

Combined balance sheets at 31 December in million CHF	Assets		■ Note	1996	1997	1998
		<u>Fixed assets</u>				
	Property, plant and equipment	4	2 821		3 075	3 377
	Accumulated depreciation	4	(1 452)	1 369	(1 526)	(1 620) 1 757
	Intangible assets	4		25	35	36
	Goodwill	4		86	83	77
	Other noncurrent assets and deferred items	4		32	41	59
	Unconsolidated investments	4		67	68	63
	Total fixed assets			1 579	1 776	1 992
	<u>Current assets</u>					
	Inventories, net	5		394	422	455
	Trade receivables, net	6	352		366	372
	Other receivables, prepaid expenses and accrued income	7	56	408	71 437	74 446
	Cash and marketable securities*			0	0	0
	Total current assets			802	859	901
	Total assets			2 381	2 635	2 893

* See "Basis of preparation of the historical combined financial statements" page 100 and following

■ The appropriate explanations can be found in the notes to the historical combined financial statements.

	■ Note	1996	1997	1998
Liabilities and shareholders' equity				
Total shareholders' equity	9	1 398	1 655	1 807
Minority interests		27	29	20
Liabilities				
Long-term provisions	10	366	371	390
Long-term debts		0	0	0
Total long-term liabilities and provisions		366	371	390
Other liabilities and deferred items	12	326	331	429
Current liabilities:				
Trade payables	13	239	228	219
Short-term debts:				
Due to bank and other financial institutions	11	25	21	28
Total current liabilities and deferred items		590	580	676
Total liabilities		956	951	1 066
Total liabilities and shareholders' equity		2 381	2 635	2 893
Contingent liabilities		17	16	9

* See "Basis of preparation of the historical combined financial statements" page 100 and following

- *The appropriate explanations can be found in the notes to the historical combined financial statements.*

Combined cash flow statements in million CHF	■ Note	1997	1998
Consolidated net income for the year		140	<u>212</u>
Depreciation of property, plant and equipment	4, 18	150	<u>165</u>
Amortization of intangibles	4, 18	2	<u>7</u>
Amortization of goodwill	4, 18	4	<u>5</u>
Increase (decrease) in long-term provisions	10	(4)	<u>5</u>
(Income) from application of the equity method	20	(1)	<u>(1)</u>
Cash flow		291	<u>393</u>
(Increase) in net working capital		(64)	<u>(26)</u>
Net cash provided by operating activities		227	<u>367</u>
Purchase of property, plant and equipment	4, 22	(353)	<u>(410)</u>
Purchase of intangibles net	4	(12)	<u>(4)</u>
Goodwill from purchase of operations	4	(7)	<u>(2)</u>
(Purchase) sale of unconsolidated investments	4	(1)	<u>6</u>
Purchase of consolidated companies (less cash acquired)		0	<u>0</u>
Sale of consolidated companies (less cash disposed)	4	23	<u>0</u>
Sale of property, plant and equipment	4	14	<u>3</u>
Goodwill from sale of operations		0	<u>0</u>
(Purchase) sale of other assets	4	(2)	<u>(3)</u>
(Purchase) sale of marketable securities		0	<u>0</u>
Increase (Decrease) in other long-term liabilities		0	<u>68</u>
Decrease in loans and advances		0	<u>0</u>
Net cash used in investing activities		(338)	<u>(342)</u>
Increase (decrease) of capital	9	112	<u>(23)</u>
Increase (decrease) in debts	11	(4)	<u>7</u>
Contribution minority interests		3	<u>(9)</u>
Net cash provided by (used for) financing activities		111	<u>(25)</u>
Translation adjustments		0	<u>0</u>
Net increase (decrease) in cash		0	<u>0</u>
Cash on hand at 1 January		0	<u>0</u>
Cash on hand at 31 December		0	<u>0</u>

■ *The appropriate explanations can be found in the notes to the combined financial statements.
Balance sheet amounts may vary due to currency translation.*

Basis of preparation of the historical combined financial statements

The historical combined financial statements have been prepared on the following basis:

1. The accompanying combined financial statements of the Lonza Group Ltd and its subsidiaries (the "Group") include the balance sheets, operating results and cash flows of those algroup activities that are intended for spin-off as described more fully under page 24 and following in this "Right Offering Circular". The businesses have been included in these combined financial statements as if they have been part of the Group throughout the three year period ended December 1998 and up to the date of disposal.
2. The balance sheets, profit and loss and cash flow statement of the individual Lonza Group operations have been combined on the basis that they will operate under the control of the Group commencing July 1, 1999.
3. Financing activities within algroup have historically been centralized and managed at corporate level on a country by country basis and not by division. These combined financial statements have been prepared on the assumption that the Group was free of debt at the end of each fiscal year. This has been accomplished by an assumed increase (decrease) of capital equal to the amount necessary to extinguish the net debt of each operating subsidiary, with the exception of net debt attributable to minority interests which continues to be shown. Furthermore, it has been assumed that all cash on hand at the end of each year in 1996, 1997 and 1998 has been distributed to shareholders. Thus, the combined income statements do not reflect any interest income or expense, other than interest expense in relation to the Group's pension obligation of its German subsidiaries. As a result, the net debt position in each of the balance sheets of the Group for the years ended December 31, 1996, 1997 and 1998 has resulted in a nil balance.
4. The foreign currency exposure for the Lonza Group has been managed at corporate level by hedging activities, therefore no costs related to financial transactions have been recognized. The impact of the gain and losses resulting from hedging transactions related to operational activities has been allocated to the single operational units.
5. Tax has been calculated on income before income taxes. Statutory tax rates have been applied on a country specific basis to income before income taxes for each subsidiary with the exception of those in the United States. Based on preliminary estimates, sufficient tax loss carryforwards would be available to shelter the US Chemical operations from full current US federal taxes. US taxes have therefore been provided at the required minimum annual federal tax rate plus full statutory state tax rates. Thirty percent of the above calculated tax expense is presented as deferred tax expense, based on historical experience.
6. The historical combined financial statements do not include costs of the algroup corporate infrastructure.

Accounting principles **General information** Subject to the comments included in the basis of preparation of the historical combined financial statements outlined before, the historical combined financial statements are based on the annual accounts of the individual subsidiaries at 31 December, which have been drawn up according to uniform Group principles. The combined accounts are prepared in conformity with the current International Accounting Standards (IAS), published by the International Accounting Standards Committee (IASC).

Principles of combination The historical combined financial statements represent the accounts for the years ended 31 December of Lonza Group Ltd and its subsidiaries.

Subsidiaries acquired during the year are included in the combined accounts from the date of acquisition, while any subsidiaries sold are excluded from the accounts from the date of sale. Acquisitions are accounted for by the use of purchase method accounting. The full consolidation method is used, whereby the assets, liabilities, income and expenses are incorporated in full. The proportion of the net assets and net income attributable to minority shareholders is shown separately in the combined balance sheet and income statement. Payables, receivables, income and expenses between the companies included in the **combination** are eliminated. Intercompany profits included at the year-end in inventories of goods produced within the Group have been eliminated. Transactions between subsidiaries are concluded under market conditions.

Immaterial subsidiaries are not included in the **combination**. These are shown under *unconsolidated investments* and the income or loss under *income (loss) from unconsolidated investments*.

Investments in affiliates are reflected in the balance sheet using the equity method of accounting. Under this method, the investment is initially recorded at cost, and is increased or decreased by the proportionate share of the affiliate's profits or losses after the date of acquisition, adjusted for any amortization of goodwill arising on acquisition and depreciation of fair market value increments/decrements recognized at that time. Dividends paid during the year reduce the carrying value of the investments. This also applies to a few wholly-owned subsidiaries, particularly sales companies, which are not significant as a whole.

Investments of less than 20 percent are not combined and are stated at cost, less any write-offs that are necessary.

The significant subsidiaries and affiliates included in the combined financial statements are shown on page 117.

Definitions A **subsidiary** is a Group company which Lonza Group Ltd controls normally by holding (either directly or indirectly) more than 50 percent of the voting shares of the company.

An **affiliate** is a Group company in which Lonza Group Ltd holds (either directly or indirectly) 20 to 50 percent of the voting shares of the company.

A **related party** is a subsidiary or affiliate of algroup which is not part of Lonza Group.

Liabilities Financing activities within algroup are centralized and managed at corporate level by on a country by country basis and not by division. For purposes of preparing this combined balance sheet and in accordance with the terms of the demerger and separation agreement between algroup and Lonza Group, it has been assumed that the Group was free

of net financial debt at December 31, 1996, 1997 and 1998. This has been accomplished by an assumed increase (decrease) of capital equal to the amount necessary to extinguish the net of financial debt of each company which has been included in the combination, with the exception of net financial debt attributable to minority interests which continues to be shown.

Extraordinary income and expenses comprise items that are clearly distinct from the ordinary activities of the Group and are not expected to recur frequently or regularly. Therefore, only on rare occasions does an event or transaction give rise to an extraordinary item.

The current ratio represents the relationship between current assets and current liabilities.

Treatment of foreign subsidiaries All assets and liabilities of a foreign subsidiary which is combined are translated using the exchange rates in effect at the balance sheet date (the current method). Income and expenses are translated at the average exchange rate for the year. Differences resulting from the application of these different methods of translation of the balance sheet and income statement, together with exchange gains or losses on the opening net asset values of the subsidiaries, are added to or deducted from the combined shareholders' equity.

Foreign currency transactions Transactions in foreign currencies are recorded using exchange rates in effect at the time of the transaction. Gains or losses arising on settlement of these transactions are included in the current year's income. Foreign currency denominated monetary assets and liabilities at 31 December are translated using the exchange rate in effect at the balance sheet date. Any gains or losses resulting from this translation are included in the current year's income.

Derivative financial instruments To manage currency exposures, the Group uses currency forwards and option contracts. Realized and unrealized gains and losses arising from currency forwards and options are recognized as adjustments to the gains and losses resulting from the underlying hedged transactions. Hedges designated as a hedge of the Group's related net asset exposures are reflected in the currency translation adjustment section of shareholders' equity offsetting the translation of the net assets. The Group does not hold or issue financial instruments for trading purposes.

Fixed assets Fixed assets (property, plant and equipment) are stated at cost less adequate adjustments for depreciation.

The assets are depreciated over their estimated useful lives, which vary from 25 to 50 years for buildings and structures, and 3 to 12 years for production facilities, machinery, plant, equipment and vehicles. Depreciation is charged on the straight-line basis.

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

Intangible assets Intangibles include software, licences, patents, trademarks and similar rights granted by third parties. These assets are amortized on the straight-line principle over their estimated useful lives, up to a maximum of five years.

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

Inventories Inventories are reported at the lower of cost (purchase price or Group production cost) or market value (net realizable values). The cost of inventories is calculated using the monthly or weighted average method. Prorated production overheads are included in the valuation of inventories. Goods with long storage periods and obsolete goods are written down. Intercompany profits on inventories of goods produced in the Group have been eliminated from net income.

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

Cash and marketable securities See basis of presentation of the historical combined financial statements.

Deferred taxes See basis of preparation of the historical combined financial statements.

Retirement benefits Most of the subsidiaries operate their own pension plans, mainly legally independent from the Group. Generally, they are funded by employees' and employer's contributions.

A policy has been established whereby actuarial valuations have been and will be performed on a three-year basis and roll-forwards will be conducted during the intervening period. The cumulative effect from initial application of IAS 19 as of 1 January 1995 is included as a transitional amount and will be recognized as an asset or liability respectively, over a period not exceeding the expected remaining working lives of the participating employees. In the following years the actuarial gains and losses are recognized over the same period as above if the accumulated gain and loss exceed the corridor of 10% of the greater of plan assets and projected benefits obligation. Some foreign pension plans not considered significant as a whole were not included in these calculations.

Research and development Expenditure on research and development is not capitalized, but charged immediately to expenses. Fixed assets (buildings, machinery, plant, equipment) used for research purposes are valued like other fixed assets, capitalized and written down over their useful life.

Expenses for research and development include associated wages and salaries, material costs, depreciation on fixed assets, as well as overhead costs.

Notes to the combined financial statements

The notes are referred to the combined balance sheet, the combined income statement and the combined cash flow statement. For 1996 the notes do not include the same level of detail, as reclassification is impracticable for the amended divisional structure.

1 Exchange rates

The following exchange rates were used to translate the most important currencies in the Group:

<u>Exchange rates</u>		1996	1997	Balance sheet year-end rates CHF	1996	1997	Income statement year average rates CHF	1998
USA	dollar	1	1.3500	1.4535	1.3775	1.2360	1.4501	1.4497
Canada	dollar	1	0.9850	1.0142	0.8896	0.9066	1.0474	0.9798
Australia	dollar	1	1.0750	0.9513	0.8448	0.9684	1.0794	0.9135
Great Britain	pound sterling	1	2.2875	2.4100	2.2860	1.9319	2.3747	2.4008
Germany	mark	100	86.8500	81.3080	82.1190	82.1210	83.7200	82.3850
France	franc	100	25.7500	24.2990	24.4870	24.1578	24.8700	24.5740
Italy	lira	100	0.0885	0.0827	0.0829	0.0803	0.0853	0.0835
Netherlands	guilder	100	77.3500	72.1560	72.8860	73.2995	74.4000	73.0860
Spain	peseta	100	1.0300	0.9594	0.9657	0.9760	0.9912	0.9704

2 Financial instruments

Risk management activities The Group is exposed to market risk from changes in currency exchange rates. To manage the volatility relating to these exposures, the Group enters into various derivative transactions pursuant to the Group's policies in areas such as counterparty exposure and hedging practices. Counterparties to these agreements are major international financial institutions. Positions are monitored using techniques such as market value and sensitivity analyses. The Group does not hold or issue derivative financial instruments for trading purposes and is not a party to leveraged instruments.

The following table presents information for foreign exchange contracts. The notional amount of derivatives summarized below represents the gross amount of the contracts and includes already closed transactions which have not yet matured. Therefore the figures are not a direct measure of the Group's exposure. The market value approximates the cost to settle the outstanding contracts. These market value amounts should be viewed not in isolation but in relation to the market values of the underlying hedged transactions and the overall reduction in the Group exposure to adverse fluctuation of foreign exchange rates.

	1997	1998
	million CHF	million CHF
Foreign exchange contracts		
Notional amount	115	48
Net negative market value	(1)	0
Net negative book value	(1)	0
Difference market value / book value	0	0
Credit risk	1	0

Foreign exchange management In management of its exposure to fluctuation in foreign currency exchange rates, the Group has entered into a variety of currency swaps, foreign exchange contracts and options. These agreements generally include the exchange of one currency for a second currency at a future date.

3 Changes in the scope of consolidation In 1996, the following company was acquired:
Celltech Biologics plc, Slough, Berkshire, GB (at 28 June 1996)
Furthermore, operations (market share and technology) of a biocide business was acquired.

In 1997 the following company was newly consolidated:
Lonza Singapore Pte Ltd (at 1 January 1997, 80% ownership interest).

During this period a few minor companies and/or activities were newly consolidated or excluded (disposed of) from the scope of consolidation.

In 1999 the company Lonza Folien GmbH will be integrated in the Fine Chemicals and Specialties division. For comparative purposes, the previous year's data of the historical combined financial statements were reclassified to reflect the current corporate structure.

		At 31 12 1996	Currency translation differences	Change in the scope of consolidation	Additions	Disposals	Transfers	At 31 12 97	Fixed assets net at 31 12 97	Insurance value at 31 12 97
4 Movements in fixed assets in million CHF	At cost									
	Land	50	0	(1)	3	(2)	0	50	47	
	Buildings and structures	849	(2)	(6)	21	(23)	32	871	462	785
	Production facilities, machinery, plant, equipment and vehicles	1 716	(9)	(15)	32	(33)	129	1 820	706	2 643
	Construction in progress and advances for property, plant and equipment	206	(3)	0	297	(5)	(161)	334	334	154
	Property, plant and equipment	2 821	(14)	(22)	353	(63)	0	3 075	1 549	3 582
	Intangible assets	47	1	0	12	(9)	0	51	35	
	Goodwill	88	2	0	7	(8)	0	89	83	
	Other noncurrent assets and deferred items	32	2	0	7	0	0	41	41	
	Unconsolidated investments	266	0	0	2	0	0	268	68	
	Total fixed assets	3 254	(9)	(22)	381	(80)	0	3 524	1 776	
	Accumulated depreciation									
	Land	(3)	0	0	0	0	0	(3)		
	Buildings and structures	(405)	1	0	(26)	20	1	(409)		
	Production facilities, machinery, plant, equipment and vehicles	(1 044)	7	10	(124)	38	(1)	(1 114)		
	Property, plant and equipment	(1 452)	8	10	(150)	58	0	(1 526)		
	Intangible assets	(22)	(1)	0	(2)	9	0	(16)		
	Goodwill	(2)	0	0	(4)	0	0	(6)		
	Unconsolidated investments	(199)	0	0	(1)	0	0	(200)		
	Total depreciation	(1 675)	7	10	(157)	67	0	(1 748)		
	Total fixed assets net	1 579	(2)	(12)	224	(13)	0	1 776		

	At 31 12 1997	Currency translation differences	Change in the scope of consolidation	Additions	Disposals	Transfers	At 31 12 98	Fixed assets net at 31 12 98	Insurance value at 31 12 98
At cost									
Land	50	(1)	0	0	(2)	4	51	47	
Buildings and structures	871	(3)	0	11	(19)	73	933	520	822
Production facilities, machinery, plant, equipment and vehicles	1 820	(30)	0	71	(35)	400	2 226	1 023	2 628
Construction in progress and advances for property, plant and equipment	334	(4)	0	328	(4)	(487)	167	167	172
Property, plant and equipment	3 075	(38)	0	410	(60)	(10)	3 377	1 757	3 622
Intangible assets	51	0	0	7	(7)	10	61	36	
Goodwill	89	(2)	0	2	0	0	89	77	
Other noncurrent assets and deferred items	41	(3)	0	29	(8)	0	59	59	
Unconsolidated investments	268	0	0	3	(7)	0	264	63	
Total fixed assets	3 524	(43)	0	451	(82)	0	3 850	1 992	
Accumulated depreciation									
Land	(3)	(1)	0	0	0	0	(4)		
Buildings and structures	(409)	1	0	(27)	16	6	(413)		
Production facilities, machinery, plant, equipment and vehicles	(1 114)	9	0	(138)	41	(1)	(1 203)		
Property, plant and equipment	(1 526)	9	0	(165)	57	5	(1 620)		
Intangible assets	(16)	0	0	(7)	3	(5)	(25)		
Goodwill	(6)	(1)	0	(5)	0	0	(12)		
Unconsolidated investments	(200)	1	0	(2)	0	0	(201)		
Total depreciation	(1 748)	9	0	(179)	60	0	(1 858)		
Total fixed assets net	1 776	(34)	0	272	(22)	0	1 992		

Commitments for capital expenditure in property, plant and equipment amount to CHF 62 million at year end 1998 (1997: CHF 244 million; 1996: n.a.).

5 Inventories	1996		1997		1998	
	million CHF	%	million CHF	%	million CHF	%
Raw materials	64	16	75	18	81	18
Work in process & finished good	252	64	266	63	282	62
Others	78	20	81	19	92	20
Total	394	100	422	100	455	100

By division	million CHF	%	million CHF	%	million CHF	%
Fine chemicals and specialties	307	78	332	79	364	80
Intermediates and additives	87	22	90	21	91	20
Energy	0	0	0	0	0	0
Others	0	0	0	0	0	0
Total	394	100	422	100	455	100

6 Trade receivables	1996	1997	1998
	million CHF	million CHF	million CHF
Receivables from customers	342	337	358
Accounts receivable from unconsolidated affiliates	16	31	17
Value adjustments	(9)	(10)	(8)
Related Parties	3	8	5
Total	352	366	372

The credit risk is generally very diversified due to the large number of entities comprising the companies' customer bases and their dispersion across many different industries and regions.

7 Other receivables, prepaid expenses and accrued income	1996	1997	1998
	million CHF	million CHF	million CHF
Other receivables	} 56	36	38
Prepaid taxes and social security payments		16	13
Prepaid expenses and accrued income		17	19
Accrued interest income		2	4
Related Parties		0	0
Total	56	71	74

8 Pledges and assets under reservation of ownership The assets pledged for security of own liabilities amount to CHF 33 million (1997: CHF 0 million; 1996: CHF 2 million).

		Total share- holders' equity
9 Changes in shareholders' equity	million CHF	
	<u>At 31 12 96</u>	<u>1 398</u>
	Increase (decrease) of capital	112
	Net income	140
	Currency translation differences	5
	<u>At 31 12 97</u>	<u>1 655</u>
	Increase (decrease) of capital	(23)
	Net income	212
	Currency translation differences	(37)
	<u>At 31 12 98</u>	<u>1 807</u>

10 Long-term provisions			1998
	1996	1997	million CHF
	million CHF	million CHF	<u>million CHF</u>
Deferred taxes	}	146	<u>193</u>
Retirement benefits	366	110	<u>107</u>
Others	}	115	<u>90</u>
Total	366	371	<u>390</u>

The provisions for retirement benefits mainly comprise the pension liability of the Group's defined benefit pension plans as disclosed in note 24. Included in the above amounts are provisions for healthcare relating to the Group's US subsidiaries. The other provisions relate to approved operational measures. The long-term provisions are operationally necessary.

11 Net debt			1998
	1996	1997	million CHF
	million CHF	million CHF	<u>million CHF</u>
Due to banks and other financial institutions	25	21	<u>28</u>

The amount reflects the portion of net debt in the minority interests.

12 Other liabilities and deferred items			1998
	1996	1997	million CHF
	million CHF	million CHF	<u>million CHF</u>
Short-term provisions	}	96	<u>95</u>
Capital tax payables	}	5	<u>3</u>
Current tax payables	}	58	<u>40</u>
Other interest-free liabilities	326	18	<u>86</u>
Accrued liabilities and deferred items	}	141	<u>188</u>
Accrued interest payables	}	4	<u>4</u>
Related Parties	}	9	<u>13</u>
Total	326	331	<u>429</u>

13 Trade payables	1996	1997	1998
	million CHF	million CHF	million CHF
Payable to third parties	230	226	207
Payable to unconsolidated affiliates	3	5	6
Related Parties	6	(3)	6
Total	239	228	219

14 Contingent liabilities Contingent liabilities concern bills discounted, purchase commitments and guarantees given to third parties in the ordinary course of business. They amount to CHF 9 million (1997: CHF 16 million; 1996: CHF 17 million). Political, legal, fiscal and other changes in the countries where the Group operates can affect business activity. The impact of such changes on consolidated income cannot be predicted and is therefore not taken into consideration.

15 Other operating income	1996	1997	1998
	million CHF	million CHF	million CHF
Work performed for investments in property, plant and equipment	33	52	43
Other operating income	20	31	16
Total	53	83	59

16 Personnel expenses	1996	1997	1998
	million CHF	million CHF	million CHF
	509	558	566

Personnel expenses include wages and salaries, pension costs, other social security contributions and other personnel expenses.

17 Other operating expenses	1996	1997	1998
	million CHF	million CHF	million CHF
	221	283	284

Apart from the repair and maintenance costs of CHF 89 million (1997: CHF 92 million; 1996: CHF 79 million), the major items reported under other operating expenses are selling, general and administrative expenses.

In 1998 one-off gains, amounting to CHF 31 million, have been fully offset by restructuring costs in our Fine Chemicals and Specialties division. Therefore, these transactions had no impact on Group operating income and net income.

18 Depreciation and amortization	1996	1997	1998
	million CHF	million CHF	million CHF
Property, plant and equipment	129	150	165
Intangible assets	5	2	7
Total	134	152	172
Amortization of goodwill	2	4	5

19 Other financial income and expenses	1996	1997	1998
	million CHF	million CHF	million CHF
	(3)	(4)	(3)

Other financial expenses comprise mainly financing costs for the German pension funds.

20 Income from unconsolidated investments	million CHF	million CHF	million CHF
Dividend earned	3	1	2
Income from application of the equity method	0	2	2
Total	3	3	4

21 Income taxes	1996	1997	1998
Major components of tax expense	million CHF	million CHF	million CHF
Current taxes	46	48	55
Deferred tax expense	20	20	23
Total	66	68	78

See also basis of preparation of the historical combined financial statements.

22 Investment in property, plant and equipment	1996	1997	1998
	million CHF	million CHF	million CHF
By division			
Fine chemicals and specialties	157	236	194
Intermediate and additives	68	99	203
Energy	12	18	13
Others	0	0	0
Total	237	353	410

23 Research and development Research and development expenses primarily reflect the cost incurred in basic scientific research and development. In 1998 these expenses amounted to CHF 105 million (1997: CHF 105 million; 1996: CHF 98 million).

24 Pension benefits The Group sponsors pension plans according to the regulations of the countries in which it operates. All significant plans provide defined benefits on retirement. The benefits are primarily based on years of service and the employees' compensation for certain periods during the last years of employment. During 1998, actuarial valuation was performed for the significant defined benefit plan using the projected unit credit valuation method.

A policy has been established whereby actuarial valuations will be performed periodically and roll forwards will be conducted as at 31 December each year during the intervening period. The assumptions used in the actuarial valuation are according to the underlying national economic conditions of the respective countries:

	1996	1997	1998
Discount rate	5.0%	4.5%	4.5%
Expected long-term rates of return on plan assets	5.0%	5.0%	5.5%
Rates of increase in compensation	3.0%	3.0%	3.0%

The funded status is as follows:

million CHF	31 12 1996	31 12 1997	Plans with PBO in excess of assets 31 12 1998
Projected benefits obligation (PBO)	921	992	1 061
Plan assets at fair value	805	921	1 044
Plan assets in excess of (less than) projected benefit obligation	(116)	(71)	(17)
Funded status	(116)	(71)	(17)

The pension assets and liabilities calculated above are disclosed in the financial statements for 1998. The net change of the prepaid pension costs accounted in financial year 1998 amounts to CHF 13.5 million and is reflected under *retirement benefits and prepaid expenses*.

The cumulated amount at the end of 1998 is CHF 70 million (1997: CHF 56 million; 1996: CHF 41 million).

Net periodic pension costs for the Group's significant defined benefit plan consist of the following:

	1996	1997	1998
	million CHF	million CHF	million CHF
Service costs	17	21	21
Interest costs	46	43	46
Actual return on plan assets	(40)	(44)	(51)
Net amortization and deferral	10	10	11
Total	33	30	27

25 Year 2000 The challenge that Year 2000 compliance presents to organizations and individuals alike worldwide has been recognized. In 1997 a comprehensive Year 2000 compliance program was initiated including the inter alia testing of plant, machinery and facilities equipped with electronic devices supposed to have a time-related computing function. This assurance program is well under way.

The Group is dependent on a large number of external suppliers whose services and products also need to achieve compliance. These relationships are managed proactively and suppliers are required to certify their products and services as Year 2000 compliant.

Costs associated with Year 2000 system adjustments are being expensed as incurred over the 1998 and 1999 period.

26 Events after balance sheet date Lonza AG has entered into a Plea Agreement with the United States Department of Justice relating to Lonza AG's sale of Niacin and Biotin. The United States Government had charged that Lonza AG fixed prices and allocated volumes in connection with its sale of niacin and niacinamide.

To settle these charges, Lonza AG agreed to plead guilty to one count of price fixing and to pay a fine of USD 10.5 mio. An appropriate provision was made at the end of 1998. No Lonza AG executives or employees are charged with any wrongdoing.

In March 1999 a number of class action lawsuits were filed against Lonza Inc. and certain other chemical producers by purchasers of vitamine products in the United States. Because of the preliminary stage of these matters, the exact outcome of the class actions cannot presently be determined. The Group has however provided on a conservative basis an amount representing its assessment of the potential exposure.

Segment data	By business segment			Net sales to customers			Operating income			Net capital invested*		
	1996	1997	1998	1996	1997	1998	1996	1997	1998	1996	1997	1998
million CHF												
Fine chemicals and specialties	1 267	1 460	1 547	161	154	229	1 137	1 366	1 469			
Intermediates and additives	525	559	524	56	60	58	344	401	505			
Energy	46	45	42	23	22	21	118	128	132			
Others	0	0	0	(17)	(23)	(16)	(90)	(90)	(89)			
Related Parties**	33	35	40	na	na	na	na	na	na			
Total	1 871	2 099	2 153	223	213	292	1 509	1 805	2 017			

%	Percentage return on sales			Return on net capital invested***		
	1996	1997	1998	1996	1997	1998
Fine chemicals and specialties	12.7	10.5	14.8	14.3	11.2	15.4
Intermediates and additives	10.7	10.7	11.1	16.4	14.2	11.3
Energy	50.0	48.9	50.0	19.5	17.0	16.1
Others	na	na	na	na	na	na
Related Parties**	na	na	na	na	na	na
Total	11.9	10.1	13.6	14.9	11.6	14.3

By region	Net sales to customers			Operating income			Net capital invested*		
	1996	1997	1998	1996	1997	1998	1996	1997	1998
million CHF									
Europe	1 374	1 518	1 505	198	209	249	1 185	1 313	1 383
Other regions	463	546	608	25	4	43	324	492	634
Related Parties**	34	35	40	0	0	0	0	0	0
Total	1 871	2 099	2 153	223	213	292	1 509	1 805	2 017

%	Percentage return on sales			Return on net capital invested***		
	1996	1997	1998	1996	1997	1998
Europe	14.4	13.8	16.5	16.8	15.7	17.9
Other regions	5.4	0.7	7.1	7.9	0.8	6.6
Related Parties	na	na	na	na	na	na
Total	11.9	10.1	13.6	14.9	11.6	14.3

* Net capital invested comprises the average of all assets and liabilities committed to the business operations of the Group at historical period end rates.

** Sales to the algroup aluminium and packaging divisions.

*** Calculated at historical yearly average rates and includes Group companies acquired during financial year.

Sales	Sales by production area	1996		1997		1998	
		million	%	million	%	million	%
		CHF		CHF		CHF	
	Switzerland	1 042	48	1 151	46	1 434	51
	EU	627	29	704	28	701	25
	Rest of Europe	12	0	27	2	33	1
	Europe	1 681	77	1 882	76	2 168	77
	North America	495	23	595	24	644	23
	Other areas	0	0	0	0	2	0
	Subtotal	2 176	100	2 477	100	2 814	100
	(Intercompany sales)	(305)		(378)		(661)	
	Total	1 871		2 099		2 153	

Sales by marketing area	1996		1997		1998	
	million	%	million	%	million	%
	CHF		CHF		CHF	
Switzerland	322	17	342	16	295	14
EU	769	41	849	40	859	40
Rest of Europe	16	1	41	3	17	0
Europe	1 107	59	1 232	59	1 171	54
North America	503	27	604	29	681	32
Other areas	228	12	228	11	261	12
Related parties	33	2	35	1	40	2
Total	1 871	100	2 099	100	2 153	100

Sales by division	1996		1997		1998	
	million	%	million	%	million	%
	CHF		CHF		CHF	
Fine chemicals and specialties	1 267	68	1 460	70	1 547	72
Intermediates and additives	525	28	559	27	524	24
Energy	46	2	45	2	42	2
Others	0	0	0	0	0	0
Related Parties	33	2	35	1	40	2
Total	1 871	100	2 099	100	2 153	100

Depreciation & Amortisation	Depreciation & Amortisation by division	1996		1997		1998	
		million	%	million	%	million	%
		CHF		CHF		CHF	
	Fine chemicals and specialties	100	75	113	74	130	76
	Intermediates and additives	29	22	33	22	38	22
	Energy	5	3	6	4	4	2
	Others	0	0	0	0	0	0
	Total	134	100	152	100	172	100

Research & Development	Research & Development by division	1996		1997		1998	
		million	%	million	%	million	%
		CHF		CHF		CHF	
	Fine chemicals and specialties	88	90	95	90	95	90
	Intermediates and additives	10	10	10	10	10	10
	Energy	0	0	0	0	0	0
	Others	0	0	0	0	0	0
	Total	98	100	105	100	105	100

Investments in property, plant and equipment	By region	1996		1997		1998	
		million	%	million	%	million	%
		CHF		CHF		CHF	
	Switzerland	96	41	122	35	105	26
	EU	56	24	63	18	68	17
	Rest of Europe	16	6	10	2	5	0
	Europe	168	71	195	55	178	43
	North America	60	25	102	29	76	19
	Other areas	9	4	56	16	156	38
	Total	237	100	353	100	410	100

By division	1996		1997		1998		
	million	%	million	%	million	%	
	CHF		CHF		CHF		
	Fine chemicals and specialties	157	66	236	67	194	47
	Intermediates and additives	68	29	99	28	203	50
	Energy	12	5	18	5	13	3
	Others	0	0	0	0	0	0
	Total	237	100	353	100	410	100

Investments calculated at average rates.

Personnel	By production area	1996		1997		1998	
			%		%		%
	Switzerland	2 821	51	2 887	52	2 725	48
	EU	1 533	28	1 365	25	1 435	25
	Rest of Europe	149	2	170	3	186	4
	Europe	4 503	81	4 422	80	4 346	77
	North America	1 053	19	1 052	19	1 068	19
	Other areas	10	0	52	1	237	4
	Total	5 566	100	5 526	100	5 651	100
	Average number of employees						

By division	1996		1997		1998		
		%		%		%	
	Fine chemicals and specialties	4 372	79	4 416	80	4 438	79
	Intermediates and additives	1 115	20	1 032	19	1 145	20
	Energy	68	1	68	1	64	1
	Others	11	0	10	0	4	0
	Total	5 566	100	5 526	100	5 651	100

Significant subsidiaries and affiliates

	Registered Office	Activities	Currency	Share capital in 000 (ITL in billion)
European countries				
<u>Lonza AG</u>	Gampel, CH	□△○	CHF	62 500
<u>Alusuisse-Lonza Energie AG</u>	Visp, CH	○◇	CHF	200
<u>Rheinkraftwerk Neuhausen AG</u>	Neuhausen am Rheinfall, CH	△	CHF	1 000
<u>Aletsch AG</u>	Mörel, CH	△	CHF	20 000
<u>Kraftwerk Lötschen AG</u>	Steg, CH	△○	CHF	25 000
<u>Rhonewerke AG</u>	Ernen, CH	△	CHF	40 000
<u>Salanfe SA</u>	Vernayaz, CH	△	CHF	18 000
<u>Lonza Benelux BV</u>	Breda, NL	○	NLG	250
<u>Lonza France Sàrl</u>	Levallois-Perret, FR	○	FRF	220
<u>Lonza UK Ltd.</u>	Bristol, GB	○	GBP	80
<u>Lonza Biologics plc</u>	Slough, GB	□△○	GBP	4 500
<u>LOFO High Tech Film GmbH</u>	Weil am Rhein, DE	△○	DEM	15 000
<u>Lonza Compounds GmbH & Co. KG</u>	Miehlen, DE	△○	DEM	1 520
<u>Lonza GmbH</u>	Wuppertal, DE	○	DEM	1 000
<u>Lonza Europe BV</u>	Breda, NL	◇	NLG	41
<u>Lonza Biotec sro</u>	Kourim, CZ	△	CSK	137 100
<u>Lonza Spa</u>	Milano, IT	□△○	ITL	100
<u>Lonza Composites srl</u>	Milano, IT	△	ITL	3
<u>Lonza Compounds Spa</u>	Milano, IT	△	ITL	11.5
Other countries				
<u>Lonza Japan Ltd</u>	Tokyo, JP	○	JPY	200 000
<u>Lonza, Inc</u>	Fair Lawn, NJ, US	□△○	USD	697
<u>Lonza Biologics Inc</u>	Porthmouth, NH, US	△○	USD	1
<u>Lonza Singapore Pte Ltd</u>	Singapore, SG	△	SGD	45 500
<u>Lonza Guangzhou Fine Chemicals Ltd</u>	Guangzhou, CN	△	USD	12 000
<u>Alusuisse-Lonza America Inc</u>	New York, NY, US	◇	USD	8

□ *Research/Applications*

△ *Production*

○ *Sales*

◇ *Services/Financing*

Abbreviations of countries and currencies in accordance with ISO standards.

Report of the independent auditors on the historical combined financial statements of Lonza Group Ltd and its subsidiaries

As independent auditors, we have audited the underlying financial statements of the major entities included in the historical combined financial statements of Lonza Group Ltd and its subsidiaries ("the Group"), presented on pages 95 to 117 and consisting of the historical combined balance sheets as of 31 December 1998, 1997 and 1996 and the historical combined statements of income and cash flows (for the years 1998 and 1997 only) and the notes to the historical combined financial statements for the year then ended and we have reviewed the compiling of the historical combined financial statements as described as basis of preparation of the historical combined financial statements. Certain financial statements of subsidiaries included in the historical combined financial statements have been audited by other auditors.

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

Our audit of the underlying financial statements was conducted in accordance with auditing standards promulgated in Switzerland by the profession and with the International Standards on Auditing issued by the International Federation of Accountants (IFAC). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial presentation. We believe that our audit provides a reasonable basis for our opinion. Our review of the compiling of the historical financial statements was conducted in accordance with the International Standards on Auditing issued by the International Federation of Accountants (IFAC) applicable to review engagement. This standard requires that we plan and perform the review to obtain reasonable assurance about whether the financial statements are free of material misstatement. A review is limited primarily to inquiries of company personnel and analytical procedures applied to financial data and thus provides less assurance than an audit.

Without qualifying our opinion, we draw your attention to the basis of preparation of the historical combined financial statements.

In our opinion and based on the work performed, the historical combined financial statements give a true and fair view of the historical combined financial position of the Group as of 31 December 1998, 1997 and 1996 and the combined results of its operations and their cash flows (for the years 1998 and 1997 only) for the years then ended in accordance with the International Accounting Standards of the International Accounting Standards Committee (IASC) and are in accordance with the provisions of the Swiss Law and the accounting principles of the Listing Rules of the Swiss Exchange.

KPMG Fides Peat

Peter Hess
Swiss Certified Accountant
Auditor in Charge

Hanspeter Stocker
Swiss Certified Accountant
Auditor in Charge

Zurich, 27 September 1999