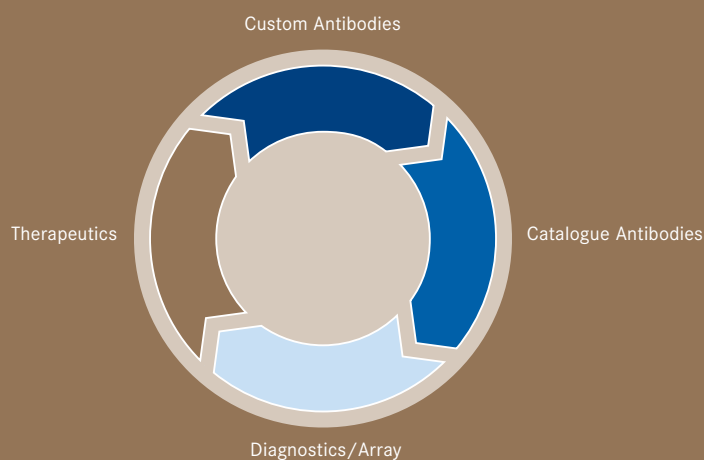


MorphoSys's HuCAL GOLD[®] library is gaining increasing recognition as the most advanced technology for the generation of fully human antibodies. Its considerable advantages over comparable antibody generation systems—speed, flexibility and powerful optimization options—are now widely recognized and accepted. The strengths of this technology, combined with MorphoSys's experience in the field of antibodies, are convincing a growing number of companies interested in this class of drugs to enter partnerships with MorphoSys.

Opportunities for HuCAL[®] in the antibody sector



Market & Strategy

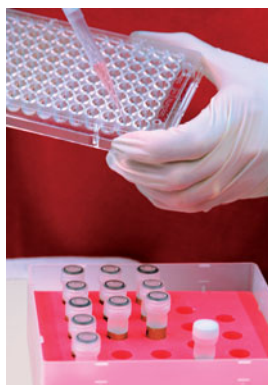
Therapeutic antibodies, once the pursuit of only a handful of smaller biotechnology companies, have become mainstream drugs and are the object of intense research and development activity throughout the pharmaceutical industry. Novartis, Pfizer and many other pharmaceutical companies have recognized the potential of therapeutic antibodies, and are committing large investments to this field. Looking ahead, antibodies may well occupy a dominant position in the product ranges of many pharmaceutical companies. Currently, five of the ten largest pharmaceutical companies use the MorphoSys technology and the expertise of its researchers.

Over the last few years, antibodies have won a secure position as an important element of modern disease therapy. Their natural properties allow a more targeted, specific and thus less invasive treatment of life-threatening diseases. Diagnosis is often a necessary prerequisite to therapy. In this regard, MorphoSys faces a multifaceted market in which antibodies are frequently utilized in tandem with other technologies. In addition to the areas of therapy and diagnostics, antibodies have also traditionally played a key role in biological research. In all fields of application, MorphoSys benefits from considerable market opportunities, whether directly, thanks to the advantages of its proprietary core technology HuCAL[®], or indirectly, via transfer of the Company's expertise in the field of antibodies to new fields of application.

The Company's aim for the future is to continue expanding its already extensive expertise in the antibody sector. The two principal fields of application of HuCAL[®] technology are currently therapeutic applications and the so-called reagent market, i.e. the sale of antibody products as tools for researchers in the life sciences.

The Market for Therapeutic Antibodies

Of the following three fields of application—therapeutics, diagnostics and research reagents—the market for therapeutic products is by far the largest. In 2004, manufacturers of therapeutic antibodies generated estimated annual sales in excess of US\$ 6 billion. Thus, therapeutic antibodies remain the fastest growing segment of the pharmaceutical market. Two new antibodies gained market approval in 2004, thereby increasing the number of therapeutic antibodies currently on the market from 16 to 18. Looking at activities that will give rise to therapeutic antibodies in the mid to long-term future, the year 2004 saw a boost in partnering deals. MorphoSys, as well as other representatives from its peer group, succeeded in striking cash-rich, multi-year partnerships with big pharmaceutical companies. MorphoSys is, and has been, active in this dynamic, rapidly growing market for several years, and is thus strategically well placed to exploit this growth. The unique features of the MorphoSys technology, which enables the creation of tailor-made antibody drugs, are expected to increase the probability of development success. This is a key factor in explaining why the technology is so highly regarded in the pharmaceutical industry.



Use of HuCAL® in research, diagnostics and as therapeutics

Therapeutic antibodies have the potential to improve the therapy of a specific disease significantly. Genentech's antibody Avastin is one of the recently representatives of drugs in this class, and received market approval in February 2004. The antibody, used for treating advanced bowel cancer, prevents a process that is "vital" for tumors: the supply of oxygen- and nutrient-rich fresh blood to the rapidly growing cancer. The tumor achieves this objective by inciting the surrounding blood vessels to grow new veinlets and branches. The growth factor VEGF has been identified as the key molecule in this process of "angiogenesis". Avastin successfully blocks this mechanism and could therefore be effective against many types of cancer. Since obtaining market approval, Genentech has generated US\$ 555 million in revenue from Avastin.

Product	Origin	Indication	Approved
OKT3	Murine	Transplant rejection	1986
ReoPro	Chimeric	Cardiovascular	1994
Rituxan	Chimeric	Cancer	1997
Zenapax	Humanized	Transplant rejection	1997
Simulect	Chimeric	Transplant rejection	1998
Remicade	Chimeric	Inflammation/ Autoimmune diseases	1998
Synagis	Humanized	Virus infection	1998
Herceptin	Humanized	Cancer	1998
Mylotarg	Humanized	Cancer	2000
Campath	Humanized	Cancer	2001
Zevalin	Murine—radiolabeled	Cancer	2002
Humira	Human (PCR library)	Inflammation/ Autoimmune diseases	2002
Bexxar	Murine—radiolabeled	Cancer	2003
Xolair	Humanized	Allergic asthma	2003
Raptiva	Humanized	Inflammation/ Autoimmune diseases	2003
Erbitux	Chimeric	Cancer	2003
Avastin	Humanized	Cancer	2004
Tysabri (Antegren)*	Humanized	Multiple sclerosis	2004

* Suspension of marketing on February 28, 2005

1. HuCAL® Therapeutics Market

MorphoSys's core technology HuCAL® accelerates the development of new antibody drugs to fight a multitude of diseases which are presently inadequately treated. HuCAL GOLD® is the latest and most technologically advanced generation of the Company's proprietary antibody library. In collaboration with biotech and pharmaceutical partners, MorphoSys is developing a comprehensive range of antibody drugs that will provide the basis for significant future growth. In addition to these pure partnership programs, MorphoSys has created further value by developing its own product portfolio. In this regard, MorphoSys is focusing on therapeutic antibodies to treat cancer and inflammatory diseases. This strategy is predicated on MorphoSys's ability to demonstrate the effectiveness of the antibody candidates in animal models, and then out-license these candidates to development partners. Such alliances are intended to exploit the maximum potential financial value of the Company's own projects. Under this scheme, MorphoSys bears all development costs incurred until the product is out-licensed to a partner. However, as a consideration, the Company receives higher fees from prospective partners, in the form of advance payments, milestones and royalties once the commercialization of the product begins.

MorphoSys Business Model—Partnered Therapeutics Business Segment

Within its Therapeutic Antibodies business segment, MorphoSys generates therapeutic antibodies against target molecules provided by its partner companies. The partner is responsible for pre-clinical and clinical drug development, as well as the commercialization of any drugs coming to market. The business model of MorphoSys AG in this segment comprises three distinct chapters.

- Through existing collaborations with pharmaceutical and biotechnology companies such as Bayer, Centocor, Pfizer, Novartis and Schering, MorphoSys generates revenue from payments for access to technology, project-specific license fees, payments for research conducted, and, when research goals are met, success-based milestone fees. This **discovery stage** is break-even or generates a slight profit, and represents the first chapter of the project cycle.
- During the development of each partner project, so-called clinical **milestone payments** are made once the developed products enter the different stages of clinical trials in human patients. Milestones are typically achieved at the beginning of phase 1 studies, marking the entry into human patients, the beginning of phase 3 studies, which investigates the efficacy of the compound and finally the filing of a Biologics License Application, leading to market approval of the drug. At the same time, new projects are constantly being developed, thus creating the basis for further milestones in the future. On the basis of a discovery business which continually expands the pipeline of possible product candidates, this second chapter of company development should be increasingly driven by an inflow of milestone payments which provide a lucrative added value to the first, discovery stage described above.
- The third chapter of the Company's business development is driven by **royalties**. When a product based on the MorphoSys HuCAL[®] technology is sold, MorphoSys receives a percentage of net sales in the form of royalty payments, which is typically in the middle single-digit percentage range. This third and last chapter of the project cycle offers additional growth potential over and beyond both the discovery and milestone-payment stages of the business model. As such, it represents the largest upside value for both investors and the Company in terms of relative payment sizes, as well as sustainability and duration of payment terms.



Dr. Barbara Krebs
Senior Director
Business Development



Dieter Lingelbach
Senior Vice President, Head of
Research Antibody Unit

2. HuCAL® in Research and Diagnostics: MorphoSys Research Antibodies Segment

MorphoSys's business unit "Antibodies by Design", the brand for the MorphoSys Research Antibodies segment, was launched in 2003. The aim of this segment is to further develop the market for non-therapeutic applications. With the recently concluded Human Genome Project, biomedical and pharmaceutical researchers worldwide are turning their attention towards the exploration of proteins. The proliferation of such projects is driving an increasing demand for novel research antibodies to study these newly characterized proteins. To this end, MorphoSys's initiative strives to establish HuCAL® as the industry standard for the manufacture of new types of antibodies in research and diagnostics applications. A key focus of the MorphoSys Research Antibodies segment is the manufacture of custom-made antibodies for research applications. Due to the advantages of the HuCAL® technology, Antibodies by Design is able to supply its clientele with highly specific antibodies within eight weeks—significantly faster than from other technologies. This key advantage has thus far allowed the business unit to acquire customers from 17 different countries including the U.S., the U.K., Germany, Canada, Switzerland and several other markets in both Asia and Europe.

During 2004, the Company continued development of the MorphoSys Research Antibodies segment, by adding new products and expanding into new geographic markets. One target of these efforts to form new sales partners in the reagent market are antibody catalogue suppliers. These companies provide antibodies to their partners through catalogues and are therefore known to a broad client base of researchers as a source of research antibodies. MorphoSys's first contract of this type was concluded in November 2004 with EMD Biosciences, Inc. In this way, MorphoSys recombinant antibodies from the HuCAL® library are made accessible to an extremely broad client base with minimal marketing investment for MorphoSys.

Finally, MorphoSys announced the acquisition of the U.K and U.S.-based Biogenesis Group early 2005, a supplier of antibodies to the life sciences research community. The acquisition provided MorphoSys with immediate access to new market channels for its HuCAL® technology. MorphoSys will continue to support Biogenesis's product portfolio and at the same time utilize all opportunities to further market HuCAL® to Biogenesis's worldwide customer and global distributor network. The acquired Biogenesis companies will be integrated with MorphoSys's existing research antibody business unit, Antibodies by Design. The new unit will run alongside the existing therapeutic antibodies unit, which comprises the largest part of the MorphoSys business.

In 2004, MorphoSys also expanded its business activities in new geographic regions. In order to develop the Japanese market, presently considered the second largest life science market in the world, MorphoSys formed a strategic marketing cooperation with the Tokyo-based GeneFrontier Corporation. With this cooperation, the objective is to establish our HuCAL® technology as a premium brand for both research and therapeutic antibody generation in Japan. The first research projects with Japanese customers have been successfully completed and revenues received.

GeneFrontier: please see also
the Interview on pages 28-31.