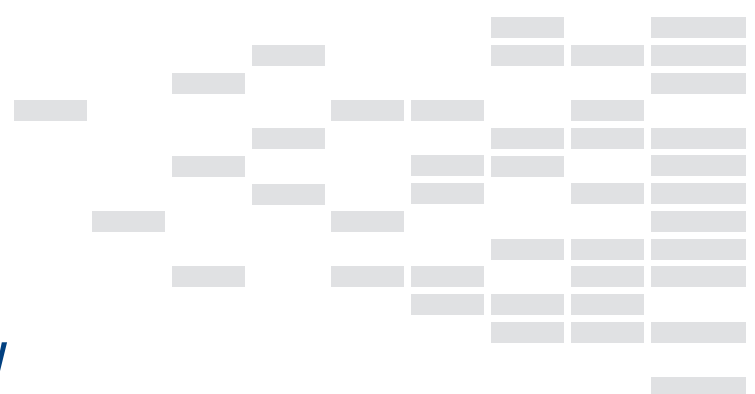


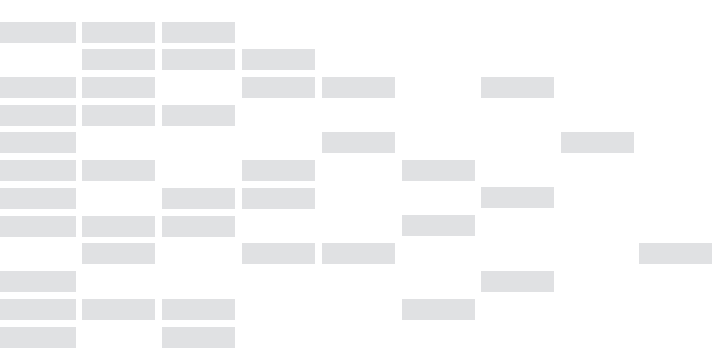
Engineering
the Medicines
of Tomorrow



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MorphoSys Group: Three Months' Financial Report 2003

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Dear Shareholders,

During the first quarter of 2003, MorphoSys made excellent progress in the development of therapeutic antibodies for its partners and its own account. As an example of this progress, Bayer purchased a license for the exclusive right to develop a HuCAL® antibody. The acquired license was for a HuCAL® antibody against an undisclosed, solid tumor cancer target molecule. The antibody, generated by Bayer using the MorphoSys HuCAL® antibody library, demonstrated significant anti tumor efficacy in several animal tumor models. Bayer intends to further characterize the antibody in additional pre-clinical studies and thereafter develop it in clinical trials in major solid tumor indications.

Furthermore, the conclusion of a collaboration and cross licensing agreement with Boehringer Ingelheim was announced in February. Under the agreement, Boehringer Ingelheim received options for exclusive licenses for two targets, against which antibodies will be made using the HuCAL® GOLD antibody library. In return MorphoSys received from Boehringer Ingelheim an exclusive worldwide license to develop and commercialize antibodies against the ICAM-1 molecule. The ICAM-1 target is the basis for MorphoSys's proprietary product programs, MOR101 and MOR102, which focus on the inflammation indications of deep dermal burn and psoriasis, respectively.

Additionally, an agreement was signed in January with UK-based Lonza Biologics allowing MorphoSys and its partners access to antibody manufacturing capabilities through a production and supply agreement over the next five years. With such access, MorphoSys can offer its partners manufacturing capacities at Lonza, thereby increasing the value of its proprietary pre-clinical deals.

In the area of intellectual property, MorphoSys also continued to make good progress. After having settled the longstanding litigation with Cambridge Antibody Technology (CAT) in December 2002 without restrictions to the Company's ability to practice, good news continued in the form of a positive recommendation from the Magistrate Judge in the Applied Molecular Evolution (AME) case. In the Magistrate Judge's report, the MorphoSys motion for non-infringement of AME's patents was allowed, and AME's motion for patent infringement was denied. Should the District Court adopt the Magistrate's recommendation, all of AME's claims will be decided in favor of MorphoSys.

Finally, MorphoSys was admitted in January 2003 to the Prime Standard segment on the Frankfurt Stock Exchange. As a Prime Standard Company, MorphoSys will continue as in prior years to meet some of the highest transparency standards in Europe. In addition, the Company's restructuring efforts announced in November 2002, were substantially completed during the first quarter of 2003, which in turn will provide the foundation and platform for growth of the business in the future.

We look forward to a successful year in 2003 and thank you for your continued interest and confidence in us.



Dave Lemus
Chief Financial Officer
MorphoSys AG

Group Management Report Q1 2003

Industry Overview

The war in Iraq and related economic uncertainties weighed upon the minds of investors during the first quarter of 2003. As a result, the DAX stock index fell below 2,200 points during the quarter, the lowest level since 1996.

In the biotechnology industry, consolidation moves were more prevalent during the first quarter of 2003, as companies seek greater critical mass. In Europe, Eurofins announced the takeover of Genescan, British Biotech merged with RiboTargets, and by the end of the quarter, several parties had made bids for Oxford Glycosciences.

Despite positive news from the Company, the price of the MorphoSys share experienced significant profit-taking on the back of the substantial share price appreciation at year-end 2002, with the share price dropping 44%. In comparison the Deutsche Börse's Prime Pharma & Healthcare Index fell 3%, and the NASDAQ Biotech index increased by 3%.

Financial Analysis

Operating Revenues

Compared to the same period of the previous year, cumulative revenues for the first three months of 2003 decreased by 8% to EUR 3.7 million (March 31, 2002: EUR 4.1 million), in line with expectations. Revenues arising from therapeutic antibody collaborations accounted for 85% of total revenues while target research collaborations generated 14% of the total. Approximately 84% of total Company revenues arose from MorphoSys' three largest alliances, and included Centocor, Bayer and Schering.

Geographically, 79% of MorphoSys' EUR 3.7 million commercial (non-grant) revenues were generated with biotechnology and pharmaceutical companies located in the United States, and 21% generated in Europe.

Operating Expenses

For the first three months of 2003, total operating expenses, including stock-based compensation expense decreased by EUR 1.8 million to EUR 5.5 million (March 31, 2002: EUR 7.3 million), resulting in an operating loss of EUR 1.7 million (March 31, 2002: EUR 3.3 million), a decrease of the loss over the same period in the prior year of 48%. The reduction in expense was in line with expectations, and resulted from the Company restructuring implemented in Q4 2002.

Research and Development Expenses

Costs for Research and Development decreased by EUR 0.9 million to EUR 2.7 million (March 31, 2002: 3.6 million). The decrease in Research and Development expenses resulted predominantly from lower costs for intangibles, which decreased from EUR 1.5 million to EUR 0.3 million compared to the same period in the prior year. The intangibles reduction resulted mainly from lower cost in the amortization of sublicense fees.

Sales, General and Administrative Expenses

Sales, General and Administrative expenses amounted to EUR 2.2 million compared to EUR 2.6 million in the same period of the previous year. The decrease in General and Administrative expenses was mainly due to the decrease in patent litigation costs as a result of the settlement with Cambridge Antibody Technology (CAT) in December 2002.

Stock-Based Compensation

Stock-based compensation in the amount of EUR 0.5 million for the first three months was recorded as a non-cash charge in the first quarter of 2003 (March 31, 2002: EUR 1.1 million), which results from application of SFAS No. 123 (expensing of stock options) under U.S. GAAP accounting. The decrease in stock based compensation is mainly due to the fact that no convertible bonds were granted in the first quarter of 2003 compared to the same period in the previous year.

Cost by Expenditure Type

For the first three months of 2003, the Company's personnel cost in the amount of EUR 1.9 million (excluding stock based compensation) accounted for approximately 35% of total operating costs, representing the largest single cost-type for the Company. Costs for external services, infrastructure and intangibles were the next largest blocks of costs for the first three months of 2003 and represented 23%, 12% and 12%, respectively, of total operating costs for the first three months of 2003.

Non-Operating Items

Non-operating income decreased by 150% to a loss of EUR 0.1 million (March 31, 2002: EUR 0.2 million), mainly due to losses resulting from foreign currency transactions (U.S.\$/EUR). The aforementioned amount was composed of exchange rate losses of EUR 0.2 million and capital gains on sale of these investments in the amount of EUR 0.1 million. In addition the company recorded interest expense of EUR 0.1 million on certain obligations to CAT.

Net Loss

For the first three months of 2003, the Company posted a net loss of EUR 1.8 million compared to EUR 3.1 million in the same period of the previous year. The decreased loss in 2003 of EUR 1.3 million was mainly due to lower intangibles associated expenses and savings in connection with the closing of the MorphoSys U.S.A., Inc. The resulting loss per share for the first three months 2003 amounted to EUR 0.46 (March 31, 2002: EUR 0.80).

Liquidity / Cash Flows

During the first quarter the Company's current assets decreased by EUR 4.9 million to EUR 24.6 million compared to EUR 29.5 million at December 31, 2002. On March 31, 2003, the Company had EUR 21.3 million in cash and cash equivalents, and marketable securities, compared to a EUR 19.1 million balance at December 31, 2002. The increase was primarily due to an inflow of funds from collaboration partners in the first quarter of 2003. Cash used in operating activities for the first three months of 2003 amounted to EUR 2.5 million compared to EUR 4.0 million in the first three months of 2002.

Assets

Total assets decreased by EUR 5.3 million to EUR 37.1 million at the end of March 2003, compared to EUR 42.4 million at December 31, 2002. The main reasons include the following: accounts receivable decreased within the first three months of 2003 by EUR 6.7 million, and cash, cash equivalents and marketable securities increased in the same period by EUR 2.2 million.

Liabilities

Total current liabilities decreased by EUR 3.7 million mainly due to the decrease in licenses payable by EUR 1.2 million, a decrease in accounts payable of EUR 0.6 million, and a decrease in deferred revenues of EUR 1.3 million. The decrease in licenses payable results partly from the payment of certain obligations under the settlement agreement with CAT. Total non-current liabilities of EUR 2.3 million at the end of March 2003 remained unchanged compared to December 31, 2002.

Equity

In 2002, MorphoSys signed licensing agreements with XOMA and CAT. Under the XOMA licensing agreement, the Supervisory Board resolved in October 2002 to issue 363,466 shares to XOMA as a capital increase against contribution in kind. In December 2002, MorphoSys signed a settlement with CAT to resolve long-standing patent litigation issues. As part of the agreement, MorphoSys will issue to CAT 588,160 MorphoSys shares as partial consideration for the CAT license.

Both the XOMA and CAT share issuances are expected to take place in 2003, and are subject to registration in the commercial register. The respective share issuances exclude shareholders' preemptive rights as allowed under the Company's articles of association. As of March 31, 2003, neither capital increase had been registered at the Commercial Register in Germany.

Capital Expenditure

During the first three months of 2003 and 2002, total investment in intangibles amounted to EUR 0.02 million and EUR 4.7 million, respectively. Amortization of capitalized intangibles for the first three months of 2003 amounted to EUR 0.3 million compared to EUR 1.6 million in the same period of the previous year which included amortization of a purchased license in the first quarter of 2002.

Investment in Property and Equipment amounted to EUR 0.1 million in the first three months of 2003 compared to EUR 0.2 million in the same period of the previous year. Depreciation for the first three months of 2003 of EUR 0.2 million remained unchanged compared to the same period in the previous year.

Human Resources

Number of Employees

On March 31, 2003, the MorphoSys Group employed 87 employees (compared to 111 employees on December 31, 2002). Of the 87 employees, 67 worked in research and development and 20 in sales, general and administrative positions. Of these employees, 34 held a Ph.D. degree at the end of the first three months of 2003, down from 45 at the end of 2002. The Company employed an average of 87 people for the first three months of 2003 (2002: 110).

Research & Development / Partnered Research

As announced in November 2002, MorphoSys has scaled back its plans for the clinical development of proprietary drug candidates, and is now focusing on the commercialization of these programs as pre-clinical drug candidates.

Proprietary Product Development

During the first three months of the year, MorphoSys continued to work on its proprietary antibody programs MOR101, MOR102 and MOR201. Also during the quarter, MorphoSys received its exclusive, worldwide license from Boehringer Ingelheim for antibodies against ICAM-1, which form the basis for programs MOR101 and MOR102. Both antibody programs are in pre-clinical development.

Partnered Product Development

Bayer AG

During Q1 2003, Bayer purchased a license for the exclusive right to develop a HuCAL® antibody. The acquired license is for an antibody against an undisclosed, solid tumor cancer target molecule. The antibody was generated and characterized by Bayer Biotechnology (Berkeley, CA, U.S.A.) using the MorphoSys HuCAL® antibody library, and has demonstrated efficacy in several in vitro and in vivo assays. Bayer demonstrated significant anti tumor efficacy in several animal tumor models. Bayer intends to further characterize the antibody in additional pre-clinical studies and thereafter develop it in clinical trials in major solid tumor indications.

MorphoSys and Bayer signed a wide-ranging antibody collaboration in December 1999. In July 2001 the collaboration was extended for four additional years, focusing on the generation of human antibodies for therapeutic, diagnostic and genomics applications. Bayer retains further options to acquire exclusive licenses for therapeutic antibody programs.

Boehringer Ingelheim

MorphoSys and Boehringer Ingelheim entered into a therapeutic antibody collaboration and cross licensing agreement in February. Under the terms of the agreements, MorphoSys received an exclusive, worldwide license to patents owned or controlled by Boehringer Ingelheim to develop, make and sell therapeutic and diagnostic antibodies targeting the ICAM-1 molecule. Boehringer Ingelheim will receive options for exclusive commercial licenses to therapeutic antibodies against two undisclosed targets, against which MorphoSys will generate fully human antibodies utilizing its HuCAL® GOLD antibody technology.

MorphoSys will develop fully human antibodies against ICAM-1, utilizing its proprietary HuCAL® GOLD technology, in two areas relating to inflammation. In the first program, MOR101, an antibody fragment is being developed in the indication of deep dermal burn. MOR102, the second antibody program, will be developed for the treatment of psoriasis. The fully human HuCAL® antibodies against ICAM-1 are expected to have excellent efficacy profiles in these inflammatory disorders while having none of the immunogenic side effects associated with a mouse antibody against the same target that was developed by Boehringer Ingelheim. MorphoSys expects to partner these compounds before entering clinical trials.

Lonza Biologics

In January, MorphoSys signed an agreement with Lonza Biologics for production and supply of clinical grade antibody drugs derived from MorphoSys HuCAL® technology within the next five years. The agreement regulates access to Lonza's process development and manufacturing capacity for future antibody projects for both MorphoSys' own and partnered therapeutic antibody projects.

MorphoSys will offer its partners manufacturing capacities at Lonza, thereby increasing the value of its pre-clinical deals.

Intellectual Property

MorphoSys continued to make good progress in the area of intellectual property. In December 2002, the Company terminated in a settlement agreement the multi-year patent litigation with Cambridge Antibody Technology (CAT).

In addition, in January 2003 MorphoSys confirmed that it has received a positive "Report and Recommendation" from the Magistrate Judge to the District Judge for the District Court in Boston, Massachusetts, USA, in the legal action filed by Applied Molecular Evolution (San Diego/CA, USA; "AME") against MorphoSys AG and MorphoSys USA, Inc. The Magistrate Judge recommended that MorphoSys' motion for summary judgment of non-infringement be allowed and that AME's motion for partial summary judgement of infringement be denied. The Magistrate Judge's Report and Recommendation now goes to the District Judge for final adoption. If the District Judge adopts the recommendation of the Magistrate Judge that MorphoSys is not infringing the Kauffman patents, all of AME's claims will be fully resolved in favor of MorphoSys.

Risk Report

The global business activities of MorphoSys are exposed to a number of risks which are intrinsic to the running of any business. MorphoSys' risk management system is actively employed in the routine identification, assessment and control of risks as an integral part of its normal business operations. The risks mentioned in this report, albeit not all inclusive, may influence the Company's operations and its financial conditions.

Marketing Risks/Competition

MorphoSys earns its revenues from the commercialization of its technologies through the out-licensing of its antibody libraries. Risks which could impede the growth of these revenues include difficulties in attaining market acceptance and slow market growth. In turn, this could lead to reduced revenues and business activities. MorphoSys plans to continue its partnering strategy. New and existing partners help to validate MorphoSys technologies and provide meaningful financial resources. Furthermore, partnerships contribute to the medium and long-term growth of MorphoSys through the payment of clinical milestones and royalties to the Company. Presently, a substantial portion of MorphoSys' revenues is generated within the scope of a few collaborations. As such, acquiring further significant collaborations of similar size and scope is a very high priority. Therefore, the ability of MorphoSys to maintain its competitive standing among increasing numbers of new entrants to the fully human antibody technology market is of significance to the short, medium, and long-term success of the Company.

R&D/Technology Risks

The worldwide markets for the antibody technology of MorphoSys are characterized by strong competition. Other companies may develop superior or more cost-effective technologies or therapeutics. The market for innovative therapeutics is characterized by rapid technological change and frequent introduction of novel solutions to partners' problems. MorphoSys' success will depend on its ability to keep pace with potential customers' changing needs. With its latest development, HuCAL® GOLD, MorphoSys believes it is strategically well positioned for the near to mid-term future. To the extent that therapeutic antibodies are developed into the clinic and marketed as drugs, MorphoSys directly, or through its partners, faces the same risk as all product-based biotechnology companies: more specifically, the low success rates of drugs emerging from clinical development.

IP Risks

The field of phage display, in which the Company is active, is relatively new and the intellectual property position of the various parties involved is becoming increasingly complex and litigious. The possibility that further patent suits could be brought by companies possessing existing patents or patents which have not yet been granted, or which the Company is not currently aware of, cannot be ruled out. Having recently settled the multi-year patent litigation dispute with CAT in December 2002, there is currently only one ongoing patent dispute, with Applied Molecular Evolution ("AME"). In January 2003, MorphoSys received a preliminary recommendation in its favor from the Magistrate Judge presiding in the case. MorphoSys remains confident of the chances of a successful outcome of this litigation issue, and therefore has included no provisions for contingent liabilities as they regard to this case. Furthermore, MorphoSys has strengthened its own proprietary patent estate in the last years. Most recently, in June 2002, the Company received its third patent on its HuCAL[®] antibody library, in Europe. HuCAL[®] patents had already been granted in 2000 and 2001 in Australia and in the U.S., respectively.

Outlook

The implementation of last year's restructuring measures was successfully completed at the end of the first quarter of 2003. With these measures in place, MorphoSys will significantly reduce its cash burn in 2003 compared to the prior year. Additionally, savings arising from the settlement agreement in December 2002 with CAT, will also serve to reduce intellectual property costs. As a result, R&D and S,G&A costs are expected to be significantly less in 2003 compared to the prior year. In summary, MorphoSys believes it has thereby put measures into place in order to preserve cash resources at least into the year 2006.

During the year the Company will strive to expand its partnered antibody generation business, as well with the outlicensing of its proprietary pre-clinical product candidates, thereby creating significant value for the Company.

Consolidated Balance Sheet (U.S. GAAP)

	03/31/2003 EURO	12/31/2002 EURO
Assets		
Current Assets		
Cash and Cash Equivalents	219,430	842,082
Marketable Securities	21,121,630	18,274,338
Accounts Receivable	2,065,810	8,732,790
Prepaid Expenses and Other Current Assets	1,187,897	1,684,729
Total Current Assets	24,594,767	29,533,939
Property and Equipment, Net	1,990,503	2,097,796
Patents, Net	6,700,780	6,898,990
Prepaid License Fees, Net	3,257,347	3,352,604
Other Assets	560,599	509,984
Total Assets	37,103,996	42,393,313
Liabilities and Stockholders' Equity		
Current Liabilities		
Accounts Payable	1,678,404	2,273,539
Licenses Payable	4,409,731	5,569,291
Deferred Revenue	6,750,228	8,086,355
Accrued Employees Benefits	835,021	1,468,907
Other Accrued Expenses and Liabilities	2,035,157	2,029,608
Total Current Liabilities	15,708,541	19,427,700
Non-Current Liabilities		
Other Non-Current Liabilities	2,275,348	2,275,347
Convertible Bonds Due to Related Parties	68,200	74,800
Total Non Current Liabilities	2,343,548	2,350,147
Stockholders' Equity		
Common Stock, EUR 3.00 Par Value; 7,345,582 and 7,345,582 Ordinary Shares Authorized; 3,949,706 and 3,949,706 Ordinary Shares Issued; 3,889,944 and 3,889,944 Ordinary Shares Outstanding;	11,849,118	11,849,118
Treasury Stock (59,762 and 59,762 shares for 2003 and 2002, respectively), at cost	(21,934)	(21,934)
Additional Paid-in Capital	59,655,007	59,193,912
Accumulated Other Comprehensive (Loss)/ Income	(754,733)	(517,591)
Accumulated Deficit	(51,675,551)	(49,888,039)
Total Stockholders' Equity	19,051,907	20,615,466
Total Liabilities and Stockholders' Equity	37,103,996	42,393,313

See accompanying notes

Consolidated Statement of Operations (U.S. GAAP)

	03/31/2003 EURO	03/31/2002 EURO
Revenues	3,744,046	4,061,041
Operating Expenses		
Research and Development	2,740,162	3,563,291
General and Administrative	2,248,421	2,625,632
Stock Based Compensation	461,095	1,139,841
Total Operating Expenses	5,449,678	7,328,764
Loss from Operations	(1,705,632)	(3,267,723)
Interest Income	20,066	86,098
Other Income (Expenses), Net	(101,946)	105,442
Loss before Taxes	(1,787,512)	(3,076,183)
Foreign Income Tax Expense	–	23,705
Net Loss	(1,787,512)	(3,099,888)
Basic and Diluted Net Loss per Share	(0.46)	(0.80)
Shares Used in Computing Basic and Diluted Net Loss per Share	3,889,944	3,889,449

See accompanying notes

Consolidated Statement of Changes in Stockholders' Equity (U.S. GAAP)

	Common Stock		Treasury Stock		Additional Paid-in Capital EURO	Accumulated Other Com- prehensive Gain (Loss) EURO		Accumulated Deficit EURO	Total Stockholders Equity EURO
	Shares	EURO	Shares	EURO		EURO	EURO		EURO
	Balance at Jan. 1, 2002	3,591,331	10,773,275	59,762		(21,934)	32,452,966		37,047
Exercise of Stock Options	495	1,485	—	—	7,177	—	—	8,662	
Compensation Related to the Grant of Stock Options	—	—	—	—	3,940,412	—	—	3,940,412	
Capital Increase for Euro Conversion	—	718	—	—	(718)	—	—	—	
Capital Increase against Cash, Net of Issuance Cost of EUR 25,249	357,880	1,073,640	—	—	22,794,075	—	—	23,867,715	
Other Comprehensive Loss: Change in Unrealized Losses on Available for Sales Securities	—	—	—	—	—	(557,178)	—	(557,178)	
Foreign Currency Gain from Consolidation	—	—	—	—	—	2,540	—	2,540	
Net Loss	—	—	—	—	—	—	(24,377,294)	(24,377,294)	
Comprehensive Loss	—	—	—	—	—	—	—	(24,931,932)	
Balance at Dec. 31, 2002	3,949,706	11,849,118	59,762	(21,934)	59,193,912	(517,591)	(49,888,039)	20,615,466	
Compensation Related to the Grant of Stock Options	—	—	—	—	461,095	—	—	461,095	
Other Comprehensive Loss: Change in Unrealized Losses on Available for Sales Securities	—	—	—	—	—	(243,666)	—	(243,666)	
Foreign Currency Gain from Consolidation	—	—	—	—	—	6,524	—	6,524	
Net Loss	—	—	—	—	—	—	(1,787,512)	(1,787,512)	
Comprehensive Loss	—	—	—	—	—	—	—	(2,024,654)	
Balance at March 31, 2003	3,949,706	11,849,118	59,762	(21,934)	59,655,007	(754,733)	(51,675,551)	19,051,907	

See accompanying notes

Consolidated Statement of Cash Flows (U.S. GAAP)

For the Period ended March 31,	2003 EURO	2002 EURO
Operating Activities		
Net Loss	(1,787,512)	3,099,888)
Adjustments to Reconcile Net Loss to Net Cash Used for Operating Activities:		
Depreciation	220,444	207,437
Amortization of Intangible Assets	308,407	1,590,027
Net Gain on Sales of Marketable Securities	(115,948)	(25,115)
(Gain) / Loss on Sale of Property and Equipment	(236)	(145)
Recognition of Deferred Revenue	(1,711,126)	(1,662,698)
Stock-Based Compensation	461,095	1,139,841
Changes in Operating Assets and Liabilities:		
Accounts Receivable	6,666,980	1,579,170
Prepaid Expenses and Other Assets	446,217	(1,427,384)
Accounts Payable	(595,135)	(309,617)
Licenses Payable	(1,159,560)	4,574,565
Deferred Revenue	374,999	1,995,025
Accrued Employee Benefits	(633,886)	(511,683)
Other Accrued Expenses and Liabilities	5,549	(33,046)
Other Non Current Liabilities	–	–
Net Cash Used in Operating Activities	2,480,288	4,016,489
Investing Activities:		
Purchases of Marketable Securities	(7,927,080)	(4,847,310)
Proceeds from Sales of Marketable Securities	4,952,073	2,606,633
Purchases of Property and Equipment	(133,387)	(167,341)
Proceeds from Disposals of Property and Equipment	20,470	240
Additions to Intangibles	(14,940)	(4,712,918)
Net Cash Provided by (Used in) Investing Activities	(3,102,864)	(7,120,696)
Financing Activities:		
Proceeds from the Issuance of Common Stock, net (Refunds)/Proceeds from the Issuance of Convertible Bonds to Related Parties	– (6,600)	23,892,964 91,300
Cost of Share Issuance	–	(15,797)
Net Cash Provided by Financing Activities	(6,600)	23,968,467
Effect of Exchange Rate Differences on Cash	6,524	(4,148)
Net (Decrease)/ Increase in Cash and Cash Equivalents	(622,652)	20,860,112
Cash and Cash Equivalents at the Beginning of the Period	842,082	4,025,334
Cash and Cash Equivalents at the End of the Period	219,430	24,885,446
Supplemental Disclosures of Cash Flow Information:		
Cash Received/(Paid) During the Year for Foreign Income Taxes	–	(23,705)
Capital Increase against Cash	–	23,892,964
Unrealized (Loss)/Gain on Marketable Securities	(243,666)	22,095
License to be Settled in Equity	3,160,386	–
See accompanying notes		

Notes to the Consolidated Financial Statements

1 Organization and Summary of Significant Accounting Policies

Business and Organization

MorphoSys AG ("the Company") is a biotechnology company using combinatorial biology in drug discovery with the principal objective of developing and commercially exploiting new enabling technologies across a broad scientific spectrum. The Company was founded in July 1992 as a German limited liability company. In June 1998, MorphoSys AG was transformed into a German stock corporation. In March 1999, the Company went public on Germany's Neuer Markt, the stock exchange designated for high-growth enterprises. On January 15, 2003 MorphoSys AG was admitted to the Prime Standard segment of the Frankfurt Stock Exchange.

Substantially all operations are located in Germany. The Company has two wholly owned subsidiaries:

- MorphoSys U.S.A., Inc., which was incorporated in the United States on February 16, 2000. The subsidiary's purpose is to assist the Company in the sale and licensing of MorphoSys AG products. MorphoSys U.S.A., Inc. substantially ceased its operations in November 2002. MorphoSys IP GmbH, which was incorporated in Munich, Germany, on November 6, 2002. The subsidiary's purpose is to purchase, maintain and administer certain intangible assets of the MorphoSys Group. The Company's operations are physically located at the premises of MorphoSys AG, and the operations of MorphoSys IP GmbH commenced on December 31, 2002.
- The accompanying consolidated financial statements reflect the application of certain significant accounting policies as described in this note and elsewhere in the accompanying consolidated financial statements and notes.

Basis of Financial Statement Presentation

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP). Accordingly, the Company has recorded certain adjustments, principally relating to revenue recognition and the recording of certain costs, in order to present the accompanying financial statements in accordance with U.S. GAAP.

Use of Estimates

The preparation of the consolidated financial statements in conformity with accounting standards generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Cash and Cash Equivalents

The Company considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. The Company invests its cash in deposits with two major German financial institutions, mainly in money market funds.

Consolidation

The accompanying financial statements consolidate the financial position, results of operations, and cash flows of MorphoSys AG and MorphoSys U.S.A., Inc. and MorphoSys IP GmbH. All intercompany transactions and balances have been eliminated.

Marketable Securities

The Company accounts for its securities using Statement of Financial Accounting Standards ("SFAS") No. 115, "Accounting for Certain Investments in Debt and Equity Securities." Management determines the proper classifications of securities at the time of purchase and reevaluates such designations as of each balance sheet date. At March 31, 2003 and at December 31, 2002, such securities that are classified as available-for-sale are carried at market value with unrealized gains and losses reported in accumulated other comprehensive income, which is a separate component of stockholders' equity. Realized gains and losses on sales of investments, as determined on a specific identification basis, are included in the statements of operations when the investment is sold or matures.

Property and Equipment

Property and equipment is stated at cost, less accumulated depreciation and amortization. Major replacements and improvements are capitalized while general repairs and maintenance are charged to expense as incurred. Assets are depreciated over three to ten years using the straight-line method. Leasehold improvements are amortized over the estimated useful lives of the assets or the related lease term, whichever is shorter.

Revenue Recognition

The Company's revenues include technology access fees; fees earned from research and development collaboration agreements mainly with companies based in the United States. Revenue related to non-refundable technology access fees, subscription fees and license fees are deferred and recognized on a straight-line basis over the relevant periods of the agreement, generally the research term or the estimated useful life of the collaboration for those contracts without a stipulated term unless a more accurate means of recognizing revenue is available. Research and development collaboration service fees are recognized in the period that the services are provided. Milestone revenues are recognized upon achievement of certain criteria.

Investment grants from governmental agencies for the support of specific research and development projects are recorded as revenue to the extent the related expenses have been incurred: Under the terms of the investment grants, the governmental agencies generally have the right to audit the use of the payments received by the Company.

Segment Reporting

The Company operates primarily in one business segment related to the development of antibody therapeutics within the Biotech-Industries. Accordingly the Company does not disclose significant additional segment information under the definition of segment reporting, defined by the standards of SFAS No. 131, "Disclosure About Segments of an Enterprise and Related Information."

Research and Development

Research and development costs are expensed as incurred.

Stock-Based Compensation

The Company applies the provisions of SFAS No.123 "Accounting for Stock-Based Compensation," which requires the Company to record the estimated fair value of stock options and other awards at the grant date as compensation expense over the period in which the employees render the services associated with the award.

Foreign Currency Translation

Investments in foreign affiliates have been translated into euro in accordance with SFAS No. 52, "Foreign Currency Translation". All balance sheet accounts have been translated using the exchange rates in effect at the balance sheet date. Income statement amounts have been translated using the average exchange rate for the year. The gains and losses resulting from the changes in exchange rates from year-to-year have been reported in accumulated other comprehensive income.

Net Loss Per Share

Basic and diluted loss per share is calculated in accordance with SFAS No. 128, "Earnings per Share". Basic loss per share is based upon the number of weighted-average shares of common stock outstanding for the respective years.

Impairment of Long-Lived and Identifiable Intangible Assets

The Company evaluates the carrying value of long-lived assets and identifiable intangible assets for potential impairment on an ongoing basis by comparing projected undiscounted cash flows associated with such assets to the related carrying value. An impairment loss would be recognized when the estimated undiscounted future cash flows are less than the carrying amount of the asset. An impairment loss would be measured as the amount by which the carrying value of the asset exceeds the fair value of the asset, based upon a discontinued cash flow analysis.

Patent Costs

The Company capitalizes costs related to obtaining patents and protecting granted patents from infringement. Capitalized costs principally relate to the costs of legal counsel. Patent costs are amortized on a straight-line basis over the lesser of their estimated economic life or remaining patent term. Amortization commences at the time the patent is issued. The Company's patents covering its proprietary HuCAL® technology were granted in Australia in October 2000, in the United States in 2001 and in Europe in June 2002. Further patent applications are pending in Canada and Japan.

Accounting for Acquired License Rights

The Company acquired license rights by making upfront licensing payments, annual maintenance fees and sublicensing payments to third parties. The Company amortizes up-front licensing payments on a straight-line basis over the estimated useful life of the acquired license. Annual maintenance fees are amortized over the term of each annual agreement. Sublicensing payments are amortized on a straight-line basis over the life of the contract or the estimated useful life of the collaboration for those contracts without a stipulated term.

Concentration of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash, cash equivalents, marketable securities and accounts receivable. The Company's cash and cash equivalents are principally denominated in euros and U.S. dollars. Marketable securities are placed in high-quality securities. Cash, cash equivalents and

marketable securities are maintained principally with two high-quality financial institutions in Germany. The Company continually monitors its positions with, and the credit quality of the financial institutions, which are counter parties to its financial instruments, and does not anticipate non-performance. The Company's revenues and accounts receivable are subject to credit risk as a result of customer concentrations. Three customers individually accounted for approximately 38%, 30% and 17% of the Company's March 31, 2003 accounts receivable balance. In addition, three customers individually accounted for 42%, 26% and 16% of the Company's total revenues in the first quarter 2003. On December 31, 2002 two customers accounted for approximately 50% and 46% of the Company's accounts receivable balance and three customers individually accounted for 34%, 28% and 14% of the Company's total revenues in the first quarter 2003.

Accounts Receivable

For accounts receivable, the allowance for doubtful accounts is based on the management's assessment of the collectibility of specific customer accounts and the aging of the accounts receivable. If there is a deterioration of a major customer's credit worthiness or actual defaults are higher than the historical experience, management's estimates of the recoverability of amounts due the Company could be adversely affected. Based on management assessment, no allowance was necessary on March 31, 2003 and December 31, 2002. On March 31, 2003 and on December 31, 2002, accounts receivable included unbilled amounts of approximately EUR 1,947,707 and EUR 265,000 respectively.

Fair Value of Financial Instruments

The carrying value of financial instruments such as cash and cash equivalents, accounts receivable and accounts payable approximate their fair value based upon the short-term maturities of these instruments. The fair value of marketable securities is based upon quoted market prices (see note 3).

Reclassifications

Certain amounts in prior year's consolidated financial statements have been reclassified to conform to the current year's presentation.

Effects of New Accounting Standards and Regulations

For the effects of new accounting standards we refer to our published accounts as of December 31, 2002.

2 Net Loss Per Share

The following table sets forth the computation of basic and diluted net loss per share:

Three Months Ended March 31,	2003 EURO	2002 EURO
Numerator		
Net loss (in thousands EUR)	(1,787)	(3,100)
Denominator		
Denominator for basic and diluted loss per share - weighted average shares	3,889,944	3,889,449
Basic and diluted net loss per share (in EUR)	0.46	0.80

The Company's outstanding stock options were excluded from the above calculations of dilutive net loss per share, as the effect of their inclusion would have been antidilutive.

3 Marketable Securities

Marketable securities consist of the following as of March 31, 2003 and December 31, 2002 (in thousands EUR):

in 000's EUR	Cost	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Market Value
December 31, 2002				
HVB Euro Bond	3,794	0	(526)	3,268
HVB Debentures	2,789	0	(269)	2,520
DB Money Market Funds	12,611	239	0	12,850
	19,194	239	(795)	18,638
Restricted Cash				364
				18,274
March 31, 2003				
HVB Euro Bond	3,794	0	(644)	3,150
HVB Debentures	2,789	0	(381)	2,408
DB Money Market Funds	15,702	226		15,928
	22,285	226	(1,025)	21,486
Restricted Cash				364
				21,122

The net unrealized holding losses of EUR 799,892 for the first three months 2003 and losses of EUR 556,228 for the full year 2002 were recorded as a separate component of stockholders' equity. The unrealized loss is due to a decline in the market value of marketable securities placed with HypoVereinsbank.

Proceeds from sales of securities available-for-sale were EUR 4,952,073 and EUR 2,606,633 for the three months 2003 and 2002, respectively. Gains on the sales of securities available-for-sale for the first three months 2003 amounted to EUR 115,948 and for the same period in 2002, EUR 25,115.

4 Restricted Assets

The Company has classified as restricted cash certain cash, cash equivalents and marketable securities that are not available for use in its operations. At March 31, 2003 the Company had commitments of EUR 364,000 for guarantees issued and EUR 68,200 for convertible bonds issued to employees.

5 Accumulated Other Comprehensive Income (Loss)

Accumulated other comprehensive income (loss) consists of unrealized gains or losses on marketable securities and translation adjustments from consolidation. For the period ended March 31, 2003 and December 31, 2002, the components of accumulated other comprehensive income (loss) were as follows (in thousands EUR):

in 000's EUR	03/31/2003	12/31/2002
Net Unrealized Gain (Loss) on Available-for Sale Securities	(800)	(556)
Foreign Currency Translation Adjustment	45	38
Accumulated Other Comprehensive Income (Loss)	(755)	(518)

6 Intangible Assets

The following sets forth the intangible asset classes as of March 31, 2003 and December 31, 2002 (in thousands EUR):

in 000's EUR	03/31/2003	12/31/2002
Amortized Intangibles		
Patents	8,541	8,531
License Rights	3,809	3,810
Accumulated Amortization Patents	(1,930)	(1,717)
Accumulated Amortization Licenses	(552)	(457)
Unamortized Intangible Assets		
Patents	90	85
Net Intangible Assets	9,958	10,252

The changes in the carrying amount of unamortized patents for the three months ended March 31, 2003 is as follows (in thousands EUR):

in 000's EUR	03/31/2003
Unamortized Intangible Assets	
Balance on December 31, 2002	85
Additions for the first three months 2003	5
Write-off of Capitalized Patent Costs	0
Balance on March 31, 2003	90

Amortization expense on intangible assets totaled EUR 308,407 for the three months period ended March 31, 2003.

7 Property and Equipment

The following sets forth the intangible asset classes as of March 31, 2003 and December 31, 2002 (in thousands EUR):

in 000's EUR	03/31/2003	12/31/2002
Office and laboratory equipment	3,196	3,145
Furniture and fixtures	1,260	1,260
Purchased software	1,106	1,044
Total	5,562	5,449
Less accumulated depreciation	(3,571)	(3,351)
Net property and equipment	1,991	2,098

8 Contingent Liabilities

In July 2001, a lawsuit was filed against the Company by Applied Molecular Evolution, Inc., San Diego, U.S.A. at the United States District Court of Massachusetts in Boston /U.S.A., alleging that the Company infringes the Kauffman-Ballivet patent family. These patents cover the stochastic production of proteins and were granted in the late 1990s. A trial date has not yet been set, although in January 2003, MorphoSys confirmed that it had received a positive "Report and Recommendation" from the Magistrate Judge to the District Judge for the District Court in Boston, Massachusetts, U.S.A., in the legal action filed by Applied Molecular Evolution. The Magistrate Judge recommended that MorphoSys' motion for summary judgment of non-infringement is allowed and that AME's motion for partial summary judgment of infringement be denied. As a result, no provisions for contingent liabilities have been made in the Company's financial statements. In December 2002, the Company and Cambridge Antibody Technology (CAT) entered into a settlement agreement pursuant to which they agreed to settle all patent disputes between the two companies. Pursuant to the settlement agreement, the Company agreed to make annual payments of EUR 1 million over the next five

years as well as issue 588,160 new shares of common stock and make certain ongoing royalty and milestone payments, and in return will receive a license under certain CAT patents with respect to the previous and future development of HuCAL[®] libraries. The Company has the option to buy out its cash obligations to CAT for a predefined fixed amount at any time during the duration of the agreement. The Company has recorded an accrual for the settlement with CAT in the year 2002. In addition, the Company recorded a discount of approximately EUR 1.2 million on the annual payments to record the liability at its estimated fair value. The discount on the cash payments will be amortized to interest expense over the period of the payments. Certain aspects of the agreements with CAT are expected to be finalized in the second half of 2003 at which time the accounting for the agreement with CAT will be finalized.

Management is not aware of any other matters that could give rise to any material liability to the Company that would have a material adverse effect on the Company's financial condition or results of operations.

9 Stockholders' Equity

Common Stock

On March 31, 2003, the common stock of the Company was EUR 11,849,118 and remained unchanged compared to December 31, 2002.

In October 2002, the Company's Management and Supervisory Boards resolved to issue 363,466 shares to XOMA after a capital increase against contribution in kind. As of March 31, 2003, the capital increase was not registered in the commercial register. On December 23, 2002, in connection with the patent litigation settlement with Cambridge Antibody Technology (CAT), MorphoSys agreed to issue an equity stake for a contribution in kind, amounting to 588,160 shares for a license to use various technologies, granted by CAT. On March 31, 2003, the capital increase was not registered.

Authorized and Conditional Share Capital

No stock options or convertible bonds were granted in the first quarter 2003.

No stock options or convertible bonds were exercised in the first quarter 2003.

Additional Paid-In Capital

On March 31, 2003, Additional Paid-in Capital amounted to EUR 59,655,007 (December 31, 2002: EUR 59,193,912). The increased amount over the prior year is due to stock based compensation provisions in the amount of EUR 461,095.

Treasury Stock

Shares totaling EUR 21,934 (59,762 shares) remained unchanged compared to December 31, 2002.

10 Convertible Bonds

With the approval of the Company's shareholder assembly, the Company was authorized, subject to Supervisory Board's and the Management Board's approval, until June 30, 2006 to issue up to 300,000 non-interest bearing convertible bonds with a par/nominal value of EUR 1.00 each (total nominal value EUR 300,000) to employees and members of the Board of Management of the Company and its affiliates. The pre-emptive rights of the shareholders' were excluded.

During the first quarter of 2003 no convertible bonds were issued.

At March 31, 2003, as part of a new grant of convertible bonds, Company employees and the management board subscribed to 70,700 convertible bonds which are intended to be issued in the second quarter of 2003.

11 Directors Dealings

The table below shows the shares, stock options and convertible bonds, and changes of ownership of the same, which were held by the Management and the Supervisory Board during the first quarter of 2003:

Shares	01/01/2003	Additions	Sales	03/31/2003
Management Board				
Dr. Simon Moroney (held through a controlled entity)	113,461	–	–	113,461
Dave Lemus	–	–	–	–
Dr. Thomas von Rüden	–	–	–	–
Total	113,461	–	–	113,461
Management Board				
Dr. Gerald Möller	–	–	–	–
Dr. Daniel Camus	–	–	–	–
Prof. Dr. Jürgen Drews	–	–	–	–
Prof. Dr. Andreas Plückthun	59,300	–	–	59,300
Dr. Jörg Reinhardt	–	–	–	–
Dr. Geoffrey N. Vernon	–	–	–	–
Total	59,300	–	–	59,300

Stock Options

	01/01/2003	Additions	Sales	03/31/2003
Management Board				
Dr. Simon Moroney	25,000	–	–	25,000
Dave Lemus	21,000	–	–	21,000
Dr. Thomas von Rüden	50,700	–	–	50,700
Total	96,700	–	–	96,700
Supervisory Board				
Dr. Gerald Möller	6,100	–	–	6,100
Dr. Daniel Camus	–	–	–	–
Prof. Dr. Jürgen Drews	5,930	–	–	5,930
Prof. Dr. Andreas Plückthun	3,500	–	–	3,500
Dr. Jörg Reinhardt	3,500	–	–	3,500
Dr. Geoffrey N. Vernon	3,500	–	–	3,500
Total	22,530	–	–	22,530

Convertible Bonds

	01/01/2003	Additions	Sales	03/31/2003
Management Board				
Dr. Simon Moroney	12,000	–	–	12,000
Dave Lemus	10,000	–	–	10,000
Dr. Thomas von Rüden	10,000	–	–	10,000
Total	32,000	–	–	32,000
Supervisory Board				
Dr. Gerald Möller	–	–	–	–
Dr. Daniel Camus	–	–	–	–
Prof. Dr. Jürgen Drews	–	–	–	–
Prof. Dr. Andreas Plückthun	–	–	–	–
Dr. Jörg Reinhardt	–	–	–	–
Dr. Geoffrey N. Vernon	–	–	–	–
Total	–	–	–	–

Imprint

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