Half-year report 2001

Financial highlights first half-year

million CHF	2000	2001
Net sales continuing	793	**912**
Change in %		15
Operating income continuing	156	**176**
Change in %		13
Operating margin in %	19.7	**19.3**
EBITDA continuing	213	**237**
Change in %		11
EBITDA margin in %	26.9	**26.0**
Operating income group	186	**223**
Change in %		20
Pre-tax earnings	180	**204**
Change in %		13
Net income	141	**153**
Change in %		9
Cash flow	225	**256**
Change in %		14
Net debt	237	**838**
Debt-equity ratio	0.1	**0.5**
Change in %		285
Earnings per share (CHF)	22.1	**27.8**
Change in %		26
Number of employees continuing	4 510	**4 790**
Change in %		6

Driven by marked advances in the Exclusive Synthesis and Biotechnology businesses, Group operating income increased by 20% to CHF 223 million. This improvement, combined with the impact of the share buy-back program completed in January 2001, pushed earnings per share 26% above the prior year to CHF 27.80. The sale of businesses designated as discontinuing is progressing well, with gross proceeds in excess of CHF 1 billion expected by year-end.

Overview

With sales from continuing operations up 15% to CHF 912 million, Lonza Group posted an operating income from continuing operations of CHF 176 million, an improvement of 13% on the previous year. Together with discontinuing operations, which generated earnings of CHF 47 million (57% higher than in 2000), Lonza Group's operating income rose to CHF 223 million, yielding operating margins of 17.0% (15.9% in 2000).

This strong advance was achieved thanks to a better performance from our custom manufacturing and biotechnology activities, more than offsetting the impact of the US economic slowdown on our Performance Chemicals business, which is predominantly US-based. Our Organic Fine Chemical activities held their own in a difficult trading environment. The adverse conditions did not prevent our Discontinuing Operations from staging an outstanding recovery from 2000 levels, with operating income reaching CHF 47 million and margins 11.8% (8% in 2000).

Following the successful share buy-back program completed in January 2001 and the subsequent cancellation of 907 978 shares, or 14.1% of the share capital, the Group's net debt position increased by more than CHF 850 million. This increase resulted in a net financial expense of CHF 16 million compared with CHF 3 million in the same period last year. The tax rate of 25% for the first half is at the low end of Group targets, with full year rates expected to be slightly higher. As a result, net income improved to CHF 153 million, representing a 9% increase over 2000.

Capital expenditure of CHF 112 million was slightly above the prior year, whilst cash flow of CHF 256 million exceeded last year's level by 14%.

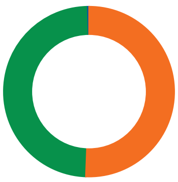
Industrial sales by division first half-year

- Exclusive Synthesis & Biotechnology 44.2%
- Organic Fine & Performance Chemicals 55.6%
- Others 0.2%

Strategic Reorientation and Divestments

As announced at the beginning of the year, Lonza Group has decided to divest businesses which are not aligned with its newly formulated life sciences orientation. Accordingly, the Energy and the Polymer Intermediate businesses of the Group are in the process of being divested. Negotiation of an agreement in principle on the sale of the Energy assets is well advanced, while efforts to find a buyer for the Polymer Intermediates businesses have only recently got underway.

Operating income by division first half-year



Exclusive Synthesis & Biotechnology 50.6%
Organic Fine & Performance Chemicals 48.9%
Others 0.5%

Outlook

Despite the ongoing softness of the global economy and barring any further substantial deterioration in trading conditions, the Group believes that it will be able to improve on its 2000 performance.

Martin Ebner
Chairman

Sergio Marchionne
Managing Director and Chief Executive Officer

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Consolidated income statement first half-year

million CHF	2000	2001
Net sales	793	**912**
Operating expenses	637	**736**
Operating income continuing	156	**176**
Operating income discontinuing	30	**47**
Operating income Group	186	**223**
Goodwill	(3)	**(3)**
Financial income net	(3)	**(16)**
Ordinary income before tax	180	**204**
Income taxes	39	**51**
Net income (loss) incl. minorities	141	**153**
Minorities income	–	**–**
Net income (loss)	141	**153**

Consolidated cash flow statement first half-year

million CHF	2000	2001
Net income	141	**153**
Depreciation	80	**86**
Change in long-term provisions	5	**20**
Expenses (income) from equity method	(1)	**(3)**
Cash flow	225	**256**
Investments	90	**112**

Consolidated balance sheet as per 31 December 2000 and 30 June 2001

million CHF	2000	2001
Fixed assets	1 602	**1 706**
Cash and marketable securities	126	**142**
Advances and loans	20	**23**
Other current assets	833	**919**
Assets held pending disposition	838	**905**
Total assets	3 419	**3 695**
Shareholders' equity	1 854	**1 671**
Minority interests	18	**18**
Long-term debts	121	**68**
Short-term debts	262	**935**
Provisions and other liabilities	1 164	**1 003**
Total liabilities and shareholders' equity	3 419	**3 695**

Changes in shareholders' equity

million CHF	2000	2001
At 31 12 1999/31 12 2000	**2 498**	**1 854**
Dividend	(64)	**(82)**
Spin-off Lonza Group from algroup	11	–
Capital payment to algroup	(277)	–
Buy-back of own shares (incl. own shares as of 31 12 99)	(595)	**(259)**
Net income	309	**153**
Translation difference	(28)	**5**
At 31 12 2000/30 06 2001	**1 854**	**1 671**

Accounting principles

These condensed consolidated financial statements are based on the accounts of the individual subsidiaries at 30 June, which have been drawn up according to uniform Group accounting principles consistent with those adopted by Lonza Group in its consolidated financial statements for the year ended 31 December 2000.

The condensed consolidated accounts are rendered in conformity with the existing International Accounting Standards (IAS), published by the International Accounting Standards Committee (IASC).

For comparative purposes, previous year's segment data has been reclassified to reflect the current corporate structure.

Exchange rates

			Balance sheet rate CHF		Income statement half-year average rate CHF	
			31 12 00	**30 06 01**	2000	**2001**
USA	Dollar	1	1.64	**1.80**	1.65	**1.70**
Great Britain	Pound Sterling	1	2.45	**2.53**	2.59	**2.45**
Germany	Mark	100	77.86	**77.87**	81.07	**78.35**
France	Franc	100	23.22	**23.22**	24.17	**23.36**
Netherlands	Guilder	100	69.11	**69.11**	71.95	**69.53**
Spain	Peseta	100	0.92	**0.92**	0.95	**0.92**
Italy	Lira	100	0.083	**0.079**	0.082	**0.079**

Sales of discontinuing operations of CHF 399 million (2000: CHF 375 million), operating income of CHF 47 million (2000: CHF 30 million) and EBITDA of CHF 69 million (2000: CHF 50 million) are excluded from sales, operating income and EBITDA from continuing operations. All other data, including net income, include the impact of discontinuing operations.

Exclusive Synthesis & Biotechnology first half-year

million CHF	2000	2001
Net sales	280	**403**
Change in %		44
Change due to		
Volume and prices		**125**
Currency translation		**(2)**
Scope of consolidation		**–**
Operating income	64	**89**
Change in %		39
Operating margin	22.9	**22.1**
EBITDA	92	**123**
Change in %		34
EBITDA as % of sales	32.9	**30.5**

Exclusive Synthesis & Biotechnology

With sales of CHF 403 million, 44% up from 2000, the Exclusive Synthesis and Biotechnology division achieved a record operating income of CHF 89 million, 39% higher than in 2000. Operating income margins declined slightly to 22.1% from 22.9%, mainly as a result of a shift in the product mix. These results are due to a sound development of our biotechnology platforms, both microbial fermentation and mammalian cell cultures, and adequate plant loadings for our chemical synthesis business. Growth in the pharmaceutical industry was again the main driving force behind this performance, while demand in the agrochemicals market was little changed compared with the previous year.

Exclusive Synthesis – Our business with the pharmaceutical industry was strong, driven by new products in the cardiovascular, pain-control and anti-viral/HIV-related areas. We continued to foster our key supplier position with leading pharmaceutical companies. Results from agro-intermediates for the production of sulfonylurea herbicides were good, but tempered by negative developments in other agrochemical intermediates and active substances.
Despite an increasingly competitive environment, our pharmaceutical R&D pipeline is well loaded. However, the number of projects in early clinical testing is increasing, necessitating an expansion of Lonza's capabilities in this area. Capital has already been committed and the new capacity will become operational in the latter part of 2002.

Biotechnology – The business area of microbial fermentation experienced strong growth in both sales and operating income, with contract manufacturing efforts beginning to show substantial results. Industrial-scale production of an intermediate for an anti-viral treatment was successfully implemented and validated at our Kourim (CZ) plant.
The market introduction of a new proprietary L-carnitine derivative further strengthened our position in the dietary supplement segment. With the Kourim (CZ) plant now running at high utilization rates, the Group has initiated measures to overcome the bottleneck in the current manufacturing process and substantially increase reactor volumes.
Progress in our mammalian cell fermentation business is based on the growing number of biopharmaceuticals moving through clinical trials to the stage of market approval. The availability of manufacturing capacity remains tight worldwide. As a result, our development services and all available production facilities were fully booked in the first half of the year. Capacity at our fermenters was restricted by ongoing expansion work and revalidation shutdowns and inspections required by various regulatory bodies in conjunction with the start-up of full production in the second half of this year.
On the R&D side, there was significant progress in the development of serum-free, chemically-defined media and simplified purification procedures. Additionally a number of license agreements have been concluded for our proprietary GS (glutamine synthetase) system. The expansion projects in Portsmouth (US) and Slough (UK) are on schedule, with the first phase coming on stream in Slough in the final quarter of 2001. These measures will enable us to meet contracted customer commitments for the next five years.

Organic Fine & Performance Chemicals first half-year

million CHF	2000	2001
Net sales	510	**507**
Change in %		(1)
Change due to		
Volume and prices		**(9)**
Currency translation		**6**
Scope of consolidation		**–**
Operating income	96	**86**
Change in %		(10)
Operating margin	18.8	**17.0**
EBITDA	125	**113**
Change in %		(10)
EBITDA as % of sales	24.5	**22.3**

Organic Fine & Performance Chemicals

The division's operating income decreased to CHF 86 million, CHF 10 million below the prior year, while the operating margin fell to 17.0% (18.8% in 2000). Sales remained almost stable at CHF 507 million. The division was adversely affected by the substantial decline in US economic activity and high raw material input prices, especially in the first quarter of this year.

Organic Fine Chemicals – Demand for the sector's products remained buoyant. Higher dollar exchange rates helped to lessen the negative impact of persistently high raw-material and energy prices. Sales of nicotinates (a vitamin of the B complex) were strong, with Lonza retaining its global leadership, driven mainly by increased market penetration in feed applications for poultry. Demand for malononitrile – a building block for the production of vitamin B_1 and a number of pharmaceuticals – was very strong. Additional production capacity, based on a new and more economic production process, will be started up in October 2001.
Sales of intermediates to agrochemical producers remained stable although prices were still under pressure from Asian-based manufacturers. Sales of Meta® – a molluscicide – were at an all-time high due to the climatic conditions in autumn and spring, favoring high slug populations and therefore multiple usage of slug pellets in all markets – except the US.

Volumes of organic intermediates for application in the pigment industry were low compared with last year, and prices suffered because of competitive pressure from Asian producers. A new facility for the production of acetoacetanilide – an arylide for the pigment and agrochemical production – was successfully started up. Demand for intermediates for the electronics industry was also lower, mainly due to the economic downturn in the US.

Performance Chemicals – A weak US trading environment impacted our operations, especially in the first quarter of 2001. To cope with the unsatisfactory US situation, restructuring measures were implemented in the second quarter in order to align the cost structure with market conditions.
Good performances in Europe, Latin America and the Asia-Pacific region were insufficient to offset our weak US businesses, notwithstanding several positive product developments. In biocides, growth of quaternary ammonium compounds and amine oxide products was achieved in the wood-protection market. Initial sales of products for new antibacterial hygiene applications are promising. Sales of biocidal products used to counter foot-and-mouth disease in Europe were up. Finally, halogenated hydantoins continued to gain acceptance as paper-mill slimicides in the United States, Europe and the Asia-Pacific region.
In the oleochemicals segment, the business with kosher ester products in food applications performed well, and interest in kosher fatty-acid products picked up in the second quarter.

Discontinuing Operations first half-year

million CHF	2000	2001
Net sales	375	**399**
Change in %		6
Change due to		
Volume and prices		**32**
Currency translation		**(8)**
Scope of consolidation		**–**
Operating income	30	**47**
Change in %		57
Operating margin	8.0	**11.8**
EBITDA	50	**69**
Change in %		38
EBITDA as % of sales	13.3	**17.3**

Discontinuing Operations

On the back of a significant recovery in the area of polymer intermediates together with stable results in the energy sector, discontinuing operations showed a significant margin improvement during the first half of 2001 to 11.8% from 8.0% in the previous year. Operating income came in at CHF 47 million on sales of CHF 399 million.

Polymer Intermediates – The sector achieved a significant margin improvement thanks to falling raw material prices, good volume growth and a successful, albeit limited, pass-through of past conversion cost increases.

Realignment of ownership and shutdown of capacity in Europe have already provided a more balanced supply/demand environment for our major building blocks. Further decisions are expected during the second half 2001 to complete the planned rationalization in these sectors.

Sales of trimellitic anhydride and special plasticizers continued to grow despite the overall flatness of demand, particularly in US. Demand for phthalic anhydride and general purpose plasticizers made uneven progress over the semester, with weaker conditions during the second quarter affected by the general economic downturn in the most important European economies and the absence of exports to Far Eastern markets. Sales of maleic anhydride and derivatives recovered from last year's low levels. Margins improved on the back of stable prices, coupled with a sharp reduction in raw material costs. Despite a weak European market, resins and compounds maintained stable volumes and improving margins.
Purified isophthalic acid produced in Singapore delivered excellent sales volumes, although an extremely poor pricing environment persists. Some movement has been achieved in the second quarter, with additional margin improvements expected in the second half of the year. The catalyst and technology business performed according to expectations, with new catalysts for the formaldehyde sector being successfully launched.

Energy – The favorable weather conditions resulted in above-average energy production, without reaching the prior year's levels.
Net sales were up nearly 8% thanks to the acquisition of additional customers. The business is expected to deliver results in line with the previous years.