidation	(4,133)	–
Total revenues	**77,228**	**69,995**

Revenues can be split, based on customers' locations, in the following geographical regions:

%	2003	2002
Germany	6	6
United Kingdom	20	16
Rest of Europe	23	27
United States	46	47
Rest of the world	5	4
	100	100

Long-lived assets of T€ 165,150 and T€ 181,078 are located in UK, and the remaining amounts of T€ 12,777 and T€ 13,932 are in Germany as of 31 December 2003 and 2002, respectively.

(17) Financial Instruments

The fair value of cash and cash equivalents, trade accounts receivable and trade accounts payable approximate their carrying values in the consolidated financial statements due to the short-term nature. The fair value of debt is determined on the basis of discounted cash flows using an appropriate discount rate. The fair values of long-term loans closely approximates their carrying values on 31 December 2003 and 2002. Marketable securities are carried at their quoted market price which represents their fair value.

The Company periodically enters into derivatives including foreign currency forward contracts and options. The objective of these transactions is to reduce the risk of exchange rate fluctuations of its foreign currency denominated cash flows. Evotec does not enter into derivatives for trading or speculative purposes. As of 31 December 2003, the Company held U.S. dollar option contracts with Euro equivalent notional amounts of approximately T€ 8,500 and T€ 11,449 as of 31 December 2003 and 2002, respectively. The fair value of the option contracts is T€ 8,552 at 31 December 2003 (2002: T€ 167). Foreign currency contracts are carried at fair value which is determined using quoted market prices or discounted cash flows. The carrying amount of the foreign currency contracts is included in prepaid expense and other current assets. Gains related to foreign currency derivatives are included in other non-operating income and amounted to T€ 459 and T€ 286 for the years ended 31 December 2003 and 2002, respectively.

(18) Risks

Credit risks of the Company consist primarily with respect to trade accounts receivable. Concentrations of credit risks with respect to trade accounts receivable are limited by a number of geographically diverse customers and the Company's monitoring procedures.

We expect that our current cash funds, together with operating revenues will be sufficient to finance our operations for at least one to three years, depending on the various scenarios of the Company's investments and strategic development. Our future cash requirements will depend on various factors, including our success in developing existing and new technologies and products, increasing sales of both existing and new products and services, expenses associated with growth as well as competition and overall market development. Moreover, in order to remain competitive, Evotec will continue to make substantial investments in research and development which may require additional financing. However, significant commitments for any funding requirements would not be entered into without secured financing.

The Company has important collaborations with pharmaceutical companies within all operating segments. Any termination of such collaborations would probably have adverse impacts on the Company's financial position, results of operations and cash flows.

The Company has two customers in the Discovery and Development Services segment as well as in the Tools and Technologies segment with more than 30% combined revenues of the group revenues. A termination of this contracts could have adverse impacts on the Company's financial results.

Foreign exchange risk of the Company stems from our exposure to the GBP with respect to the UK subsidiaries as well as to the USD. Whilst a significant weakening of the USD | GBP has occurred this year, any further weakening will reduce reported revenues. The hedging activities of the Company aim to mitigate the impact on the result before tax.

(19) Pension Plan

The Company operates a defined contribution Group Personal Pension Plan (GPPP) and makes contributions to employees' own schemes. The pension charge for the year represents contributions payable by the Company to the fund (and to employees' own pension schemes) and amounted to T€ 594 (2002: T€ 513).
Contributions amounting to T€ 103 (2002: T€ 77) were payable to the fund managers at the year and are included in creditors.
The Company's contribution rate is determined by the employees contribution and their age. There were no changes in the basis for such contributions during the year. The Company's disclosure for its pension and other post-retirement plans are in compliance with FAS 132, Employers' Disclosures about Pensions and Other Post-Retirement Benefits.

(20) Commitments and Contingencies

(a) Operating Leases. The Company leases office space and other equipment under operating leases. The future minimum lease payments under non-cancellable operating leases are approximately as follows:

T€	
2004	4,296
2005	4,264
2006	3,942
2007	3,895
2008	3,728
Thereafter	24,623
Total	**44,748**

The majority of operating leases is related to rent expenses for facilities. The rent expense for such leases amounted to T€ 3,021 and T€ 3,336 for the years ended 31 December 2003 and 2002, respectively. Rental income under sub-lease agreements in the UK amounts to T€ 0 and T€ 30 for the years ended 31 December 2003 and 2002, respectively. The rental income over the next five years is expected to be immaterial.

(b) Other Commitments and Contingencies. The Company has entered into long-term consultant contracts. During 2003 and 2002, payments under consultant contracts totalled T€ 543 and T€ 366, respectively. The future minimum payments associated with long-term consultant and other miscellaneous long-term commitments totals approximately T€ 1,471 and T€ 2,083 at 31 December 2003 and 2002, respectively.
As discussed in note 3, the Company has certain commitments resulting from the amendments to our agreements with our technology funding partners.
The Company has given a guaranty with regard to all terms and conditions of a specific customer contract. No current liabilities from that guaranty exist at 31 December 2003.
The Company is not aware of any significant litigation as of 31 December 2003.

(c) Product Warranties. The warranties of the Company are issued by the Tools and Technology segment. They are usually accompanied by a twelve month warranty for systems and devices delivered to customers. These warranties cover factors such as non-conformance to specifications and defects in material.
Estimated warranty costs are recorded in the period in which the related product sales occur. The warranty liability recorded at each balance sheet date reflects the estimated average of historical yearly warranty payments. The following table summarises product warranties recorded during 2003.

T€	01 | 01 | 2003	2003 net change	31 | 12 | 2003
Product warranties	468	(26)	442

(21) Related Party Transactions

The following Supervisory Board members of the Company are also supervisory board members or management board members in companies Evotec works with in the ordinary course of business:
Prof Dr Heinz Riesenhuber is a member of the supervisory board of Altana Pharma AG, with whom the Company entered into a service agreement in the ordinary course of business. Revenue from this agreement in 2003 and 2002 amounted to T€ 84 and T€ 975, respectively. Accounts receivable from Altana as of 31 December 2003 and 2002 amount to T€ 0 and T€ 232, respectively.

Peer Schatz is a managing director of Qiagen NV. From affiliates controlled by Qiagen NV the Company bought products in the amount of T€ 215 and T€ 45 in 2003 and 2002, respectively. The amount of payables to Qiagen on 31 December 2003 and 2002, including VAT amounts to T€ 5 and T€ 2, respectively.
Dr Pol Bamelis is a member of the supervisory board of Innogenetics N.V. from whom the Company bought raw materials in the ordinary course of business in the amount of T€ 1 and T€ 2 in 2003 and 2002, respectively. The amount of payables to Innogenetics as of 31 December 2003 and 2002, including VAT amounts to T€ 0 and T€ 1, respectively. The Company also entered into a service agreement with Innogenetics N.V. in the ordinary course of business. Revenues from this agreement in 2003 amounted to T€ 6. Accounts receivable from Innogenetics as of 31 December 2003 amount to T€ 2. Dr Bamelis is also a member of the supervisory board of MediGene AG with whom the Company entered into a service agreement in 2002 which resulted in revenues of T€ 256 and T€ 647 in 2003 and 2002, respectively.
Dr Karsten Henco is a member of the supervisory board of NewLab BioQuality AG with whom the Company entered into a rental agreement for laboratory space in the ordinary course of business. Rental expenses amounted to T€ 16 and T€ 176 in 2003 and 2002, respectively. He is also a member of the Kuratorium of the Fraunhofer Institut für biomedizinische Technik, St. Ingbert with whom the Company entered into a scientific research cooperation agreement. The expenses in 2003 and 2002 amounted to T€ 283 and T€ 263, respectively, related payables to the Fraunhofer Institut as of 31 December 2003 and 2002 amounted to T€ 0 and T€ 4, respectively. The revenues in 2003 with Fraunhofer Institut amounted to T€ 74, related receivables as of 31 December 2003 amounted to T€ 0. Dr Henco is also a member of the supervisory board of Garching Innovation GmbH from which the Company has obtained licences in 2001. Licence expense amounted to T€ 88 and T€ 88 in 2003 and 2002, respectively. The Company entered into a consultancy contract, in the ordinary course of business and with the approval of the Supervisory Board, with Dr Karsten Henco in order to exploit his significant expertise in the business and industry of the Company. The associated expenses in 2003 and 2002 amounted to T€ 170 and T€ 172, respectively and the related payables to Dr Henco as of 31 December 2003 and 2002 amounted to T€ 27 and T€ 52, respectively.
Dr Edwin Moses was a member of the supervisory board of Prolysis Ltd until June 2003 with whom the Company entered into a service agreement and acquired a 3.88% equity interest. The related revenues associated with the service agreement amounted to T€ 1,747 and T€ 1,018 in 2003 and 2002, respectively and the related accounts receivable as of 31 December 2003 and 2002 amounted to T€ 466 and T€ 504, respectively. He is also a member of the supervisory boards of BioImage A|S and Ionix Ltd. with whom the Company entered into service agreements in the ordinary course of business. Revenues amounted to T€ 575 and T€ 0 in 2003, respectively, and to T€ 37 and T€ 367 in 2002, respectively, and the related accounts receivable as of 31 December 2003 amounted to T€ 38 and T€ 0, respectively, and as of 31 December 2002 amounted to T€ 17 and T€ 0, respectively.
Dr Michael Redmond is chairman of the supervisory board of Microscience Ltd. with whom the Company founded Vmax Ltd.
Dr Phil Boyd, an officer of the Company is a member of the board of Vmax Ltd. with whom the Company entered into a loan stock and investment agreement. See note 7.

(22) Other Disclosures

The following additional disclosures are required by German law in accordance with the European Directives on Accounting and the Corporate Governance Codex:

(a) Number of Employees. The average number of persons employed by the Company in 2003 was 646 (2002: 619).

(b) Personnel Expenses and Cost of Material. The personnel expenses of the Company amounted to T€ 36,364 of which T€ 21,516 relates to personnel expenses in the UK (2002: T€ 35,768 and T€ 20,009, respectively).
Cost of materials amounted to T€ 24,829, thereof T€ 7,173 are cost of materials in the UK (2002: T€ 18,505 and T€ 8,027, respectively).

(c) Corporate Governance Codex. A declaration according to § 161 AktG was made by the Management Board and the Supervisory Board of the Company. This declaration regarding the Company's compliance with the Corporate Governance Codex is accessible to the shareholders on Evotec's website.

(d) Consolidated Subsidiaries and Equity Investees. Information below is as per the statutory financial statements prepared in accordance with the respective local generally accepted accounting principles.
In 2003, Evotec Technologies GmbH incorporated Evotec Technolgies Inc. as a 100% subsidiary in the U.S.| Delaware. This new entity will act as a sales agent for Evotec Technologies GmbH and, in addition, perform services and maintenance in the U.S. market.
In 2003, Evotec OAI AG has transferred its shares in EVOTEC NeuroSciences GmbH to ENS Holdings Inc. incorporated in Delaware | USA. As of 31 December 2003, Evotec OAI AG holds 84.7% of that new company.

	Company's voting interest in %	2003 Net income	(loss) in T€	2003 Equity in T€
Subsidiaries (verbundene Unternehmen)			
– Evotec OAI Ltd., Abingdon	UK	100.0	4,310	55,393
– Evotec Technologies GmbH, Duesseldorf	D	86.1	(490)	(349)
– Evotec Technologies Inc., Delaware	USA (unaudited)	86.1	–	–
– EVOTEC NeuroSciences GmbH, Hamburg	D (unaudited)	84.7	(2,972)	(2,097)
– ENS Holdings Inc., Delaware	USA (unaudited)	84.7	–	–
– ProPharma Ltd, Glasgow	UK	61.0	34	1,367
– Evotec OAI Inc., Delaware	USA (unaudited)	100.0	16	100
– Oxford Diversity Ltd., Abingdon	UK (unaudited)	100.0	–	–
– Oxford Asymmetry Employee Shares Trust Ltd., Abingdon	UK (unaudited)	100.0	–	–
Investees (assoziierte Unternehmen)				
DIREVO Biotech AG, Cologne	D (unaudited)	22.7	(2,689)	12,917
SiREEN AG, Munich	D	6.4	(2,725)	497
Vmax Ltd., Winnersh Triangle	UK (unaudited)	46.4	(330)	(51)
Prolysis Ltd., Oxford	UK (2002 figures)	3.9	(2,223)	4,315
DeveloGen joint venture		50.0	–	–

(e) Management Board. The members of the Management Board are listed at the end of this report.
The remuneration paid to the members of the Management Board in the financial year totalled T€ 1,229 (2002: T€ 1,249) of which T€ 163 (2002: T€ 183) was variable. The variable pay for the Management Board is based on a bonus scheme designed by the Remuneration Committee, which is composed on entirely non management board members of the supervisory board, and is then approved by the Supervisory Board. The variable portion of the remuneration in 2003 for the business year 2002 is based on a performance related bonus split into three parts; 20% is based on the achievement of a revenue target, 20% on an EBITDA target and 60% on the achievement of personal objectives. In the case of the C.E.O. these percentages are 30, 30 and 40, respectively. The scheme will be the same as in 2003 for the variable portion of the remuneration in 2004, which is based on the business year 2003. Under the Company's stock option plan, the members of the Management Board received in 2003 152,000 (2002: 130,000) options of which one-third may be exercised after two years.

	Fixed remuneration	Variable remuneration	Stock options
	T€	T€	pcs.
Joern Aldag	279	47	27,000
Dr Dirk Ehlers	248	39	15,000
Dr Ian Hunneyball	261	39	55,000
Dr Timm Jessen	219	35	15,000
Bernard Questier	62	–	40,000
Total	**1,069**	**160**	**152,000**

Joern Aldag was member of the supervisory board of LION Biosciences AG, Heidelberg (until August 2003) and is member of the Monopolkommission der Bundesrepublik Deutschland.
Timm Jessen is member of the supervisory board of ascenion GmbH, Munich (from July 2003).

(f) Supervisory Board. The members of the Supervisory Board and their additional memberships in supervisory boards and memberships incomparable governing bodies of enterprisees according to § 125 (1) third sentence of the AktG are listed at the end of this report.
The remuneration paid to the members of the Supervisory Board in the financial year amounted to T€ 30 for Prof Dr Riesenhuber, T€ 22.5 for Peer Schatz, and T€ 15 each for Dr Pol Bamelis, Dr Karsten Henco, Dr Edwin Moses and Michael Redmond. The remuneration for the chairman of the Supervisory Board is twice, for the vice chairman is one and a half the amount of the remuneration for the Supervisory Board members. The total remuneration paid to Supervisory Board members totalled T€ 112.5 (2002: T€ 112.5).

(g) Scientific Advisory Committee. The Company is currently in the process of restructuring its Scientific Advisory Board according to the Company's advanced strategy.

(h) Summary of Significant Differences between U.S. GAAP and HGB Accounting Requirements

Introduction. Evotec OAI AG, as a German company, is subject to the German Commercial Code ("Handelsgesetzbuch", or "HGB"), which principally requires the Company to prepare consolidated financial statements in accordance with the HGB accounting principles and regulations ("German GAAP"). Pursuant to HGB Section 292a, the Company is exempt from this requirement if consolidated financial statements are prepared and issued in accordance with a body of internationally accepted accounting principles (such as U.S. GAAP). Accordingly, the Company has prepared its consolidated financial statements in accordance with U.S. GAAP. The following is a description of the significant differences between German GAAP and U.S. GAAP.

Fundamental Differences. The emphasis of U.S. GAAP is to provide all relevant information to investors in order to facilitate future investment decisions. The primary difference between German GAAP and U.S. GAAP is that they are based on different concepts. German GAAP is oriented towards the protection of creditors and emphasis on the prudence concept.

Financial Statement Presentation. The balance sheet presentation under U.S. GAAP is based on the planned realisation of assets and the maturity of liabilities in the normal course of business. The balance sheet under German GAAP is principally defined in HGB section 266 and is based on enterprise's planned holding time for the respective asset, liability or equity.

Status Report and Fixed Asset Movement Schedule. According to HGB companies have the obligation to disclose a status report and a fixed asset movement schedule. U.S. GAAP requires from public traded companies a disclosure of a Management Discussion and Analysis (MD&A) which differs from the status report in contents and scope. The disclosure of a fixed asset movement schedule is not required by U.S. GAAP.

Revenue Recognition. Revenue recognition is generally the same under German and U.S. GAAP, whereby revenue is recognised when realised and earned. Differences in the timing of recognition can exist in transaction when the Company retains on-going financial, operational or performance commitments or the contractual amounts are not objectively verifiable.

Marketable Securities. Under German GAAP, marketable debt and equity securities are valued at the lower of acquisition cost or fair market value as of the balance sheet date. Under U.S. GAAP, the Company's marketable securities are classified as available-for-sale and valued at fair market value as of balance sheet date. Unrealised gains and losses are reported in other comprehensive income, net of deferred taxes.

Inventories. Inventory valuation is based on manufacturing cost under both German and U.S. GAAP. Manufacturing costs under U.S. GAAP, however, are defined as production costs on a full absorption basis, whereby manufacturing overhead is included together with material and other direct manufacturing costs.

Goodwill. Under U.S. GAAP, pursuant to SFAS No. 141, "Business Combinations", in connection with SFAS No. 142, "Goodwill and Other Intangible Assets", goodwill arising from business combinations accounted for as a purchase is no longer amortised but is reviewed for impairment once a year.

Financial Instruments. Under German GAAP, derivative financial instruments are not recorded on the balance sheet. Unrealised gains are not recognised and unrealised losses are accrued. Under U.S. GAAP, derivative financial instruments are recorded on the balance sheet at their fair value. Changes in fair value are recorded in current earnings or other comprehensive income, depending on whether the derivative financial instruments are designated as part of a hedge transaction and depending on the type of hedge transaction.

Stock-Based Compensation. Under German GAAP, the Company recognises the difference between the fair market value of the Evotec shares and the exercise price of the stock options as expense, if the fair market value is higher. Under U.S. GAAP, the Company accounts for stock-based compensation on the intrinsic value method pursuant to APB Opinion No. 25.

Accrued Liabilities. Under German GAAP, certain costs can be accrued for anticipated future events in certain circumstances. Under U.S. GAAP, recognition of an accrued liability represents an existing liability to third parties or must meet specific recognition criteria.

Foreign Currency Translation. Under German GAAP, foreign currency denominated assets and liabilities are recorded at spot rate on the transaction date with only unrealised losses reflected in income at the balance sheet date. Under U.S. GAAP, foreign currency denominated assets and liabilities are translated at the spot rate at the balance sheet date, with both unrealised gains and losses reflected in income.

Report of the Supervisory Board

The key task of the Evotec OAI Supervisory Board is to regularly advise and supervise the Evotec OAI Management Board in the management of the enterprise.

During the year 2003, the Supervisory Board convened for five formal meetings and held one telephone conference to discuss the operational and strategic development of Evotec OAI AG. In addition, the Supervisory Board discussed important issues in three telephone calls and approved one separate management decision through written circulation. The Audit committee met separately in four additional teleconferences, the Remuneration Committee convened twice. The Management Board continuously provided updates to the Supervisory Board through regular verbal and written reports that included information on the status of operations. Furthermore the Chairman of the Supervisory Board and the Chief Executive Officer discussed ongoing and current topics on the telephone regularly, typically every two weeks, and whenever appropriate.

In addition to business updates and other standard agenda items, the Supervisory Board discussed at its meetings the following specific subjects in detail:

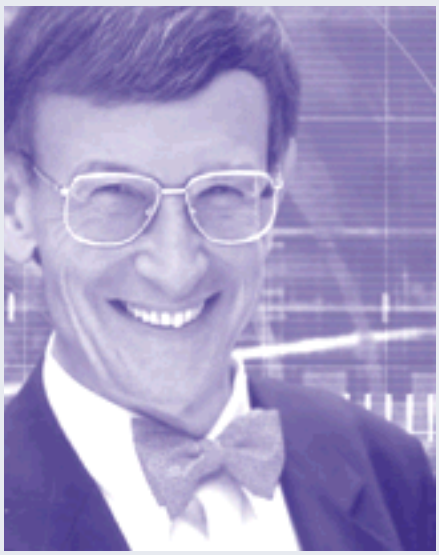
> In March, the Board discussed the 2002 annual financial statements in presence of the auditors.
> In April, the Board discussed company strategy in depth.
> In May, the Board focused on R&D and the Discovery Programs Division and prepared for the Annual General Meeting.
> At its telephone conference in July, the Board discussed a specific project within the Discovery Programs Division.
> In August, the Board reviewed the financial forecast for the year 2003.
> In November, the Board focused on the budget for the year 2004.

The financial statements and the management report of Evotec OAI AG for the year 2003, as well as the consolidated financial statements together with the consolidated management report of the Evotec OAI Group, were audited by KPMG Deutsche Treuhandgesellschaft Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Hamburg. The auditors issued an unqualified audit opinion. They gave a comprehensive report on the audit and their observations at the Supervisory Board Meeting on 11 March 2004. The Supervisory Board examined and approved both the financial statements and the consolidated financial statements prepared by the Management Board.

The Supervisory Board appointed Bernard Questier member of the Management Board and Chief Business Officer effective 6 October 2003.

The Supervisory Board thanks the Management Board and the Company's employees for their hard and successful work during the year and wishes them continued success for 2004.

Hamburg, 11 March 2004



Chairman of the Supervisory Board
Prof Dr Heinz Riesenhuber

Supervisory Board

Prof Dr Heinz Riesenhuber Chemist, Frankfurt am Main	D	**Chairman of the Supervisory Board**	**Member of the Supervisory Board:** Altana AG, Bad Homburg	D Frankfurter Allgemeine Zeitung, Frankfurt am Main	D Henkel KGaA, Duesseldorf	D InSynCo AG, Hamburg	D (from February 2003) Osram GmbH, Munich	D VfW AG, Cologne	D (from June 2003) Vodafone GmbH, Duesseldorf	D Portum AG, Frankfurt am Main	D (until September 2003) **Member of the Investorenbeirat:** Heidelberg Innovation BioScience Venture II GmbH & Co. KG, Heidelberg	D **Member of the Verwaltungsrat:** HBM BioVentures AG, Baar	CH
Peer Schatz Business Executive, Duesseldorf	D	**Vice Chairman of the Supervisory Board**	**Chairman of the Supervisory Board:** Qiagen S.A., Courtaboeuf Cedex	F **Member of the Supervisory Board:** GenoVision Inc, West Chester	USA (from August 2003) Mulligan BioCapital AG, Hamburg	D Qiagen AS, Oslo	N Qiagen Genomics, Inc, Bothell	USA Qiagen Inc, Mississauga	Canada (from June 2003) Qiagen Inc, Valencia	USA Qiagen K.K., Tokyo	J Qiagen Ltd, Crawly West Sussex	UK Qiagen North American Holdings, Inc, Valencia	USA Qiagen Operon, Inc, Alameda	USA Qiagen Pty Ltd, Clifton Hill, Victoria	AUS Qiagen S.p.A., Milan	I Qiagen Sciences, Inc, Germantown	USA Qiagen Sciences K.K., Tokyo	J (formerly Sawady Technology Co, Ltd, Tokyo | J) Xeragon, Inc, Germantown	USA **Member of the Beirat:** ACS Moschner & Co. GmbH, Vienna	A Venture Capital Partners KEG, Vienna	A **Member of the Boersenrat:** Frankfurter Wertpapierboerse, Frankfurt am Main	D
Dr Pol Bamelis Chemist, Knokke	B	**Member of the Supervisory Board**	**Chairman of the Supervisory Board:** Agfa-Gevaert N.V., Mortsel	B Crop Design N.V., Gent	B **Member of the Supervisory Board:** Bekaert N.V., Kortrijk	B Innogenetics N.V., Gent	B MediGene AG, Munich	D Oleon N.V., Ertvelde	B PolyTechnos (GP) II Ltd, St Peters Port, Guernsey	UK (from July 2003)
Dr Karsten Henco Biochemist, Duesseldorf	D	**Member of the Supervisory Board**	**Member of the Supervisory Board:** Direvo Biotech AG, Cologne	D (from August 2003, formerly chairman) Garching Innovation GmbH, Munich	D NewLab BioQuality AG, Erkrath	D U3 Pharma AG, Martinsried	D **Member of the Kuratorium:** Fraunhofer-Institut für Biomedizinische Technik (IBMT), St. Ingbert	D Universitätsklinikum Hamburg-Eppendorf, Hamburg	D

Dr Edwin Moses Chemist, Goring, Berkshire	UK	**Member of the Supervisory Board**	**Chairman of the Supervisory Board:** Amedis Ltd, Cambridge | UK Avantium Technologies, Amsterdam | NL BioImage A|S, Copenhagen | DK Inpharmatica Ltd, London | UK (from August 2003, formerly member) Paradigm Therapeutics Ltd, Cambridge | UK (from October 2003) ProImmune Ltd, Oxford | UK Prolysis Ltd, Oxford | UK (until June 2003) **Member of the Supervisory Board:** Ionix Ltd, Cambridge | UK Personal Chemistry AB, Uppsala | S (until October 2003)
Michael Redmond Business Executive, Bury St Edmunds | UK	**Member of the Supervisory Board**	**Chairman of the Supervisory Board:** Arakis Ltd, Cambridge | UK Dechra Pharmaceuticals plc, Stoke-on-Trent | UK Microscience Ltd, Reading | UK Synexus Ltd, Chorley | UK **Member of the Supervisory Board:** Atugen AG, Berlin | D Strakan Group Ltd, Galashiels | UK

Management Board

Joern Aldag Business Executive, Hamburg | D	**President & Chief Executive Officer**	**Member of the Supervisory Board:** LION bioscience AG, Heidelberg | D (until August 2003) **Member of the Monopolkommission der Bundesrepublik Deutschland**
Dr Dirk H. Ehlers Physicist, Wohltorf | D	**Chief Financial Officer**	
Dr Ian M. Hunneyball Biochemist, Abingdon, Oxfordshire | UK	**President, Services Division**	
Dr Timm-H. Jessen Chemist, Fleckeby | D	**Chief Scientific Officer & President, Discovery Programs Division**	**Member of the Supervisory Board:** ascenion GmbH, Munich | D (from July 2003)
Bernard Questier Chemist, Hamburg | D	**Chief Business Officer** (from 6 October 2003)	

Evotec OAI's financial calendar

25 March 2004	Annual report 2003, balance sheet press conference and analysts' meeting
12 May 2004	First quarter report 2004
01 June 2004	Annual general meeting
11 August 2004	Second quarter report 2004
11 November 2004	Third quarter report 2004

Imprint

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This annual report is also available in German.

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Lithography: Colorlux new, Verona | I

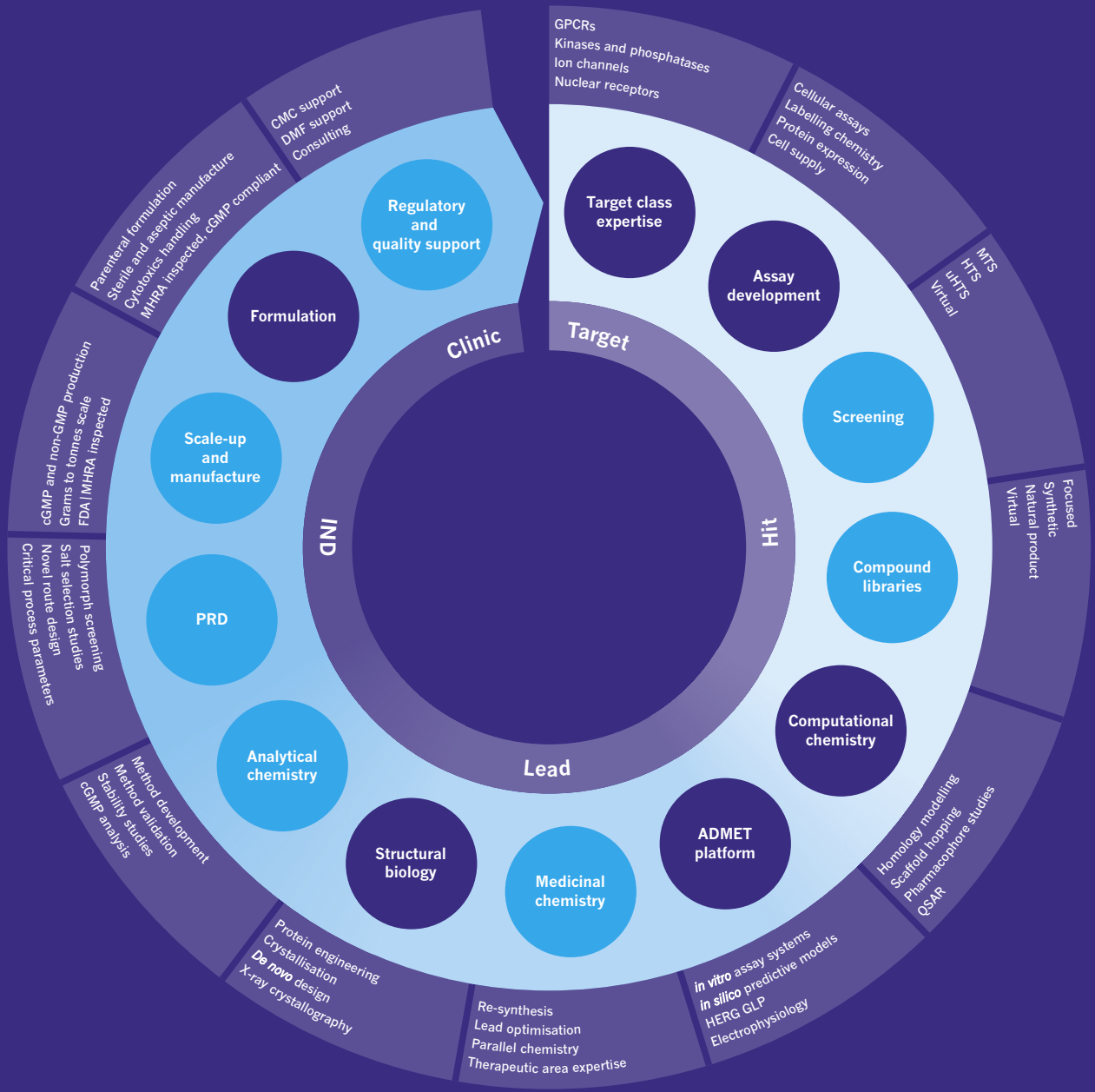
Key figures

Evotec OAI AG		1999	2000	2001	2002	2003	Δ 03 | 02 in %
Results							
Revenue	T€	9,786	28,276	63,225	69,995	77,228	10.3
R&D expenses	T€	12,952	18,480	23,012	23,012	15,466	(32.8)
Operating loss	T€	10,154	48,926	152,469	135,512	15,777	(88.4)
Operating loss*	T€	10,106	14,291	12,294	14,105	5,106	(63.8)
Net loss	T€	9,482	47,074	147,750	131,630	14,242	(89.2)
Net loss*	T€	9,434	12,493	7,575	10,223	3,571	(65.1)
EBITDA	T€	(7,953)	(9,459)	(1,011)	(2,221)	4,086	284.0
Cash flow	T€	41,549	(24,760)	(12,733)	5,313	(1,333)	(125.1)
Balance sheet data							
Subscribed capital**	T€	24,156	35,452	35,507	35,510	35,510	–
Number of shares**	T	24,156	35,452	35,507	35,510	35,510	–
Stockholders' equity	T€	60,299	502,495	347,591	195,407	172,101	(11.9)
Equity ratio	%	81.70	94.33	88.08	81.07	77.9	–
Investments***	T€	5,059	493,757	36,908	9,284	17,027	83.4
– Intangible assets	T€	337	433,819	20,246	28	1,689	–
– Tangible fixed assets	T€	4,715	56,626	16,652	8,634	13,613	57.7
– Financial assets	T€	7	3,312	10	622	1,725	177.3
Cash including marketable securities	T€	57,488	48,924	27,833	21,308	19,471	(8.6)
Balance sheet total	T€	73,806	532,706	394,617	241,042	220,919	(8.4)
Personnel data							
Employees as of 31 December		228	505	585	635	644	1.4
Total corporate personnel expenditures	T€	10,519	17,997	31,917	35,768	36,364	1.7
Revenue per employee	T€	43	56	108	110	120	9.1
Per share							
Result	€	(0.60)	(1.75)	(4.17)	(3.71)	(0.40)	89.2
Dividends	€	–	–	–	–	–	–
Security identification No.						566480	

* before amortisation and impairment
** refers to 1 € (retrospectively adopted to stock split)
*** including additions from acquisitions of OAI and GENION

The leading drug discovery and development engine

From recent competitive benchmarking we determined that Evotec OAI has the broadest and deepest range of integrated drug discovery and development capabilities.



In order to further complete and rejuvenate our offering, we added the following in 2003:

> Build-up of a dedicated **Structural Biology group** (through acquisition of ex-Pantherix technologies and skills)
> Expansion of **Computational Chemistry capabilities**
> Expansion of *in vitro* and *in silico* **ADMET platform**
> Improved integration of **formulation capabilities** at ProPharma
> Expansion of cellular **assay capabilities**
> **GPCR collaboration** with Euroscreen
> **Natural product** screening collaboration with Biofrontera

Glossary

ADMET Acronym for **A**bsorption, **D**istribution, **M**etabolism, **E**xcretion and **T**oxicity of a substance reflecting the → physiological processes *in vivo*. ADMET studies are used to characterise how drugs are taken up by the body, where they go in the body, the chemical changes they undergo in the body and how they are eliminated from the body.

Antagonist Drug that binds a cellular → receptor thereby inhibiting the natural function of the receptor.

Assay Any combination of → targets and compounds which is exposed to a detection device to measure chemical or biological activity.

Bead based assay A biological → assay in which one of the components or reagents is attached to small beads. For such assays the beads are usually insoluble and are often made from cross-linked polystyrene.

Bioavailability The percent of dose of a drug entering the systemic circulation after administration of a given dosage form. This is usually determined from the ratio of the amount of drug "absorbed" from an oral formulation to the amount "absorbed" after administration of an aqueous solution of the drug, given intravenously.

Calcium flux assay An → assay that measures the movement of calcium across cellular →membranes into or out of cells.

Cell based assay | screen → Assay | → screen performed using whole living cells.

Cell line Cells with an unlimited replication capacity, which maintain specific and useful characteristics identical between the parent and the daughter cells.

Clinical trials Drug research studies that involve patients or healthy volunteers.

Cloning Isolation of genetically identical cells by Elektra technology.

Combinational chemistry Chemical synthesis whereby a very large number of organic compounds is created by putting chemical "building blocks" together in every possible combination.

Computational chemistry Discipline of using computational methods to calculate properties of chemical compounds and their interaction with biological →targets (e.g. proteins).

FCS single molecule detection | FCS⁺plus Evotec OAI's proprietary detection technology. A laser beam is directed towards a very small focal point using a special confocal lens. Biological substances, marked with a fluorescent dye, show up brightly at the focal point of the laser. Their species-specific photons are picked up by a highly sensitive detector as a function of time.

Formulation development The formulation by which a drug is delivered *in vivo* can have a profound effect on its → bioavailability. Therefore it is necessary to develop the optimal formulation; this will involve the selection of the dosage form (e.g. softgel capsule or tablet), choice of excipients and studies on the chemical stability of the formulated drug.

GLP The principles of **G**ood **L**aboratory **P**ractice define a set of rules and criteria for a quality system concerned with the organisational process and the conditions under which non-clinical health and environmental safety studies are planned, performed, monitored, recorded, archived and reported.

G-Protein Coupled Receptors Large family of related cell surface → receptors which play a very important role in drug therapy. These receptors stimulate and convey signals within cells harbouring these proteins through interactions with a conserved family of proteins known as G-proteins.

High-throughput screening (HTS) Technique of rapidly searching for molecules with desired biological effects from very large compound libraries, often exceeding 100,000 tests a day.

Hit (compound) A molecule which has a robust dose-response activity in a primary → screen of known confirmed structure and preliminary →SAR information.

IND (**I**nvestigational **N**ew **D**rug) Substance which enters →clinical trials in humans following approval for initiation of clinical trial by the FDA or similar regulatory authority.

In silico Pertaining to the computational modelling of biological tests or experiments.

Ion channel →Receptor which, when activated, allows the passage of ions across cell →membranes that influence the →physiology of a cell.

Lead (compound) A representative of a compound series with sufficient potential (as measured by potency, selectivity, →pharmacokinetics, physicochemical properties, novelty and absence of toxicity) to progress to a full drug optimisation programme.

Lead optimisation The synthetic modification of a biologically active compound, to fulfil all → pharmacological, physicochemical, → pharmacokinetic and toxicologic requirements for clinical usefulness.

Linux cluster A large computer system built from smaller, standard, off-the-shelf systems, networked together as nodes functioning with parallel processing, and running the Linux® operating system.

Lipinski donor and acceptor counts Counts of the number of hydrogen bond donors and hydrogen bond acceptors within a small molecule drug. These numbers will vary from molecule to molecule and will be dependent on the chemical structure. The Rule-of-5 was derived by a scientist working at Pfizer called Dr Lipinski. He analysed the key properties of 2,245 drug molecules believed to have entered Phase II → clinical trials. According to the Rule-of-5 poor absorption and permeability are more likely when there are more than 5 hydrogen bond donors, more than 10 hydrogen bond acceptors, the molecular weight is more than 500 and | or the calculated →LogP is greater than 5.

LogP The logP value of a compound, which is the logarithm of its partition coefficient between n-octanol and water, is a well established measure of the compound's lipophilicity. High lipophilicities, indicated by high logP values, may result in poor →bioavailability.

Medicinal chemistry A chemistry-based discipline, also involving knowledge and aspects of biological, medicinal and pharmaceutical sciences. It is concerned with the invention, discovery, design, identification and preparation of biologically active compounds, the study of their → ADMET properties, the interpretation of their mode of action at the molecular level and the construction of →structure activity relationships. Medicinal chemistry optimisation is the "fine tuning" required to turn a validated →lead into a →pre-clinical candidate involving subtle structural changes to the lead using a "hand-crafted" approach.

Membrane Is a covering or skin for cells, tissues or organs within the body.

NMDA receptor A subfamily of →receptors for the major neurotransmitter glutamate. A receptor is a protein on the surface of a cell that selectively binds a neurotransmitter or hormone to mediate its effects.

NMDA receptor subtype Subtype of → NMDA receptors, which is located in specific brain regions and responsible for specific functions.

Pharmacokinetics Movements of drugs within biological systems, as affected by absorption, distribution, metabolism, excretion (→ADME).

Pharmacology The science concerned with drugs, their sources, appearance, chemistry, actions and uses.

Phase IIa Controlled clinical study of a drug to identify common short-term side effects and risks associated with the drug, and to demonstrate its efficacy conducted on a limited number of patients with disease.

Physiology Physiology is the science of living organisms and their parts.

Polar surface area The polar surface area (PSA) is the sum of the surfaces of the polar atoms in a molecule.

Pre-clinical development The phase of drug discovery extending from → target identification, the search for chemical compounds with desired properties, through to the end of efficacy studies in animal models and safety evaluation prior to →clinical trials.

Proof-of-concept drug (POCD) Drug candidate which has completed → Phase IIa clinical trials demonstrating that the molecule proves the concept that → pharmacological intervention of the selected biological →target will be therapeutically useful in the selected clinical indication.

R-group For a series of chemically related compounds an R-group denotes that part of the parent molecule that is subject to variation by different chemical substituents.

Receptor Protein in a cell or on its surface that selectively binds a specific substance (ligand). Upon binding its ligand, the receptor triggers a specific response in the cell.

Reporter assay Particular type of →cellular assay whereby the activity of a compound is reported by the activity of a newly synthesised protein in the cell.

Screening Mass testing of compound libraries using an established →assay format.

Screening library Collection of a multitude of different molecules; used for →screening.

Secretion assay A → cell based assay that measures the quantity of a specific molecule (usually a protein) that is secreted from a cell into the solution in which the cells are residing. Such assays can be configured to measure whether an externally applied chemical compound stimulates secretion or inhibits secretion.

Serum albumin binding Serum albumin is a large protein molecule present in the plasma component of blood and which can bind drug molecules. If a drug is very strongly bound to serum albumin there may not be sufficient concentration of the unbound drug in order for it to exhibit the desired pharmacological effect at the biological → target within the body.

Signalling pathway When cells respond to external stimuli such as natural hormones and environmental conditions they do so by a cascade of biochemical events within each cell termed the signal transduction pathway.

Structure Activity Relationships (SAR) Information collectively describing the structure and the interaction of a specific chemical compound with a →target molecule.

Structure-based drug design A drug design strategy based on the 3D structure of the → target obtained by X-ray or NMR (**N**uclear **M**agnetic **R**esonance).

Structural biology Dealing with the structural analysis of living material that lead to an understanding of biological function in terms of molecular and submolecular structure.

Systems biology The study of whole biological systems within a cell, an organ or an organism with particular emphasis on →signalling pathways and their network.

Target Specific biological molecule, such as an enzyme, →receptor or →ion channel, assumed to be relevant to a certain disease. Most drugs work by binding to a target, thereby affecting its biological function.

Target identification Identifying a molecule (often a protein) that is instrumental to a disease process (though not necessarily directly involved), with the intention of finding a way to regulate that molecule's activity for therapeutic purposes.

Target validation Involves the verification of the relevance of a →target to the course of a specific illness.

Virtual library of compounds A multitude of chemical compounds that exists within the computer. Such virtual libraries of molecules are carefully designed so that they can be readily synthesised in the laboratory should they be predicted from computational studies to be advantageous.

Virtual screening A → computational chemistry technique whereby existing compounds and | or virtual collections of compounds are →screened →*in silico*.

X-ray crystallography The determination of the 3D-structure of molecules from the diffraction pattern obtained upon irradiation of a crystalline form of the substance being studied by X-ray radiation.

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