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Securities and Exchange Commission
Washington, D.C. 20549

Form 10-K

Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 31, 2003

Commission file number 001-6351

Eli Lilly and Company

An Indiana corporation

I.R.S. employer number 35-0470950

Address: Lilly Corporate Center, Indianapolis, Indiana 46285

Telephone number, including area code: (317) 276-2000

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange On Which Registered
Common Stock	New York and Pacific Stock Exchanges
Preferred Stock Purchase Rights	New York and Pacific Stock Exchanges
8-3/8% Notes Due December 1, 2006	New York Stock Exchange
6.57% Notes Due January 1, 2016	New York Stock Exchange
7-1/8% Notes Due June 1, 2025	New York Stock Exchange
6.77% Notes Due January 1, 2036	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months, and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in the definitive proxy statement incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [X]

Indicate by check mark whether the Registrant is an accelerated filer as defined in Exchange Act Rule 12b-2. Yes ☒ No o

Aggregate market value of voting stock of the Registrant held by non-affiliates as of February 27, 2004 (Common Stock): approximately $71,971,900,000

Number of shares of common stock outstanding as of February 27, 2004: 1,128,884,423

Portions of the following documents have been incorporated by reference into this report:

Registrant's Document	Parts Into Which Incorporated
Annual Report to Shareholders for fiscal year ended December 31, 2003	Parts I, II, and IV
Proxy Statement dated March 12, 2004	Part III

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Part I

Item 1. Business

Eli Lilly and Company (the "Company" or "Registrant", which may be referred to as "we", "us", or "our") was incorporated in 1901 in Indiana to succeed to the drug manufacturing business founded in Indianapolis, Indiana, in 1876 by Colonel Eli Lilly. We discover, develop, manufacture, and sell products in one significant business segment—pharmaceutical products. Operations of our animal health business segment are not material to our financial statements. We manufacture and distribute our products through owned or leased facilities in the United States, Puerto Rico, and 17 other countries. Our products are sold in approximately 140 countries.

Most of the products we sell today were discovered or developed by our own scientists, and our success depends to a great extent on our ability to continue to discover and develop innovative new pharmaceutical products. We direct our research efforts primarily toward the search for products to prevent and treat human diseases. We also conduct research to find products to treat diseases in animals and to increase the efficiency of animal food production.

Products

Our products include:

Neuroscience products, our largest-selling product group, including Zyprexa®, a product for the treatment of schizophrenia, bipolar mania and bipolar maintenance; Prozac®, indicated for the treatment of depression and, in many countries, for bulimia and obsessive-compulsive disorder; Strattera™, for the treatment of attention-deficit hyperactivity disorder in children, adolescents and adults; Permax®, a treatment for Parkinson's disease; Sarafem®, for the treatment of pre-menstrual dysphoric disorder; the Darvon® line of analgesic products; and Symbyax™, approved in late December 2003 for the treatment of bipolar depression.

Endocrine products, including Humulin®, human insulin produced through recombinant DNA technology; Humalog® and Humalog Mix 75/25®, injectable human insulin analogs of recombinant DNA origin; Actos®, an oral agent for Type 2 diabetes that is manufactured and sold by a unit of Takeda Chemical Industries, Ltd. of Japan ("Takeda") and co-promoted by us in the U.S. and certain other countries and sold by us alone in other countries; Evista®, an oral agent for the prevention and treatment of osteoporosis in post-menopausal women; Humatrope®, human growth hormone produced by recombinant DNA technology; and Forteo®, a recombinant form of parathyroid hormone for the treatment of osteoporosis in women and men;

Oncology products, consisting primarily of Gemzar®, indicated for treatment of pancreatic cancer and, in combination with other agents, for treatment of non-small-cell lung cancer; and Alimta®, approved in February 2004 in the U.S. for malignant pleural mesothelioma;

Animal health products, including Tylan®, an antibiotic used to control certain diseases in cattle, swine, and poultry; Rumensin®, a cattle feed additive that improves feed efficiency and growth and also controls and prevents coccidiosis; Coban®, Monteban® and Maxiban®, anticoccidial agents for use in poultry; Apralan®, an antibiotic used to control enteric infections in calves and swine; Micotil® and Pulmotil®, antibiotics used to treat respiratory disease in cattle and swine, respectively; Surmax® (sold as Maxus® in some countries), a performance enhancer for swine

and poultry; Paylean®, a leanness and performance enhancer for swine; and Optaflexx®, a leanness and performance enhancer for cattle;

Cardiovascular agents, including ReoPro®, a monoclonal antibody product developed and manufactured by Centocor, Inc. (a unit of Johnson & Johnson) and co-marketed by Centocor and us for use as an adjunct to percutaneous coronary intervention ("PCI"), including patients undergoing angioplasty, atherectomy or stent placement; Xigris®, a novel biotech agent to treat adults with severe sepsis at high risk of death; Dobutrex®, an agent for cardiac decompensation; and Cynt™, marketed outside the United States for treatment of hypertension;

Anti-infectives, including the oral antibiotics Ceclor®, Keflex®, Keftab®, and Lorabid®, used to treat a wide range of bacterial infections; and Vancocin® HCl, an antibiotic used primarily to treat staphylococcal infections; and

Other pharmaceutical products, including the anti-ulcer agent Axid® and the erectile dysfunction treatment Cialis®, approved in over 55 countries in 2003. Cialis is sold in North America and the European Union by a joint venture between Lilly and ICOS Corporation, and is sold by us in other territories. Cialis was launched in the United States by the Lilly ICOS joint venture in December 2003.

Marketing

We sell most of our products worldwide. We adapt our marketing methods and product emphasis in various countries to meet local needs.

Pharmaceuticals – United States

In the United States, we distribute pharmaceutical products principally through independent wholesale distributors. Our marketing policy is designed to assure that products and relevant medical information are immediately available to physicians, pharmacies, hospitals, and appropriate health care professionals throughout the country. Three wholesale distributors in the United States – AmerisourceBergen Corporation, Cardinal Health, Inc., and McKesson Corporation – each accounted for between 15 and 16 percent of our worldwide consolidated net sales in 2003. No other distributor accounted for more than 10 percent of consolidated net sales. We also sell pharmaceutical products directly to the United States government and other manufacturers, but those sales are not material.

We promote our major pharmaceutical products in the United States through sales representatives who call upon physicians, wholesalers, hospitals, managed-care organizations, retail pharmacists, and other health care professionals. We advertise in medical and drug journals, distribute literature and samples of certain products to physicians, and exhibit at medical meetings. In addition, we advertise certain products directly to consumers in the United States and we maintain web sites with information about all our major products. Divisions of our sales force are dedicated to product lines or practice areas, such as primary care, neuroscience, diabetes care, acute care, endocrinology, and oncology. We have entered into licensing arrangements under which other companies market certain products manufactured by us, such as Darvon, Sarafem, Axid, Keftab, Lorabid, and Permax.

Large purchasers of pharmaceuticals, such as managed-care groups and government and long-term care institutions, account for a significant portion of total pharmaceutical purchases in the United States. We have created special sales groups to service managed-care organizations, government and long-term care institutions, hospital contract administrators, and certain retail pharmacies. In response to competitive

pressures, we have entered into arrangements with a number of these organizations providing for discounts or rebates on one or more Company products or other cost-sharing arrangements.

Pharmaceuticals – Outside the United States

Outside the United States, we promote our pharmaceutical products primarily through sales representatives. While the products marketed vary from country to country, neuroscience products constitute the largest single group in total sales. Distribution patterns vary from country to country. In most countries, we maintain our own sales and distribution organizations. In some countries, however, we market our products through independent distributors.

Animal Health Products

Our Elanco Animal Health business unit employs field salespeople throughout the United States to market animal health products. Elanco also has an extensive sales force outside the United States. Elanco sells its products primarily to wholesale distributors.

Raw Materials and Product Supply

Most of the principal materials we use in our manufacturing operations are available from more than one source. We obtain certain raw materials principally from only one source. In addition, three of our significant products are manufactured by others: Actos by Takeda; ReoPro by Centocor; and Xigris by Lonza Biologics (bulk product) and DSM, N.V. (finished product). If we were unable to obtain certain materials from present sources, we could experience an interruption in supply until we established new sources or, in some cases, implemented alternative processes.

Our primary bulk manufacturing occurs at three sites in Indiana as well as locations in Ireland, Puerto Rico, and the United Kingdom. Finishing operations, including labeling and packaging, take place at a number of sites throughout the world.

We seek to design and operate our manufacturing facilities and maintain inventory in a way that will allow us to meet all expected product demand while maintaining flexibility to reallocate manufacturing capacity to improve efficiency and respond to changes in supply and demand. However, pharmaceutical production processes are complex, highly regulated, and vary widely from product to product. Shifting or adding manufacturing capacity can be a very lengthy process requiring significant capital expenditures. Accordingly, if we were to experience extended plant shutdowns or extraordinary unplanned increases in demand, we could experience an interruption in supply of certain products or product shortages until production could be resumed or expanded.

Patents, Trademarks, and Other Intellectual Property Rights

Overview

Intellectual property protection is, in the aggregate, material to our ability to successfully commercialize our life sciences innovations. We own, have applied for, or are licensed under, a large number of patents, both in the United States and in other countries, relating to products, product uses, formulations, and manufacturing processes. There is no assurance that the patents we are seeking will be granted or that the patents we have been granted would be found valid if challenged. Moreover, patents relating to particular products, uses, formulations, or processes do not preclude other manufacturers from employing

alternative processes or from marketing alternative products or formulations that might successfully compete with our patented products.

Outside the United States, the standard of intellectual property protection for pharmaceuticals varies widely. While many countries have reasonably strong patent laws, other countries currently provide little or no effective protection for inventions or other intellectual property rights. Under the Trade-Related Aspects of Intellectual Property Agreement (TRIPs) administered by the World Trade Organization (WTO), over 140 countries have now agreed to provide non-discriminatory protection for most pharmaceutical inventions and to assure that adequate and effective rights are available to all patent owners. However, in many countries, this agreement will not become fully effective for many years. It is possible that changes to this agreement will be made in the future that will diminish or further delay its implementation in developing countries. It is too soon to assess how much, if at all, we will benefit commercially from these changes.

When a product patent expires, the patent holder often loses effective market exclusivity for the product. This can result in a severe and rapid decline in sales of the formerly patented product, particularly in the United States. However, in some cases the innovator company can obtain additional commercial benefits through manufacturing trade secrets; later-expiring patents on processes, uses, or formulations; trademark use; or marketing exclusivity that may be available under pharmaceutical regulatory laws.

Our Intellectual Property Portfolio

We consider patent protection for certain products, processes, and uses – particularly that relating to Zyprexa, Gemzar, Humalog, Evista, Actos, ReoPro, Xigris, Strattera and Cialis – to be important to our operations. For many of our products, in addition to the compound patent we hold other patents on manufacturing processes, formulations, or uses that may extend exclusivity beyond the expiration of the product patent.

United States compound patent expirations include those claiming the respective active ingredients in Zyprexa, 2011; Humalog, 2013; and ReoPro, 2015. The Gemzar compound patent in the U.S. expires in 2010, but a use patent covering treatment of neoplasms with Gemzar is in force until 2012. We hold a number of U.S. patents covering Evista and its approved uses in osteoporosis prevention and treatment that we believe should provide us exclusivity in the United States until at least 2012. In the United States, the Actos compound patent extends beyond the duration of our co-promotion agreement, which is in force until 2006. Xigris is a complex glycoprotein biologic product that is produced through recombinant DNA technology. Xigris is not subject to the Abbreviated New Drug Application process under the Hatch-Waxman law as described below. In addition, we hold patents on the DNA materials, certain uses, manufacturing process, and the glycoprotein itself. We believe the intellectual property protection for Xigris should provide us marketing exclusivity until 2015. For Strattera, we hold a use patent in the U.S. for treating attention deficit-hyperactivity disorder, the sole approved use of the drug. This use patent expires in 2015 and we have applied for a patent term extension to 2016. For Cialis, compound and method of use patent protection exists into 2016 and we have applied for a patent term extension into 2017.

Worldwide, we sell all of our major products under trademarks that we consider in the aggregate to be important to our operations. Trademark protection varies throughout the world, with protection continuing in some countries as long as the mark is used, and in other countries as long as it is registered. Registrations are normally for fixed but renewable terms.

Patent Challenges Under the Hatch-Waxman Act

The Drug Price Competition and Patent Term Restoration Act of 1984, commonly known as “Hatch-Waxman,” made a complex set of changes to both patent and new-drug-approval laws in the United

States. Before Hatch-Waxman, no drug could be approved without providing the Food and Drug Administration (FDA) complete safety and efficacy studies, *i.e.*, a complete New Drug Application (NDA). Hatch-Waxman authorizes the FDA to approve generic versions of innovative medicines without such information by filing an Abbreviated New Drug Application (ANDA). In an ANDA, the generic manufacturer must demonstrate only "bioequivalence" between the generic version and the NDA-approved drug – not safety and efficacy.

Absent a successful patent challenge, the FDA cannot approve an ANDA until after the innovator's patents expire. However, after the innovator has marketed its product for four years, a generic manufacturer may file an ANDA alleging that one or more of the patents listed in the innovator's NDA are invalid or not infringed. This allegation is commonly known as a "Paragraph IV certification." The innovator must then file suit against the generic manufacturer to protect its patents. If one or more of the NDA-listed patents are successfully challenged, the first filer of a Paragraph IV certification may be entitled to a 180-day period of market exclusivity over all other generic manufacturers.

In recent years, generic manufacturers have used Paragraph IV certifications extensively to challenge patents on a wide array of innovative pharmaceuticals, and we expect this trend to continue. We are currently in litigation with numerous generic manufacturers arising from their Paragraph IV certifications on Zyprexa, Evista, and Sarafem. For more information on the Zyprexa and Evista patent litigation, see Part 1, Item 3, Legal Proceedings.

The FDA has recently finalized regulations clarifying the process by which patents can be listed with the FDA by innovators. In addition, Congress made significant changes to the Hatch-Waxman law as part of the Medicare Prescription Drug, Improvement and Modernization Act of 2003 by allowing only a single 30-month period during which the approval of any individual generic drug application can be delayed while patent issues are resolved. Finally, the so-called "generic exclusivity" provisions that provide incentives for generic companies to challenge drug patents were substantially tightened by Congress. New statutory provisions now mandate sharing the generic exclusivity in certain situations and may require forfeiting the exclusivity altogether, and/or further limit the so-called "exclusivity parking" after a patent challenge has been completed. Collectively, these regulatory and statutory changes are not expected to significantly affect the operation of the Hatch-Waxman law as it relates to our ability to realize patent-based exclusivity for new drugs.

Competition

Our pharmaceutical products compete with products manufactured by many other companies in highly competitive markets throughout the world. Our animal health products compete on a worldwide basis with products of pharmaceutical, chemical, and other companies that operate animal health divisions or subsidiaries.

Important competitive factors include product efficacy, safety, and ease of use, price and demonstrated cost-effectiveness, marketing effectiveness, service, and research and development of new products and processes. If competitors introduce new products, delivery systems or processes with therapeutic or cost advantages, our products can be subject to progressive price reductions or decreased volume of sales, or both. Most new products that we introduce must compete with other products already on the market or products that are later developed by competitors. Manufacturers of generic pharmaceuticals typically invest far less in research and development than research-based pharmaceutical companies and therefore can price their products significantly lower than branded products. Accordingly, when a branded product loses its market exclusivity, it normally faces intense price competition from generic forms of the product. In many countries outside the United States, patent protection is weak or nonexistent and we must compete with generic or "knockoff" versions of our products. To successfully compete for business with managed care and pharmacy benefits management organizations, we must often demonstrate that

our products offer not only medical benefits but also cost advantages as compared with other forms of care.

We believe our long-term competitive position depends upon our success in discovering and developing innovative, cost-effective products that serve unmet medical needs, together with our ability to manufacture the products efficiently and to market them effectively in a highly competitive environment. There can be no assurance that our research and development efforts will result in commercially successful products or that our products or processes will not become outmoded from time to time as a result of products or processes developed by our competitors.

Government Regulation

Our operations are regulated extensively by numerous national, state and local agencies. The lengthy process of laboratory and clinical testing, data analysis, manufacturing development, and regulatory review necessary for required governmental approvals is extremely costly and can significantly delay product introductions in a given market. Promotion, marketing, manufacturing, and distribution of pharmaceutical products are extensively regulated in all major world markets. In addition, our operations are subject to complex federal, state, local, and foreign environmental and occupational safety laws and regulations. The laws and regulations affecting the manufacture and sale of current products and the introduction of new products will continue to require substantial scientific and technical effort, time, and expense and significant capital investment.

Of particular importance is the FDA in the United States. Pursuant to the Federal Food, Drug, and Cosmetic Act, the FDA has jurisdiction over virtually all of our businesses and administers requirements covering the testing, safety, effectiveness, manufacturing, quality control, distribution, labeling, marketing, advertising, dissemination of information and post-marketing surveillance of our pharmaceutical products. The FDA, along with the U.S. Department of Agriculture (USDA) and the U.S. Environmental Protection Agency (EPA), also regulates our animal health products.

Since 1995, the approval of new drugs across the European Union (EU) has been possible using the European Medicines Evaluation Agency's (EMEA) centralized approval process or using the national mutual recognition process. The use of either of these procedures provides a more consistent and, in some cases, a more rapid approval within the EU member states than was the case when each member state operated its own approval process.

In addition, the marketing, promotional and pricing practices of pharmaceutical manufacturers, as well as the manner in which manufacturers interact with purchasers and prescribers, are subject to various other federal and state laws, including the federal anti-kickback statute and the False Claims Act and state laws governing kickbacks and false claims. These laws are administered by, among others, the Department of Justice, the Office of Inspector General of the Department of Health and Human Services, the Federal Trade Commission, the Office of Personnel Management and state attorneys general. Over the past several years, many of those agencies have increased their enforcement activities with respect to pharmaceutical companies. Over this period, several cases brought by these agencies against other companies under these and other laws have resulted in corporate criminal sanctions and very substantial civil settlements. In recent months, several pharmaceutical companies have received subpoenas from one or more of these agencies regarding promotional practices with respect to a variety of products, including neuroscience products. It is possible that we could become subject to administrative and legal proceedings and actions by those governmental agencies. Such actions could include claims for civil penalties (including treble damages under the False Claims Act), criminal sanctions, and administrative remedies, including exclusion from federal health care programs. It is possible that an adverse outcome in such an action could have a material adverse impact on the Company. See Part I, Item 3, "Legal Proceedings," for currently pending matters involving the Company.

In the United States, we are required to provide rebates to state governments on their purchases of certain of our products under state Medicaid programs. In addition, a model waiver program has been created administratively that allows states to expand the Medicaid drug benefit to include low-income Medicare beneficiaries. Other cost containment measures have been adopted or proposed by federal, state, and local government entities that provide or pay for health care. In most international markets, we operate in an environment of government-mandated cost containment programs, which may include price controls, discounts and rebates, restrictions on physician prescription levels, restrictions on reimbursement, compulsory licenses and generic substitution.

In the U.S., we expect branded pharmaceutical products to be subject to increasing pricing pressures. In December 2003, President Bush signed into law the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (MMA), providing a prescription drug benefit under the Medicare program beginning in 2006. This is expected to put downward pressure on prescription drug prices. This pressure may be offset by volume increases, but the business impact of this legislation will not be known until implementation in 2006. While the MMA retains the authority of the Secretary of Health and Human Services to prohibit the importation of prescription drugs, several bills have been introduced that would remove that authority and allow for the immediate importation of products into the U.S. regardless of their safety or cost. Such legislation would likely have a negative effect on our U.S. sales.

As a result of the passage of the MMA, all the aged and many of the disabled Medicaid recipients will receive their benefits through the Medicare program in the future. This should relieve some state budget pressures but is unlikely to result in less pricing pressure. A number of states have begun to implement supplemental rebates and restricted formularies in their Medicaid programs. Several states are also attempting to extend discounted Medicaid prices to non-Medicaid patients. Additionally, over 25 states are considering proposals that would result in the importation of prescription drugs for state employees, state beneficiaries, and in some cases, state citizens. As a result, we expect pressures on pharmaceutical pricing to continue.

International operations are also generally subject to extensive price and market regulations, and there are many proposals for additional cost-containment measures, including proposals that would directly or indirectly impose additional price controls or reduce the value of our intellectual property protection.

We cannot predict the extent to which our business may be affected by these or other potential future legislative or regulatory developments. However, we expect that pressures on pharmaceutical pricing will continue and likely intensify in the near term.

Research and Development

Our commitment to research and development dates back more than 100 years. Our research and development activities are responsible for the discovery and development of most of the products we offer today. We invest heavily in research and development because we believe it is critical to our long-term competitiveness. At the end of 2003, we employed approximately 8,800 people in pharmaceutical and animal health research and development activities, including a substantial number of physicians, scientists holding graduate or postgraduate degrees, and highly skilled technical personnel. Our research and development expenses were $2.24 billion in 2001, $2.15 billion in 2002, and $2.35 billion in 2003.

We concentrate our pharmaceutical research and development efforts in five therapeutic categories: central nervous system and related diseases; endocrine diseases, including diabetes and osteoporosis; cancer; cardiovascular diseases; and inflammation. However, we remain opportunistic, selectively pursuing promising leads in other therapeutic areas. We are actively engaged in biotechnology research programs involving recombinant DNA, proteins, and genomics (the development of therapeutics through

identification of disease-causing genes and their cellular function). In addition to discovering and developing new chemical entities, we look for ways to expand the value of existing products through new uses and formulations that can provide additional benefits to patients. We also conduct research in the animal sciences, including animal nutrition and physiology and veterinary medicine.

To supplement our internal efforts, we collaborate with others, including educational institutions and research-based pharmaceutical and biotechnology companies, and we contract with others for the performance of research in their facilities. We use the services of physicians, hospitals, medical schools, and other research organizations worldwide to conduct clinical trials to establish the safety and effectiveness of new products. We actively seek out investments in external research and technologies that hold the promise to complement and strengthen our own research efforts. These investments can take many forms, including licensing arrangements, co-development and co-marketing agreements, co-promotion arrangements, joint ventures, and acquisitions.

Drug development is time-consuming, expensive, and risky. On average, only one out of many thousands of chemical compounds discovered by researchers proves to be both medically effective and safe enough to become an approved medicine. The process from discovery to regulatory approval typically takes 10 to 15 years or longer. Drug candidates can fail at any stage of the process, and even late-stage product candidates sometimes fail to receive regulatory approval. We believe our investments in research, both internally and in collaboration with others, have been rewarded by the number of new pharmaceutical compounds and indications we have in all stages of development. Among our new investigational compounds in the later stages of development are potential therapies for depression, stress urinary incontinence, diabetes and its complications, osteoporosis, and acute coronary syndrome. Further, we are studying many other drug candidates in the earlier stages of development. We are also developing new uses and formulations for many of our important currently marketed products, such as Zyprexa, Gemzar, Evista, ReoPro, and Alimta.

Quality Assurance

Our success depends in great measure upon customer confidence in the quality of our products and in the integrity of the data that support their safety and effectiveness. Product quality arises from a total commitment to quality in all parts of our operations, including research and development, purchasing, facilities planning, manufacturing, and distribution. We have implemented quality-assurance procedures relating to the quality and integrity of scientific information and production processes.

Control of production processes involves rigid specifications for ingredients, equipment, facilities, manufacturing methods, packaging materials, and labeling. We perform tests at various stages of production processes and on the final product to assure that the product meets all regulatory requirements and our standards. These tests may involve chemical and physical chemical analyses, microbiological testing, testing in animals, or a combination. Additional assurance of quality is provided by a corporate quality-assurance group that monitors existing pharmaceutical and animal health manufacturing procedures and systems in the parent company, subsidiaries and affiliates, and third-party suppliers.

As a result of preapproval plant inspections for Zyprexa IntraMuscular and Forteo in early 2001, the FDA informed us of a number of observations and issued a warning letter regarding adherence to current Good Manufacturing Practices (cGMP) regulations. In response, we have been implementing comprehensive, companywide improvements in our manufacturing operations. In the fall of 2002, we provided the FDA with a comprehensive plan to upgrade our manufacturing and quality operations, particularly at our injectable and dry products facilities in Indianapolis.

In late October 2003, the FDA advised us that the agency now considers our injectable and dry products facilities in Indianapolis to have reached a level of cGMP compliance that will allow preapproval site

inspections for products under review. No further regulatory action is expected at this time. Although the FDA assessment is an important milestone, we still have considerable work to do to reach our ultimate goal of building and sustaining world-class manufacturing, product and process development, and quality capabilities.

Executive Officers of the Company

The following table sets forth certain information regarding our executive officers. All executive officers except Mr. Robert A. Armitage have been employed by the Company in executive positions during the last five years. Prior to joining Lilly in 1999, Mr. Armitage was a partner in the law firm of Vinson & Elkins LLP and headed the firm's intellectual property law practice in Washington, D.C. Previously, he held various positions at The Upjohn Company, where he was vice president, corporate intellectual property law, from 1987 to 1993.

The term of office for each executive officer expires on the date of the annual meeting of the Board of Directors, to be held on April 19, 2004, or on the date his or her successor is chosen and qualified. No director or executive officer of the Company has a "family relationship" with any other director or executive officer of the Company, as that term is defined for purposes of this disclosure requirement. There is no understanding between any executive officer and any other person pursuant to which the executive officer was selected.

Name	Age	Offices
Sidney Taurel	55	Chairman of the Board (since January 1999), President and Chief Executive Officer (since June 1998), and a Director
Charles E. Golden	57	Executive Vice President and Chief Financial Officer (since March 1996) and a Director
John C. Lechleiter, Ph.D.	50	Executive Vice President, Pharmaceutical Operations (since February 2004)
Gerhard N. Mayr	57	Executive Vice President, Pharmaceutical Operations (since October 1999) (retired February 2004)
Steven M. Paul, M.D.	53	Executive Vice President, Science and Technology (since July 2003)
Robert A. Armitage	55	Senior Vice President and General Counsel (since January 2003)
Pedro P. Granadillo	56	Senior Vice President (since June 1998)
Gino Santini	47	President, U.S. Operations (since August 1999)
Lorenzo Tallarigo, M.D.	53	President, International Operations (since January 2004)

Employees

At the end of 2003, we employed approximately 46,100 people, including approximately 21,650 employees outside the United States. A substantial number of our employees have long records of continuous service.

Financial Information Relating to Business Segments and Classes of Products

You can find financial information relating to our business segments and classes of products in our 2003 Annual Report at page 24 under “Segment Information” (page 17 of Exhibit 13 to this Form 10-K). That information is incorporated into this report by reference.

The relative contribution of any particular product to our consolidated net sales changes from year to year. This is due to several factors, including the introduction of new products by us and by other manufacturers and the introduction of generic pharmaceuticals upon patent expirations. In addition, margins vary for our different products due to various factors, including differences in the cost to manufacture and market the products, the value of the products to the marketplace, and government restrictions on pricing and reimbursement.

Financial Information Relating to Foreign and Domestic Operations

You can find financial information relating to foreign and domestic operations in our 2003 Annual Report at page 24 under “Segment Information” (page 17 of Exhibit 13). That information is incorporated in this Report by reference.

To date, our overall operations abroad have not been significantly deterred by local restrictions on the transfer of funds from branches and subsidiaries located abroad, including the availability of dollar exchange. We cannot predict what effect these restrictions or the other risks inherent in foreign operations, including possible nationalization, might have on our future operations or what other restrictions may be imposed in the future. In addition, changing currency values can either favorably or unfavorably affect our financial position and results of operations. We actively manage foreign exchange risk through various hedging techniques including the use of foreign currency contracts.

Available Information on Our Web Site

We make available through our company web site, free of charge, our company filings with the Securities and Exchange Commission (SEC) as soon as reasonably practicable after we electronically file them with, or furnish them to, the SEC. The reports we make available include annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements, registration statements, and any amendments to those documents.

The company web site link to our SEC filings is http://investor.lilly.com/edgar.cfm.

Item 2. Properties

Our principal domestic and international executive offices are located in Indianapolis. At December 31, 2003, we owned 13 production and distribution facilities in the United States and Puerto Rico. Together with the corporate administrative offices, these facilities contain an aggregate of approximately 9.5 million square feet of floor area dedicated to production, distribution, and administration. Major production sites include Indianapolis; Clinton and Lafayette, Indiana; and Carolina and Mayaguez,

Puerto Rico. We also lease sales and administrative offices in Indianapolis and a number of other cities located in the United States and abroad.

We own production and distribution facilities in 13 countries outside the United States and Puerto Rico, containing an aggregate of approximately 4.4 million square feet of floor space. Major production sites include facilities in the United Kingdom, France, Ireland, Spain, Brazil, Italy, and Mexico. We lease production and warehouse facilities in Puerto Rico and several countries outside the United States.

Our research and development facilities in the United States consist of approximately 4.2 million square feet and are located primarily in Indianapolis and Greenfield, Indiana. Our major research and development facilities abroad are located in Belgium, United Kingdom, Germany, Canada, and Spain and contain an aggregate of approximately 650,000 square feet.

We believe that none of our properties is subject to any encumbrance, easement, or other restriction that would detract materially from its value or impair its use in the operation of the business. The buildings we own are of varying ages and in good condition.

Item 3. Legal Proceedings

Zyprexa Patent Litigation

Three generic pharmaceutical manufacturers, Zenith Goldline Pharmaceuticals, Inc. (Zenith), Dr. Reddy's Laboratories, Ltd. (Reddy) and Teva Pharmaceuticals (Teva) have submitted abbreviated new drug applications (ANDAs) seeking permission to market generic versions of Zyprexa in various dosage forms several years prior to the expiration of our U.S. patents for the product, alleging that our patents are invalid or not infringed. In April 2001, we filed suit against Zenith in the U.S. District Court for the Southern District of Indiana seeking a ruling that the challenges to our compound patent (expiring in 2011) are without merit. We filed similar suits in the same court against Reddy in June 2001 and Teva in September 2002. The cases have been consolidated. A trial before a district court judge in Indianapolis was held in January and February of 2004 and the parties are now in the process of submitting post-trial briefs. A ruling from the trial court is expected in the second or third quarter of 2004. Regardless of the trial court's ruling, we anticipate that appeals will follow. If we are unsuccessful at the trial court level, we cannot predict whether any of the generic companies would launch generic versions of Zyprexa prior to a final resolution of any appeals.

We believe that the generic manufacturers' claims are without merit and we expect to prevail in this litigation. However, it is not possible to predict or determine the outcome of this litigation and, accordingly, we can provide no assurance that we will prevail. An unfavorable outcome would have a material adverse impact on our consolidated results of operations, liquidity, and financial position.

Other Patent Litigation

In October 2002, we were notified that Barr Laboratories, Inc. had submitted an ANDA with the U.S. FDA seeking permission to market a generic version of Evista several years prior to the expiration of our U.S. patents covering the product, alleging that the patents are invalid or not infringed. In November 2002, we filed suit against Barr in the U.S. District Court for the Southern District of Indiana seeking a ruling that Barr's challenges to our patents claiming the method of use and pharmaceutical form (expiring from 2012 to 2017) are without merit. In June 2003, Barr added a challenge to one of our additional patents (expiring in 2017) claiming a component in the pharmaceutical form of Evista. That patent has been added to the lawsuit. The suit is in discovery with a trial date currently proposed for August 2005. While we believe that Barr's claims are without merit and expect to prevail, it is not

possible to predict or determine the outcome of the litigation. Therefore, we can provide no assurance that we will prevail. An unfavorable outcome could have a material adverse impact on our consolidated results of operations, liquidity, and financial position.

In October 2002, Pfizer Inc. filed a lawsuit in the United States District Court in Delaware against us, Lilly ICOS LLC, and ICOS Corporation alleging that the proposed marketing of Cialis for erectile dysfunction would infringe its newly issued method-of-use patent. In September 2003, the U.S. Patent and Trademark Office, on its own initiative, ordered that Pfizer's patent be reexamined. The Delaware suit has been stayed pending the outcome of the reexamination. Previously, Pfizer's corresponding European method-of-use patent was held invalid in the first stage of an opposition proceeding in the European Patent Office. Pfizer is now appealing that decision to the Technical Board of Appeal of the European Patent Office. A hearing is expected in the second half of 2004. The U.K. Court of Appeal has previously held the U.K. counterpart to this patent invalid. Litigation relating to the corresponding patent is pending in Australia, Brazil, Canada, Mexico, New Zealand, and South Africa. We intend to vigorously defend this litigation and expect to prevail. However, it is not possible to predict or determine the outcome of this litigation and therefore we can provide no assurance that we will prevail.

Product Liability Litigation

We are currently a defendant in a variety of product liability litigation lawsuits in the United States involving primarily diethylstilbestrol ("DES") and thimerosal.

In approximately 115 U.S. actions, including several with multiple claimants, plaintiffs seek to recover damages on behalf of children or grandchildren of women who were prescribed DES during pregnancy.

We have been named as a defendant in approximately 315 actions in the U.S., involving approximately 820 claimants, brought in various state courts and federal district courts on behalf of children with autism or other neurological disorders who received childhood vaccines (manufactured by other companies) that contained thimerosal, a generic preservative used in certain vaccines in the U.S. from the 1930's until approximately 2000. We discovered and developed thimerosal in the 1920's. We have been named in the suits even though we discontinued manufacturing the raw material in 1974 and discontinued selling it in the United States to vaccine manufacturers in 1992. The lawsuits typically name the vaccine manufacturers as well as Lilly and other distributors of thimerosal, and allege that the children's exposure to thimerosal-containing vaccines caused their autism or other neurological disorders. We strongly deny any liability in these cases. There is no credible scientific evidence establishing a causal relationship between thimerosal-containing vaccines and autism or other neurological disorders. In addition, we believe the cases should not be prosecuted in the courts in which they have been brought because the underlying claims are subject to the National Childhood Vaccine Injury Act of 1986. Implemented in 1988, the Act established a mandatory, federally administered no-fault claims process for individuals who allege that they were harmed by the administration of childhood vaccines. Under the Act, claims must first be brought before the U.S. Court of Claims for an award determination under the compensation guidelines established pursuant to the Act. Claimants who are unsatisfied with their awards under the Act may reject the award and seek traditional judicial remedies.

We have been named in approximately 15 product liability cases in the United States involving plaintiffs claiming a variety of injuries from the administration of Zyprexa. Most of the cases allege that the product caused or contributed to diabetes or high blood glucose levels. We are vigorously defending these suits. Our request that the Zyprexa matters pending in federal courts be consolidated in a Multidistrict Litigation (MDL) before one federal judge for pre-trial purposes will be considered on March 23, 2004.

Other Matters

In July 2002, we received a grand jury subpoena for documents from the Office of Consumer Litigation, Department of Justice, related to our marketing and promotional practices and physician communications with respect to Evista. We received a second subpoena seeking additional documents in July 2003. We continue to cooperate with the government and have provided a broad range of information concerning our U.S. marketing and promotional practices, including documents relating to communications with physicians and the remuneration of physician consultants and advisers. We continue to review and enhance policies and procedures designed to assure that our marketing and promotional practices and physician communications comply with promotional laws and regulations. In recent months, several pharmaceutical companies have received subpoenas from government agencies with respect to a variety of products, including a number of neuroscience products. It is possible that other Lilly products, including Zyprexa, could become subject to investigation. It is possible that the outcome of the above matters could include criminal charges and fines and/or civil penalties. We cannot predict or determine the outcome of the above matters or reasonably estimate the amount or range of amounts of any fines or penalties that might result from an adverse outcome. It is possible, however, that an adverse outcome could have a material adverse impact on our consolidated financial position, liquidity and results of operations.

In August 2003, we received notice that the staff of the SEC is conducting an investigation into the compliance by Polish subsidiaries of certain pharmaceutical companies, including Lilly, with the U.S. Foreign Corrupt Practices Act of 1977. The staff has issued subpoenas requesting production of documents related to the investigation. We are cooperating with the SEC in responding to the investigation.

In March 1996, the U.S. Federal Trade Commission (FTC) commenced a non-public antitrust investigation focusing on the pharmaceutical industry practice of providing discounts or rebates to managed-care organizations and certain other purchasers. We are cooperating with the investigation and have responded to two subpoenas from the FTC requesting production of certain documents and other discovery responses. We have received no additional requests for documents or information for several years. We believe that all of our actions have been lawful and proper.

In March 2001, we received a subpoena, issued at the request of the Commonwealth’s attorney for the Commonwealth of Massachusetts, for production of documents related to pricing and Medicaid reimbursement of our products in Massachusetts. We are not the only pharmaceutical company to receive such a request. We are cooperating with the inquiry and we believe that all of our practices have been lawful and proper.

In 2003, three counties in New York (Suffolk, Rockland, and Westchester) sued Lilly and many other pharmaceutical manufacturers, claiming in general that as a result of alleged improprieties by the manufacturers in the calculation and reporting of average wholesale prices for purposes of Medicaid reimbursement, the counties overpaid their portion of the cost of pharmaceuticals. The suits seek monetary and other relief, including civil penalties and treble damages. The three county suits have been transferred to the U.S. District Court for the District of Massachusetts for pretrial proceedings (along with several other suits to which Lilly is not a party). The Suffolk County case is now the subject of a pending motion to dismiss, and the Rockland and Westchester cases are stayed pending the resolution of that motion. While we are vigorously defending these cases, given their early procedural stage, we cannot predict or determine the outcome of this litigation, and therefore we can provide no assurance that we will prevail.

We are also a defendant in other litigation and investigations, including product liability and patent suits, of a character we regard as normal to our business.

While it is not possible to predict or determine the outcome of the legal actions and investigations described above, we believe that except as otherwise specifically noted above, the resolution of all such matters will not have a material adverse effect on our consolidated financial position or liquidity but could possibly be material to our consolidated results of operations in any one accounting period.

Item 4. Submission of Matters to a Vote of Security Holders

During the fourth quarter of 2003, no matters were submitted to a vote of security holders.

Part II

Item 5. Market For the Company's Common Stock and Related Stockholder Matters

You can find information relating to the principal market for our common stock and related stockholder matters in our 2003 Annual Report under "Selected Quarterly Data (unaudited)," at page 25 (page 18 of Exhibit 13), and "Selected Financial Data (unaudited)," at page 26 (page 19 of Exhibit 13). That information is incorporated in this Report by reference.

Item 6. Selected Financial Data

You can find selected financial data for each of our five most recent fiscal years in our 2003 Annual Report under "Selected Financial Data (unaudited)," at page 26 (page 19 of Exhibit 13). That information is incorporated in this report by reference.

Item 7. Management's Discussion and Analysis of Results of Operations and Financial Condition

You can find management's discussion and analysis of results of operations and financial condition in the following portions of our 2003 Annual Report (found at pages 1-5, 7, and 9-14 of Exhibit 13):

"Review of Operations—Executive Overview" (pages 8-10)
"Review of Operations—Operating Results—2003" (pages 10-12)
"Review of Operations—Operating Results—2002" (pages 12 and 14)
"Review of Operations—Financial Condition" (pages 16-18)
"Review of Operations—Application of Critical Accounting Policies" (pages 18-20)
"Review of Operations—Financial Expectations for 2004" (page 20)
"Review of Operations—Legal and Environmental Matters" (pages 20-21)
"Review of Operations—Private Securities Litigation Reform Act of 1995 – A Caution Concerning Forward-Looking Statements" (page 21)

The information referred to above is incorporated in this report by reference.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

You can find quantitative and qualitative disclosures about market risk (*e.g.*, interest rate risk) in our 2003 Annual Report at "Review of Operations – Financial Condition" on pages 16-17 (pages 9-10 of Exhibit 13). That information is incorporated in this report by reference.

Item 8. Financial Statements and Supplementary Data

You can find the consolidated financial statements of the Company and its subsidiaries in our 2003 Annual Report at the pages indicated in the parentheses. All of this information is incorporated in this report by reference.

- Consolidated Statements of Income—Years Ended December 31, 2003, 2002, and 2001 (page 13) (page 6 of Exhibit 13)
- Consolidated Balance Sheets—December 31, 2003 and 2002 (page 15) (page 8 of Exhibit 13)
- Consolidated Statements of Cash Flows—Years Ended December 31, 2003, 2002, and 2001 (page 22) (page 15 of Exhibit 13)
- Consolidated Statements of Comprehensive Income—Years Ended December 31, 2003, 2002, and 2001 (page 23) (page 16 of Exhibit 13)
- Segment Information (page 24) (page 17 of Exhibit 13)
- Notes to Consolidated Financial Statements (pages 27-42) (pages 20-35 of Exhibit 13).

Also incorporated by reference are the following portions of the 2003 Annual Report:

- Information on quarterly results of operations, which can be found under "Selected Quarterly Data (unaudited)," at page 25 (page 18 of Exhibit 13)
- The Report of Independent Auditors at page 44 (page 37 of Exhibit 13).

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Under applicable SEC regulations, management of a reporting company, with the participation of the principal executive officer and principal financial officer, must periodically evaluate the company's "disclosure controls and procedures," which are defined generally as controls and other procedures of a reporting company designed to ensure that information required to be disclosed by the reporting company in its periodic reports filed with the commission (such as this Form 10-K) is recorded, processed, summarized, and reported on a timely basis.

Our management, with the participation of Sidney Taurel, chairman, president, and chief executive officer, and Charles E. Golden, executive vice president and chief financial officer, evaluated our disclosure controls and procedures as of December 31, 2003, and concluded that they are effective.

Changes in Internal Controls

During the fourth quarter of 2003, there were no changes in our internal control over financial reporting that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Part III

Item 10. Directors and Executive Officers of the Company

Information relating to our Board of Directors is found in our Proxy Statement dated March 12, 2004, under "Board of Directors" at pages 52-55 (pages 8-11 of Schedule 14A filed with the SEC on the EDGAR database), and is incorporated in this report by reference. Information relating to our executive officers is found at Part I, Item 1 of this Form 10-K under "Executive Officers of the Company."

We have adopted a code of ethics that complies with the applicable SEC and New York Stock Exchange requirements. The code is set forth in:

- *The Red Book*, a comprehensive code of ethical and legal business conduct applicable to all employees worldwide and to our Board of Directors; and
- *Code of Ethical Conduct for Lilly Financial Management*, a supplemental code for our chief executive officer and all members of financial management that focuses on accounting, financial reporting, internal controls, and financial stewardship.

Both documents are online on our web site at http://investor.lilly.com/code_business_conduct.cfm. In the event of any amendments to, or waivers from, a provision of the code affecting the chief executive officer, chief financial officer, chief accounting officer, controller, or persons performing similar functions, we intend to post on the above web site within five business days after the event a description of the amendment or waiver as required under applicable SEC rules. We will maintain that information on our web site for at least 12 months.

Item 11. Executive Compensation

You can find information on executive compensation and director compensation in the Proxy Statement under "Directors' Compensation" at page 62 (page 18 of Schedule 14A) and "Executive Compensation" at pages 66-72 (pages 22-28 of Schedule 14A). That information is incorporated in this report by reference, except that the Compensation Committee Report and the Performance Graph are not incorporated in this report.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

You can find information relating to ownership of the Company's common stock by management and by persons known by the Company to be the beneficial owners of more than five percent of the outstanding shares of common stock in the Proxy Statement under "Ownership of Company Stock," at pages 73-74 (pages 29-30 of Schedule 14A). That information is incorporated in this report by reference.

You can find information relating to shares of the Company's common stock authorized for issuance under equity compensation plans in the Proxy Statement under "Equity Compensation Plan Information," at page 77 (page 33 of Schedule 14A). That information is incorporated in this report by reference.

Item 13. Certain Relationships and Related Transactions

None.

Item 14. Principal Accountant Fees and Services

Information related to the fees and services of our independent auditor, Ernst & Young LLP, can be found in the Proxy Statement under "Services Performed by the Independent Auditor" and "Independent Auditor Fees" at pages 64-65 (pages 20-21 of Schedule 14A). That information is incorporated in this report by reference.

Item 15. Exhibits, Financial Statement Schedules, and Reports on Form 8-K

(a)1. Financial Statements

The following consolidated financial statements of the Company and its subsidiaries, included in our 2003 Annual Report at the pages indicated in parentheses, are incorporated by reference in Item 8:

- Consolidated Statements of Income—Years Ended December 31, 2003, 2002, and 2001 (page 13) (page 6 of Exhibit 13)
- Consolidated Balance Sheets—December 31, 2003 and 2002 (page 15) (page 8 of Exhibit 13)
- Consolidated Statements of Cash Flows—Years Ended December 31, 2003, 2002, and 2001 (page 22) (page 15 of Exhibit 13)
- Consolidated Statements of Comprehensive Income—Years Ended December 31, 2003, 2002, and 2001 (page 23) (page 16 of Exhibit 13)
- Segment Information (page 24) (page 17 of Exhibit 13)
- Notes to Consolidated Financial Statements (pages 27-42) (pages 20-35 of Exhibit 13)

(a)2. Financial Statement Schedules

The consolidated financial statement schedules of the Company and its subsidiaries have been omitted because they are not required, are inapplicable, or are adequately explained in the financial statements.

Financial statements of interests of 50 percent or less, which are accounted for by the equity method, have been omitted because they do not, considered in the aggregate as a single subsidiary, constitute a significant subsidiary.

(a)3. Exhibits

3.1	Amended Articles of Incorporation
3.2	By-laws
4.1	Rights Agreement dated as of July 20, 1998, between Eli Lilly and Company and Norwest Bank Minnesota, N.A., as successor Rights Agent
4.2	Amendment No. 1 to Rights Agreement dated as of May 27, 2003, between Eli Lilly and Company and Wells Fargo Bank Minnesota, N.A., as successor Rights Agent
4.3	Form of Indenture with respect to Debt Securities dated as of February 1, 1991, between Eli Lilly and Company and Citibank, N.A., as Trustee
4.4	Form of Standard Multiple-Series Indenture Provisions dated, and filed with the Securities and Exchange Commission on, February 1, 1991
4.5	Form of Fiscal and Paying Agency Agreement dated February 7, 1995, between Eli Lilly and Company and Citibank, N.A., Fiscal and Paying Agent, including forms of Notes, relating to 8-3/8% Notes Due February 7, 2005[1]
4.6	Form of Indenture with respect to Capital Securities dated August 5, 1999 between Lilly del Mar, Inc. and Citibank, N.A., as Trustee[1]
4.7	Form of Resettable Coupon Capital Security due 2029 of Lilly del Mar, Inc.[1]
4.8	Form of Floating Rate Capital Security due 2029 of Lilly del Mar, Inc.[1]
4.9	Form of Fiscal Agency Agreement dated March 22, 2001, between Eli Lilly and Company and Citibank, N.A., Fiscal Agent, relating to Puttable Reset Securities PURSsm due March 22, 2021[1]
4.10	Form of Puttable Reset Securities PURSsm due March 22, 2021[1]
4.11	Form of Fiscal Agency Agreement dated May 30, 2001, between Eli Lilly and Company and Citibank, N.A., Fiscal Agent, relating to Resetable Floating Rate Debt Security due May 15, 2037[1]

[1] This exhibit is not filed with this Report. Copies will be furnished to the Securities and Exchange Commission upon request.

4.12	Form of Resetable Floating Rate Debt Security due May 15, 2037[1]
10.1	1989 Lilly Stock Plan, as amended[2]
10.2	1994 Lilly Stock Plan, as amended[2]
10.3	1998 Lilly Stock Plan, as amended[2]
10.4	2002 Lilly Stock Plan[2]
10.5	Lilly GlobalShares Stock Plan, as amended[2]
10.6	The Lilly Deferred Compensation Plan, as amended[2]
10.7	The Lilly Directors' Deferral Plan, as amended[2]
10.8	The Eli Lilly and Company EVA Bonus Plan, as amended[2,3]
10.9	The Eli Lilly and Company Bonus Plan[2]
10.10	Eli Lilly and Company Change in Control Severance Pay Plan for Select Employees, as amended[2]
10.11	Letter agreement dated September 17, 2001 between the company and Sidney Taurel, Chairman, President, and Chief Executive Officer, concerning Mr. Taurel's request that his base salary for 2002 be reduced to $1.00 [2]
12.	Computation of Ratio of Earnings from Continuing Operations to Fixed Charges
13.	Annual Report to Shareholders for the Year Ended December 31, 2003 (portions incorporated by reference into this Form 10-K)
21.	List of Subsidiaries
23.	Consent of Independent Auditors
31.1	Rule 13a-14(a) Certification of Sidney Taurel, Chairman of the Board, President, and Chief Executive Officer
31.2	Rule 13a-14(a) Certification of Charles E. Golden, Executive Vice President and Chief Financial Officer
32.	Section 1350 Certification
99.	Cautionary Statement under Private Securities Litigation Reform Act of 1995 – "Safe Harbor" for Forward-Looking Disclosures

[2] Indicates management contract or compensatory plan.

[3] Terminated December 31, 2003.

(b) Reports on Form 8-K

During the fourth quarter of 2003, the Company filed one Form 8-K, on October 22, 2003, furnishing information in connection with its public release of financial results for the third quarter of 2003.

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Signatures

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Eli Lilly and Company

By /s/Sidney Taurel

Sidney Taurel, Chairman of the Board,
President and Chief Executive Officer

March 12, 2004

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below on March 12, 2004 by the following persons on behalf of the Registrant and in the capacities indicated.

Signature	Title
/s/ Sidney Taurel SIDNEY TAUREL	Chairman of the Board, President, Chief Executive Officer, and a Director (principal executive officer)
/s/Charles E. Golden CHARLES E. GOLDEN	Executive Vice President, Chief Financial Officer, and a Director (principal financial officer)
/s/Arnold C. Hanish ARNOLD C. HANISH	Chief Accounting Officer (principal accounting officer)
/s/Steven C. Beering STEVEN C. BEERING, M.D.	Director
/s/ Sir Winfried Bischoff SIR WINFRIED BISCHOFF	Director
/s/Martin S. Feldstein MARTIN S. FELDSTEIN, Ph.D.	Director

Signature	Title
/s/George M. C. Fisher	Director
GEORGE M. C. FISHER	
/s/Karen N. Horn	Director
KAREN N. HORN, Ph.D.	
/s/Alfred G. Gilman	Director
ALFRED G. GILMAN, M.D., Ph.D.	
/s/Ellen R. Marram	Director
ELLEN R. MARRAM	
/s/Franklyn G. Prendergast	Director
FRANKLYN G. PRENDERGAST, M.D., Ph.D.	
	Director
SIR JOHN ROSE	
s/Kathi P. Seifert	Director
KATHI P. SEIFERT	

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Trademarks Used In This Report

Trademarks or service marks owned by Eli Lilly and Company or its subsidiaries or affiliates, when first used in this report, appear with an initial capital and are followed by the symbol ® or ™, as applicable. In subsequent uses of the marks in the report, the symbols are omitted.

Table of Contents

Index to Exhibits

The following documents are filed as part of this report:

Exhibit		Location
3.1	Amended Articles of Incorporation	Attached
3.2	By-laws	Incorporated by reference from Exhibit 3 to the Company's Report on Form 10-Q for the quarter ended June 30, 2001
4.1	Rights Agreement dated as of July 20, 1998, between Eli Lilly and Company and Wells Fargo Bank Minnesota, N.A., as successor Rights Agent	Attached
4.2	Amendment No. 1 to Rights Agreement dated as of May 27, 2003, between Eli Lilly and Company and Wells Fargo Bank Minnesota, N.A., as successor Rights Agent	Incorporated by reference from Exhibit 4.2 to the Company's Form 8-A/A, Amendment No. 1, dated May 29, 2003
4.3	Form of Indenture with respect to Debt Securities dated as of February 1, 1991, between Eli Lilly and Company and Citibank, N.A., as Trustee	Incorporated by reference from Exhibit 4.1 to the Company's Registration Statement on Form S-3, Amendment No. 1, Registration No. 333-106478
4.4	Form of Standard Multiple-Series Indenture Provisions dated, and filed with the Securities and Exchange Commission on February 1, 1991	Incorporated by reference from Exhibit 4.2 to the Company's Registration Statement on Form S-3, Amendment No. 1, Registration No. 333-106478
4.5	Form of Fiscal and Paying Agency Agreement dated February 7, 1995, between Eli Lilly and Company and Citibank, N.A., Fiscal and Paying Agent, including forms of Notes, relating to 8-3/8% Notes Due February 7, 2005	*
4.6	Form of Indenture with respect to Capital Securities dated August 5, 1999, between Lilly del Mar, Inc. and Citibank, N.A., as Trustee	*
4.7	Form of Resettable Coupon Capital Security due 2029 of Lilly del Mar, Inc.	*

* Not filed with this report. Copies will be furnished to the Securities and Exchange Commission upon request.

Exhibit		Location
4.8	Form of Floating Rate Capital Security due 2029 of Lilly del Mar, Inc.	*
4.9	Form of Fiscal Agency Agreement dated March 22, 2001, between Eli Lilly and Company and Citibank, N.A., Fiscal Agent, relating to Puttable Reset Securities PURS[sm] due March 22, 2021	*
4.10	Form of Puttable Reset Securities PURS[sm] due March 22, 2021	*
4.11	Form of Fiscal Agency Agreement dated May 30, 2001, between Eli Lilly and Company and Citibank, N.A., Fiscal Agent, relating to Resettable Floating Rate Debt Security due May 15, 2037	*
4.12	Form of Resettable Floating Rate Debt Security due May 15, 2037	*
10.1	1989 Lilly Stock Plan, as amended	Incorporated by reference from Exhibit 10.1 to the Company's report on Form 10-K for the year ended December 31, 2000
10.2	1994 Lilly Stock Plan, as amended	Incorporated by reference from Exhibit 10.1 to the Company's Report on Form 10-Q for the quarter ended September 30, 2001
10.3	1998 Lilly Stock Plan, as amended	Incorporated by reference from Exhibit 10.2 to the Company's Report on Form 10-Q for the quarter ended September 30, 2001
10.4	2002 Lilly Stock Plan	Incorporated by reference from the Appendix to the Company's Proxy Statement dated March 4, 2002
10.5	The Lilly GlobalShares Stock Plan	Incorporated by reference from Exhibit 10.5 to the Company's Report of Form 10-K for the year ended December 31, 2002
10.6	The Lilly Deferred Compensation Plan, as amended	Attached

Exhibit		Location
10.7	The Lilly Directors' Deferral Plan, as amended	Attached
10.8	The Eli Lilly and Company EVA® Bonus Plan, as amended	Incorporated by reference from Exhibit 10.6 to the Company's Report on Form 10-K for the year ended December 31, 2001
10.9	The Eli Lilly and Company Bonus Plan	Incorporated by reference from Appendix B to the Company's Proxy Statement dated March 12, 2004
10.10	Eli Lilly and Company Change in Control Severance Pay Plan for Select Employees, as amended	Incorporated by reference from Exhibit 10.3 to the Company's Report on Form 10-Q for the quarter ended September 30, 2001
10.11	Letter Agreement dated September 17, 2001 between the Company and Sidney Taurel, Chairman, President, and Chief Executive Officer, concerning Mr. Taurel's request that his base salary for 2002 be reduced to $1.00	Incorporated by reference from Exhibit 10.4 to the Company's Report on Form 10-Q for the quarter ended September 30, 2001
12.	Statement regarding Computation of Ratio of Earnings from Continuing Operations to Fixed Charges	Attached
13.	Annual Report to Shareholders for the Year Ended December 31, 2003 (portions incorporated by reference in this Form 10-K)	Attached
21.	List of Subsidiaries	Attached
23.	Consent of Independent Auditors	Attached
31.1	Rule 13a-14(a) Certification of Sidney Taurel, Chairman of the Board, President, and Chief Executive Officer	Attached
31.2	Rule 13a-14(a) Certification of Charles E. Golden, Executive Vice President and Chief Financial Officer	Attached
32	Section 1350 Certification	Attached
99	Cautionary Statement Under Private Securities Litigation Reform Act of 1995 — "Safe Harbor" for Forward-Looking Disclosures	Attached

EXHIBIT 3.1

(As amended and restated through October 20, 1998)

ELI LILLY AND COMPANY
(AN INDIANA CORPORATION)

AMENDED ARTICLES OF INCORPORATION

1. The name of the Corporation shall be

ELI LILLY AND COMPANY.

2. The purposes for which the Corporation is formed are to engage in any lawful act or activity for which a corporation may be organized under the Indiana Business Corporation Law.

3. The period during which the Corporation is to continue as a corporation is perpetual.

4. The total number of shares which the Corporation shall have authority to issue is 3,205,000,000 shares, consisting of 3,200,000,000 shares of Common Stock and 5,000,000 shares of Preferred Stock. The Corporation's shares do not have any par or stated value, except that, solely for the purpose of any statute or regulation imposing any tax or fee based upon the capitalization of the Corporation, each of the Corporation's shares shall be deemed to have a par value of $0.01 per share.

5. The following provisions shall apply to the Corporation's shares:

(a) The Corporation shall have the power to acquire (by purchase, redemption, or otherwise), hold, own, pledge, sell, transfer, assign, reissue, cancel, or otherwise dispose of the shares of the Corporation in the manner and to the extent now or hereafter permitted by the laws of the State of Indiana (but such power shall not imply an obligation on the part of the owner or holder of any share to sell or otherwise transfer such share to the Corporation), including the power to purchase, redeem, or otherwise acquire the Corporation's own shares, directly or indirectly, and without pro rata treatment of the owners or holders of any class or series of shares, unless, after giving effect thereto, the Corporation would not be able to pay its debts as they become due in the usual course of business or the Corporation's total assets would be less than its total liabilities (and without regard to any amounts that would be needed, if the Corporation were to be dissolved at the time of the purchase, redemption, or other acquisition, to satisfy the preferential rights upon dissolution of shareholders whose preferential rights are superior to those of the holders of the shares of the Corporation being purchased, redeemed, or otherwise acquired, unless otherwise expressly provided with respect to a series of Preferred Stock). Shares of the Corporation purchased, redeemed, or otherwise acquired by it

shall constitute authorized but unissued shares, unless prior to any such purchase, redemption, or other acquisition, or within thirty (30) days thereafter, the Board of Directors adopts a resolution providing that such shares constitute authorized and issued but not outstanding shares.

(b) Preferred Stock of any series that has been redeemed (whether through the operation of a retirement or sinking fund or otherwise) or purchased by the Corporation, or which, if convertible, have been converted into shares of the Corporation of any other class or series, may be reissued as a part of such series or of any other series of Preferred Stock, subject to such limitations (if any) as may be fixed by the Board of Directors with respect to such series of Preferred Stock in accordance with the provisions of Article 7 of these Amended Articles of Incorporation.

(c) The Board of Directors of the Corporation may dispose of, issue, and sell shares in accordance with, and in such amounts as may be permitted by, the laws of the State of Indiana and the provisions of these Amended Articles of Incorporation and for such consideration, at such price or prices, at such time or times and upon such terms and conditions (including the privilege of selectively repurchasing the same) as the Board of Directors of the Corporation shall determine, without the authorization or approval by any shareholders of the Corporation. Shares may be disposed of, issued, and sold to such persons, firms, or corporations as the Board of Directors may determine, without any preemptive or other right on the part of the owners or holders of other shares of the Corporation of any class or kind to acquire such shares by reason of their ownership of such other shares.

6. The following provisions shall apply to the Common Stock:

(a) Except as otherwise provided by the Indiana Business Corporation Law and subject to such shareholder disclosure and recognition procedures (which may include voting prohibition sanctions) as the Corporation may by action of its Board of Directors establish, shares of Common Stock shall have unlimited voting rights and each outstanding share of Common Stock shall, when validly issued by the Corporation, entitle the record holder thereof to one vote at all shareholders' meetings on all matters submitted to a vote of the shareholders of the Corporation.

(b) Shares of Common Stock shall be equal in every respect insofar as their relationship to the Corporation is concerned, but such equality of rights shall not imply equality of treatment as to redemption or other acquisition of shares by the Corporation. Subject to the rights of the holders of any outstanding series of Preferred Stock, the holders of Common Stock shall be entitled to share ratably in such dividends or other distributions (other than purchases, redemptions, or other acquisitions of shares by the Corporation), if any, as are declared and paid from time to time on the Common Stock at the discretion of the Board of Directors.

(c) In the event of any liquidation, dissolution, or winding up of the Corporation, either voluntary or involuntary, after payment shall have been made to the holders of any outstanding series of Preferred Stock of the full amount to which they shall be entitled, the holders of Common Stock shall be entitled, to the exclusion of the holders of the Preferred Stock of any and all series, to share, ratably according to the number of shares of Common Stock held by them, in all remaining assets of the Corporation available for distribution to its shareholders.

7. The Board of Directors is hereby expressly authorized to provide, out of the unissued shares of Preferred Stock, for one or more series of Preferred Stock. Before any shares of any such series are issued, the Board of Directors shall fix, and hereby is expressly empowered to fix, by the adoption and filing in accordance with the Indiana Business Corporation Law, of an amendment or amendments to these Amended Articles of Incorporation, the terms of such Preferred Stock or series of Preferred Stock, including the following:

(a) the designation of such series, the number of shares to constitute such series and the stated value thereof if different from the par value thereof;

(b) whether the shares of such series shall have voting rights, in addition to any voting rights provided by law, and, if so, the terms of such voting rights, which may be general or limited and may include the right, under specified circumstances, to elect additional directors;

(c) the dividends, if any, payable on such series, whether any such dividends shall be cumulative, and, if so, from what dates, the conditions and dates upon which such dividends shall be payable, the preference or relation which such dividends shall bear to the dividends payable on any shares of stock of any other class or any other series of Preferred Stock;

(d) whether the shares of such series shall be subject to redemption by the Corporation and, if so, the times, prices and other conditions of such redemption;

(e) the amount or amounts payable upon shares of such series upon, and the rights of the holders of such series in, the voluntary or involuntary liquidation, dissolution or winding up, or upon any distribution of the assets, of the Corporation;

(f) whether the shares of such series shall be subject to the operation of a retirement or sinking fund and, if so, the extent to and manner in which any such retirement or sinking fund shall be applied to the purchase or redemption of the shares of such series for retirement or other corporate purposes and the terms and provisions relative to the operation thereof;

(g) whether the shares of such series shall be convertible into, or exchangeable for, shares of stock of any other class or any other series of Preferred Stock or any other securities (whether or not issued by the

Corporation) and, if so, the price or prices or the rate or rates of conversion or exchange and the method, if any, of adjusting the same, and any other terms and conditions of conversion or exchange;

(h) the limitations and restrictions, if any, to be effective while any shares of such series are outstanding upon the payment of dividends or the making of other distributions on, and upon the purchase, redemption or other acquisition by the Corporation of, the Common Stock or shares of stock of any other class or any other series of Preferred Stock;

(i) the conditions or restrictions, if any, upon the creation of indebtedness of the Corporation or upon the issue of any additional stock, including additional shares of such series or of any other series of Preferred Stock or of any other class of stock; and

(j) any other powers, preferences and relative, participating, optional and other special rights, and any qualifications, limitations and restrictions thereof.

Except to the extent otherwise expressly provided in these Amended Articles of Incorporation or required by law (i) no share of Preferred Stock shall have any voting rights other than those which shall be fixed by the Board of Directors pursuant to this Article 7 and (ii) no share of Common Stock shall have any voting rights with respect to any amendment to the terms of any series of Preferred Stock; provided however, that in the case of this clause (ii) the terms of such series of Preferred Stock, as so amended, could have been established without any vote of any shares of Common Stock.

8. The Corporation shall have the power to declare and pay dividends or other distributions upon the issued and outstanding shares of the Corporation, subject to the limitation that a dividend or other distribution may not be made if, after giving it effect, the Corporation would not be able to pay its debts as they become due in the usual course of business or the Corporation's total assets would be less than its total liabilities (and without regard to any amounts that would be needed, if the Corporation were to be dissolved at the time of the dividend or other distribution, to satisfy the preferential rights upon dissolution of shareholders whose preferential rights are superior to those of the holders of shares receiving the dividend or other distribution, unless otherwise expressly provided with respect to any outstanding series of Preferred Stock). The Corporation shall have the power to issue shares of one class or series as a share dividend or other distribution in respect of that class or series or one or more other classes or series.

9. The following provisions are inserted for the management of the business and for the conduct of the affairs of the Corporation, and it is expressly provided that the same are intended to be in furtherance and not in limitation or exclusion of the powers conferred by statute:

(a) The number of directors of the Corporation, exclusive of directors who may be elected by the holders of any one or more series of Preferred Stock

pursuant to Article 7(b) (the "Preferred Stock Directors"), shall not be less than nine, the exact number to be fixed from time to time solely by resolution of the Board of Directors, acting by not less than a majority of the directors then in office.

(b) The Board of Directors (exclusive of Preferred Stock Directors) shall be divided into three classes, with the term of office of one class expiring each year. At the annual meeting of shareholders in 1985, five directors of the first class shall be elected to hold office for a term expiring at the 1986 annual meeting, five directors of the second class shall be elected to hold office for a term expiring at the 1987 annual meeting, and six directors of the third class shall be elected to hold office for a term expiring at the 1988 annual meeting. Commencing with the annual meeting of shareholders in 1986, each class of directors whose term shall then expire shall be elected to hold office for a three-year term. In the case of any vacancy on the Board of Directors, including a vacancy created by an increase in the number of directors, the vacancy shall be filled by election of the Board of Directors with the director so elected to serve for the remainder of the term of the director being replaced or, in the case of an additional director, for the remainder of the term of the class to which the director has been assigned. All directors shall continue in office until the election and qualification of their respective successors in office. When the number of directors is changed, any newly created directorships or any decrease in directorships shall be so assigned among the classes by a majority of the directors then in office, though less than a quorum, as to make all classes as nearly equal in number as possible. No decrease in the number of directors shall have the effect of shortening the term of any incumbent director. Election of directors need not be by written ballot unless the By-laws so provide.

(c) Any director or directors (exclusive of Preferred Stock Directors) may be removed from office at any time, but only for cause and only by the affirmative vote of at least 80% of the votes entitled to be cast by holders of all the outstanding shares of Voting Stock (as defined in Article 13 hereof), voting together as a single class.

(d) Notwithstanding any other provision of these Amended Articles of Incorporation or of law which might otherwise permit a lesser vote or no vote, but in addition to any affirmative vote of the holders of any particular class of Voting Stock required by law or these Amended Articles of Incorporation, the affirmative vote of at least 80% of the votes entitled to be cast by holders of all the outstanding shares of Voting Stock, voting together as a single class, shall be required to alter, amend or repeal this Article 9.

10. The Board of Directors of the Corporation is exclusively authorized (a) to adopt, repeal, alter or amend the By-laws of the Corporation by the vote of a majority of the entire Board of Directors and (b) to adopt any By-laws which the Board of Directors may deem necessary or desirable for the efficient conduct of the affairs of the Corporation, including, without limitation, provisions governing the conduct of, and the matters which may properly be brought before, meetings of the shareholders and

provisions specifying the manner and extent to which prior notice shall be given of the submission of proposals to be submitted at any meeting of shareholders or of nominations of elections of directors to be held at any such meeting.

11. The Corporation shall, to the fullest extent permitted by applicable law now or hereafter in effect, indemnify any person who is or was a director, officer or employee of the Corporation (an "Eligible Person") and who is or was involved in any manner (including, without limitation, as a party or a witness) or is threatened to be made so involved in any threatened, pending or completed investigation, claim, action, suit or proceeding, whether civil, criminal, administrative or investigative (including, without limitation, any action, suit or proceeding by or in the right of the Corporation to procure a judgment in its favor) (a "Proceeding") by reason of the fact that such person is or was a director, officer or employee of the Corporation or is or was serving at the request of the Corporation as a director, officer, employee, partner, member, manager, trustee, fiduciary or agent of another corporation, partnership, joint venture, limited liability company, trust or other enterprise (including, without limitation, any employee benefit plan), against all expenses (including attorneys' fees), judgments, fines or penalties (including excise taxes assessed with respect to an employee benefit plan) and amounts paid in settlement actually and reasonably incurred by such Eligible Person in connection with such Proceeding; provided, however, that the foregoing shall not apply to a Proceeding commenced by an Eligible Person except to the extent provided otherwise in the Corporation's By-laws or an agreement with an Eligible Person. The Corporation may establish provisions supplemental to or in furtherance of the provisions of this Article 11, including, but not limited to, provisions concerning the determination of any Eligible Person to indemnification, mandatory or permissive advancement of expenses to an Eligible Person incurred in connection with a Proceeding, the effect of any change in control of the Corporation on indemnification and advancement of expenses and the funding or other payment of amounts necessary to effect indemnification and advancement of expenses, in the By-laws of the Corporation or in agreements with any Eligible Person.

12. Except as otherwise expressly provided for in these Amended Articles of Incorporation, the Corporation reserves the right to amend, alter or repeal any provision contained in these Amended Articles of Incorporation, in the manner now or hereafter prescribed by law, and all rights conferred upon shareholders herein are subject to this reservation.

13. In addition to all other requirements imposed by law and these Amended Articles and except as otherwise expressly provided in paragraph (c) of this Article 13, none of the actions or transactions listed below shall be effected by the Corporation, or approved by the Corporation as a shareholder of any majority-owned subsidiary of the Corporation if, as of the record date for the determination of the shareholders entitled to vote thereon, any Related Person (as hereinafter defined) exists, unless the applicable requirements of paragraphs (b), (c), (d), (e), and (f) of this Article 13 are satisfied.

(a) The actions or transactions within the scope of this Article 13 are as follows:

(i) any merger or consolidation of the Corporation or any of its subsidiaries into or with such Related Person;

(ii) any sale, lease, exchange, or other disposition of all or any substantial part of the assets of the Corporation or any of its majority-owned subsidiaries to or with such Related Person;

(iii) the issuance or delivery of any Voting Stock (as hereinafter defined) or of voting securities of any of the Corporation's majority-owned subsidiaries to such Related Person in exchange for cash, other assets or securities, or a combination thereof;

(iv) any voluntary dissolution or liquidation of the Corporation;

(v) any reclassification of securities (including any reverse stock split), or recapitalization of the Corporation, or any merger or consolidation of the Corporation with any of its subsidiaries, or any other transaction (whether or not with or otherwise involving a Related Person) that has the effect, directly or indirectly, of increasing the proportionate share of any class or series of capital stock of the Corporation, or any securities convertible into capital stock of the Corporation or into equity securities of any subsidiary, that is beneficially owned by any Related Person; or

(vi) any agreement, contract, or other arrangement providing for any one or more of the actions specified in the foregoing clauses (i) through (v).

(b) The actions and transactions described in paragraph (a) of this Article 13 shall have been authorized by the affirmative vote of at least 80% of all of the votes entitled to be cast by holders of the outstanding shares of Voting Stock, voting together as a single class.

(c) Notwithstanding paragraph (b) of this Article 13, the 80% voting requirement shall not be applicable if any action or transaction specified in paragraph (a) is approved by the Corporation's Board of Directors and by a majority of the Continuing Directors (as hereinafter defined).

(d) Unless approved by a majority of the Continuing Directors, after becoming a Related Person and prior to consummation of such action or transaction.

(i) the Related Person shall not have acquired from the Corporation or any of its subsidiaries any newly issued or treasury shares of capital stock or any newly issued securities convertible into capital stock of the Corporation or any of its majority-owned subsidiaries, directly or indirectly (except upon conversion of convertible securities acquired by it prior to becoming a Related Person or as a result of a pro rata stock

dividend or stock split or other distribution of stock to all shareholders pro rata);

(ii) such Related Person shall not have received the benefit directly or indirectly (except proportionately as a shareholder) of any loans, advances, guarantees, pledges, or other financial assistance or tax credits provided by the Corporation or any of its majority-owned subsidiaries, or made any major changes in the Corporation's or any of its majority-owned subsidiaries' businesses or capital structures or reduced the current rate of dividends payable on the Corporation's capital stock below the rate in effect immediately prior to the time such Related Person became a Related Person; and

(iii) such Related Person shall have taken all required actions within its power to ensure that the Corporation's Board of Directors included representation by Continuing Directors at least proportionate to the voting power of the shareholdings of Voting Stock of the Corporation's Remaining Public Shareholders (as hereinafter defined), with a Continuing Director to occupy an additional Board position if a fractional right to a director results and, in any event, with at least one Continuing Director to serve on the Board so long as there are any Remaining Public Shareholders.

(e) A proxy statement responsive to the requirements of the Securities Exchange Act of 1934, as amended, whether or not the Corporation is then subject to such requirements, shall be mailed to the shareholders of the Corporation for the purpose of soliciting shareholder approval of such action or transaction and shall contain at the front thereof, in a prominent place, any recommendations as to the advisability or inadvisability of the action or transaction which the Continuing Directors may choose to state and, if deemed advisable by a majority of the Continuing Directors, the opinion of an investment banking firm selected by a majority of the Continuing Directors as to the fairness (or not) of the terms of the action or transaction from a financial point of view to the Remaining Public Shareholders, such investment banking firm to be paid a reasonable fee for its services by the Corporation. The requirements of this paragraph (e) shall not apply to any such action or transaction which is approved by a majority of the Continuing Directors.

(f) For the purpose of this Article 13

(i) the term "Related Person" shall mean any other corporation, person, or entity which beneficially owns or controls, directly or indirectly, 5% or more of the outstanding shares of Voting Stock, and any Affiliate or Associate (as those terms are defined in the General Rules and Regulations under the Securities Exchange Act of 1934) of a Related Person; provided, however, that the term Related Person shall not include (a) the Corporation or any of its subsidiaries, (b) any profit-sharing,

employee stock ownership or other employee benefit plan of the Corporation or any subsidiary of the Corporation or any trustee of or fiduciary with respect to any such plan when acting in such capacity, or (c) Lilly Endowment, Inc.; and further provided, that no corporation, person, or entity shall be deemed to be a Related Person solely by reason of being an Affiliate or Associate of Lilly Endowment, Inc.;

(ii) a Related Person shall be deemed to own or control, directly or indirectly, any outstanding shares of Voting Stock owned by it or any Affiliate or Associate of record or beneficially, including without limitation shares

a. which it has the right to acquire pursuant to any agreement, or upon exercise of conversion rights, warrants, or options, or otherwise or

b. which are beneficially owned, directly or indirectly (including shares deemed owned through application of clause a. above), by any other corporation, person, or other entity with which it or its Affiliate or Associate has any agreement, arrangement, or understanding for the purpose of acquiring, holding, voting, or disposing of Voting Stock, or which is its Affiliate (other than the Corporation) or Associate (other than the Corporation);

(iii) the term "Voting Stock" shall mean all shares of any class of capital stock of the Corporation which are entitled to vote generally in the election of directors;

(iv) the term "Continuing Director" shall mean a director who is not an Affiliate or Associate or representative of a Related Person and who was a member of the Board of Directors of the Corporation immediately prior to the time that any Related Person involved in the proposed action or transaction became a Related Person or a director who is not an Affiliate or Associate or representative of a Related Person and who was nominated by a majority of the remaining Continuing Directors; and

(v) the term "Remaining Public Shareholders" shall mean the holders of the Corporation's capital stock other than the Related Person.

(g) A majority of the Continuing Directors of the Corporation shall have the power and duty to determine for the purposes of this Article 13, on the basis of information then known to the Continuing Directors, whether (i) any Related Person exists or is an Affiliate or an Associate of another and (ii) any proposed sale, lease, exchange, or other disposition of part of the assets of the Corporation or any majority-owned subsidiary involves a substantial part of the assets of the Corporation or any of its subsidiaries. Any such determination by the Continuing Directors shall be conclusive and binding for all purposes.

(h) Nothing contained in this Article 13 shall be construed to relieve any Related Person or any Affiliate or Associate of any Related Person from any fiduciary obligation imposed by law.

(i) The fact that any action or transaction complies with the provisions of this Article 13 shall not be construed to waive or satisfy any other requirement of law or these Amended Articles of Incorporation or to impose any fiduciary duty, obligation, or responsibility on the Board of Directors or any member thereof, to approve such action or transaction or recommend its adoption or approval to the shareholders of the Corporation, nor shall such compliance limit, prohibit, or otherwise restrict in any manner the Board of Directors, or any member thereof, with respect to evaluations of or actions and responses taken with respect to such action or transaction. The Board of Directors of the Corporation, when evaluating any actions or transactions described in paragraph (a) of this Article 13, shall, in connection with the exercise of its judgment in determining what is in the best interests of the Corporation and its shareholders, give due consideration to all relevant factors, including without limitation the social and economic effects on the employees, customers, suppliers, and other constituents of the Corporation and its subsidiaries and on the communities in which the Corporation and its subsidiaries operate or are located.

(j) Notwithstanding any other provision of these Amended Articles of Incorporation or of law which might otherwise permit a lesser vote or no vote, but in addition to any affirmative vote of the holders of any particular class of Voting Stock required by law or these Amended Articles of Incorporation, the affirmative vote of the holders of at least 80% of the votes entitled to be cast by holders of all the outstanding shares of Voting Stock, voting together as a single class, shall be required to alter, amend, or repeal this Article 13.

14. A total of 1,500,000 shares of the 5,000,000 shares of authorized Preferred Stock are designated as "Series B Junior Participating Preferred Stock" (the "Series B Preferred Stock"). Such number of shares may be increased or decreased by resolution of the Board of Directors; provided that no decrease shall reduce the number of shares of Series B Preferred Stock to a number less than the number of shares then outstanding plus the number of shares reserved for issuance upon the exercise of outstanding options, rights or warrants or upon the conversion of any outstanding securities issued by the Corporation convertible into Series B Preferred Stock. The Series B Preferred Stock shall possess the rights, preferences, qualifications, limitations, and restrictions set forth below:

(a) The holders of shares of Series B Preferred Stock shall have the following rights to dividends and distributions:

(i) Subject to the rights of the holders of any shares of any series of Preferred Stock (or any similar stock) ranking prior and superior to the Series B Preferred Stock with respect to dividends, the holders of shares of Series B Preferred Stock, in preference to the holders of Common Stock, without par value (the "Common Stock"), of the

Corporation, and of any other junior stock, shall be entitled to receive, when, as and if declared by the Board of Directors out of funds legally available for the purpose, quarterly dividends payable in cash on the tenth day of March, June, September and December in each year (each such date being referred to herein as a "Quarterly Dividend Payment Date"), commencing on the first Quarterly Dividend Payment Date after the first issuance of a share or fraction of a share of Series B Preferred Stock, in an amount per share (rounded to the nearest cent) equal to the greater of (a) $10 or (b) subject to the provision for adjustment hereinafter set forth, 1,000 times the aggregate per share amount of all cash dividends, and 1,000 times the aggregate per share amount (payable in kind) of all non- cash dividends or other distributions, other than a dividend payable in shares of Common Stock or a subdivision of the outstanding shares of Common Stock (by reclassification or otherwise), declared on the Common Stock since the immediately preceding Quarterly Dividend Payment Date or, with respect to the first Quarterly Dividend Payment Date, since the first issuance of any share or fraction of a share of Series B Preferred Stock. In the event the Corporation shall at any time declare or pay any dividend on the Common Stock payable in shares of Common Stock, or effect a subdivision or combination or consolidation of the outstanding shares of Common Stock (by reclassification or otherwise than by payment of a dividend in shares of Common Stock) into a greater or lesser number of shares of Common Stock, then in each such case the amount to which holders of shares of Series B Preferred Stock were entitled immediately prior to such event under clause (b) of the preceding sentence shall be adjusted by multiplying such amount by a fraction, the numerator of which is the number of shares of Common Stock outstanding immediately after such event and the denominator of which is the number of shares of Common Stock that were outstanding immediately prior to such event.

(ii) The Corporation shall declare a dividend or distribution on the Series B Preferred Stock as provided in paragraph (A) of this Section immediately after it declares a dividend or distribution on the Common Stock (other than a dividend payable in shares of Common Stock); provided that, in the event no dividend or distribution shall have been declared on the Common Stock during the period between any Quarterly Dividend Payment Date and the next subsequent Quarterly Dividend Payment Date, a dividend of $10 per share on the Series B Preferred Stock shall nevertheless be payable on such subsequent Quarterly Dividend Payment Date.

(iii) Dividends shall begin to accrue and be cumulative on outstanding shares of Series B Preferred Stock from the Quarterly Dividend Payment Date next preceding the date of issue of such shares, unless the date of issue of such shares is prior to the record date for the first Quarterly Dividend Payment Date, in which case dividends on such shares shall begin to accrue from the date of issue of such shares, or

unless the date of issue is a Quarterly Dividend Payment Date or is a date after the record date for the determination of holders of shares of Series B Preferred Stock entitled to receive a quarterly dividend and before such Quarterly Dividend Payment Date, in either of which events such dividends shall begin to accrue and be cumulative from such Quarterly Dividend Payment Date. Accrued but unpaid dividends shall not bear interest. Dividends paid on the shares of Series B Preferred Stock in an amount less than the total amount of such dividends at the time accrued and payable on such shares shall be allocated pro rata on a share-by-share basis among all such shares at the time outstanding. The Board of Directors may fix a record date for the determination of holders of shares of Series B Preferred Stock entitled to receive payment of a dividend or distribution declared thereon, which record date shall be not more than 60 days prior to the date fixed for the payment thereof.

(b) The holders of shares of Series B Preferred Stock shall have the following voting rights:

(i) Subject to the provision for adjustment hereinafter set forth, each share of Series B Preferred Stock shall entitle the holder thereof to 1000 votes on all matters submitted to a vote of the stockholders of the Corporation. In the event the Corporation shall at any time declare or pay any dividend on the Common Stock payable in shares of Common Stock, or effect a subdivision or combination or consolidation of the outstanding shares of Common Stock (by reclassification or otherwise than by payment of a dividend in shares of Common Stock) into a greater or lesser number of shares of Common Stock, then in each such case the number of votes per share to which holders of shares of Series B Preferred Stock were entitled immediately prior to such event shall be adjusted by multiplying such number by a fraction, the numerator of which is the number of shares of Common Stock outstanding immediately after such event and the denominator of which is the number of shares of Common Stock that were outstanding immediately prior to such event.

(ii) Except as otherwise provided herein, in any other Articles of Amendment creating a series of Preferred Stock or any similar stock, or by law, the holders of shares of Series B Preferred Stock and the holders of shares of Common Stock and any other capital stock of the Corporation having general voting rights shall vote together as one class on all matters submitted to a vote of stockholders of the Corporation.

(iii) Except as set forth herein, or as otherwise provided by law, holders of Series B Preferred Stock shall have no special voting rights and their consent shall not be required (except to the extent they are entitled to vote with holders of Common Stock as set forth herein) for taking any corporate action.

(c) The Corporation shall be subject to the following restrictions:

(i) Whenever quarterly dividends or other dividends or distributions payable on the Series B Preferred Stock as provided in Section 2 are in arrears, thereafter and until all accrued and unpaid dividends and distributions, whether or not declared, on shares of Series B Preferred Stock outstanding shall have been paid in full, the Corporation shall not:

a. declare or pay dividends, or make any other distributions, on any shares of stock ranking junior (either as to dividends or upon liquidation, dissolution or winding up) to the Series B Preferred Stock;

b. declare or pay dividends, or make any other distributions, on any shares of stock ranking on a parity (either as to dividends or upon liquidation, dissolution or winding up) with the Series B Preferred Stock, except dividends paid ratably on the Series B Preferred Stock and all such parity stock on which dividends are payable or in arrears in proportion to the total amounts to which the holders of all such shares are then entitled;

c. redeem or purchase or otherwise acquire for consideration shares of any stock ranking junior (either as to dividends or upon liquidation, dissolution or winding up) to the Series B Preferred Stock, provided that the Corporation may at any time redeem, purchase or otherwise acquire shares of any such junior stock in exchange for shares of any stock of the Corporation ranking junior (either as to dividends or upon dissolution, liquidation or winding up) to the Series B Preferred Stock; or

d. redeem or purchase or otherwise acquire for consideration any shares of Series B Preferred Stock, or any shares of stock ranking on a parity with the Series B Preferred Stock, except in accordance with a purchase offer made in writing or by publication (as determined by the Board of Directors) to all holders of such shares upon such terms as the Board of Directors, after consideration of the respective annual dividend rates and other relative rights and preferences of the respective series and classes, shall determine in good faith will result in fair and equitable treatment among the respective series or classes.

(ii) The Corporation shall not permit any subsidiary of the Corporation to purchase or otherwise acquire for consideration any shares of stock of the Corporation unless the Corporation could, under paragraph (i) of this Article 14(c), purchase or otherwise acquire such shares at such time and in such manner.

(d) Any shares of Series B Preferred Stock purchased or otherwise acquired by the Corporation in any manner whatsoever shall be retired and canceled promptly after the acquisition thereof. All such shares shall upon their cancellation become authorized but unissued shares of Preferred Stock and may be reissued as part of a new series of Preferred Stock subject to the conditions and restrictions on issuance set forth herein, in the Articles of Incorporation, or in any other Articles of Amendment creating a series of Preferred Stock or any similar stock or as otherwise required by law.

(e) Upon any liquidation, dissolution or winding up of the Corporation, no distribution shall be made (i) to the holders of shares of stock ranking junior (either as to dividends or upon liquidation, dissolution or winding up) to the Series B Preferred Stock unless, prior thereto, the holders of shares of Series B Preferred Stock shall have received the greater of (a) $1000 per share, plus an amount equal to accrued and unpaid dividends and distributions thereon, whether or not declared, to the date of such payment, or (b) an aggregate amount per share, subject to the provision for adjustment hereinafter set forth, equal to 1000 times the aggregate amount to be distributed per share to holders of shares of Common Stock, or (ii) to the holders of shares of stock ranking on a parity (either as to dividends or upon liquidation, dissolution or winding up) with the Series B Preferred Stock, except distributions made ratably on the Series B Preferred Stock and all such parity stock in proportion to the total amounts to which the holders of all such shares are entitled upon such liquidation, dissolution or winding up. In the event the Corporation shall at any time declare or pay any dividend on the Common Stock payable in shares of Common Stock, or effect a subdivision or combination or consolidation of the outstanding shares of Common Stock (by reclassification or otherwise than by payment of a dividend in shares of Common Stock) into a greater or lesser number of shares of Common Stock, then in each such case the aggregate amount to which holders of shares of Series B Preferred Stock were entitled immediately prior to such event under the proviso in clause (i) of the preceding sentence shall be adjusted by multiplying such amount by a fraction the numerator of which is the number of shares of Common Stock outstanding immediately after such event and the denominator of which is the number of shares of Common Stock that were outstanding immediately prior to such event.

(f) In case the Corporation shall enter into any consolidation, merger, combination or other transaction in which the shares of Common Stock are exchanged for or changed into other stock or securities, cash and/or any other property, then in any such case each share of Series B Preferred Stock shall at the same time be similarly exchanged or changed into an amount per share, subject to the provision for adjustment hereinafter set forth, equal to 1000 times the aggregate amount of stock, securities, cash and/or any other property (payable in kind), as the case may be, into which or for which each share of Common Stock is changed or exchanged. In the event the Corporation shall at any time declare or pay any dividend on the Common Stock payable in shares of Common Stock, or effect a subdivision or combination or consolidation of the outstanding shares of Common Stock (by reclassification or otherwise than by

payment of a dividend in shares of Common Stock) into a greater or lesser number of shares of Common Stock, then in each such case the amount set forth in the preceding sentence with respect to the exchange or change of shares of Series B Preferred Stock shall be adjusted by multiplying such amount by a fraction, the numerator of which is the number of shares of Common Stock outstanding immediately after such event and the denominator of which is the number of shares of Common Stock that were outstanding immediately prior to such event.

(g) The shares of Series B Preferred Stock shall not be redeemable.

(h) The Series B Preferred Stock shall rank, with respect to the payment of dividends and the distribution of assets, junior to all series of any other class of the Corporation's Preferred Stock.

(i) The Amended Articles of Incorporation of the Corporation shall not be amended in any manner which would materially alter or change the powers, preferences or special rights of the Series B Preferred Stock so as to affect them adversely without the affirmative vote of the holders of at least two-thirds of the outstanding shares of Series B Preferred Stock, voting together as a single class.

(j) In the event that the Rights Agreement dated as of July 20, 1998 between the Corporation and First Chicago Trust Company of New York, as Rights Agent (or any successor Rights Agent) is terminated or expires prior to the issuance of any shares of Series B Preferred Stock, all shares of Series B Preferred Stock shall become authorized but unissued shares of Preferred Stock and may be reissued as part of a new series of Preferred Stock subject to the conditions and restrictions on issuance set forth in the Articles of Incorporation or in any other Articles of Amendment creating a series of Preferred Stock or any similar stock or as otherwise required by law.

EXHIBIT 4.1

ELI LILLY AND COMPANY

And

FIRST CHICAGO TRUST COMPANY OF NEW YORK

As Rights Agent

Rights Agreement

Dated as of July 20, 1998

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Rights Agreement

Rights Agreement, dated as of July 20, 1998, between Eli Lilly and Company, an Indiana corporation (the "Company"), and First Chicago Trust Company of New York (the "Rights Agent").

The Board of Directors of the Company has authorized and declared a dividend of one preferred share purchase right (a "Right") for each Common Share of the Company outstanding on July 28, 1998 (the "Record Date"), each Right representing the right to purchase one one-thousandth of a Preferred Share, upon the terms and subject to the conditions herein set forth, and has further authorized and directed the issuance of one Right with respect to each Common Share that shall become outstanding between the Record Date and the earliest of the Distribution Date, the Redemption Date and the Expiration Date.

Accordingly, in consideration of the premises and the mutual agreements herein set forth, the parties hereby agree as follows:

Section 1. Certain Definitions. For purposes of this Rights Agreement, the following terms have the meanings indicated:

(a) "Acquiring Person" shall mean any Person who or which, together with all Affiliates and Associates of such Person, shall be the Beneficial Owner of 15% or more of the Common Shares then outstanding, but shall not include (i) the Company, any Subsidiary of the Company, any employee benefit plan of the Company or of any Subsidiary of the Company, or any entity holding Common Shares for or pursuant to the terms of any such plan, (ii) any person who becomes the Beneficial Owner of 15% or more of the Common Shares then outstanding as the result of a reduction in the outstanding Common Shares resulting from acquisition of Common Shares by the Company approved by a majority of the Continuing Directors, unless and until such Person become the Beneficial Owner of any additional Common Shares, (iii) any person who becomes the Beneficial Owner of 15% or more of the Common Shares then outstanding pursuant to any action or transaction or series of related actions or transactions approved by a majority of the Continuing Directors, unless and until such Person become the Beneficial Owner of any additional Common Shares or (iv) Lilly Endowment, Inc. Notwithstanding the foregoing, any Person who or which the Board of Directors of the Company (upon the approval of a majority of the Continuing Directors) determines, in good faith, became an Acquiring Person inadvertently, if such Person divests as promptly as practicable a sufficient number of Common Shares so that such Person would no longer be an Acquiring Person, shall be deemed not to be and never to have been an Acquiring Person.

(b) "Affiliate" and "Associate" shall have the respective meanings ascribed to such terms in Rule 12b-2 under the Exchange Act.

(c) A Person shall be deemed the "Beneficial Owner" of and shall be deemed to "Beneficially Own" any securities:

(i) which such Person or any of such Person's Affiliates or Associates beneficially owns, as determined pursuant to Rule 13d-3 under the Exchange Act;

(ii) which such Person or any of such Person's Affiliates or Associates has (A) the right to acquire (whether such right is exercisable immediately or only after the passage of time) pursuant to any agreement, arrangement or understanding (other than customary agreements with and between underwriters and selling group members with respect to a bona fide public offering of securities), or upon the exercise of conversion rights, exchange rights, rights (other than these Rights), warrants or options, or otherwise, provided, however, that a Person shall not be deemed the Beneficial Owner of, or to Beneficially Own, securities tendered pursuant to a tender or exchange offer made by or on behalf of such Person or any of such Person's Affiliates or Associates until such tendered securities are accepted for purchase or exchange or (B) the right to vote pursuant to any agreement, arrangement or understanding, provided, however, that a Person shall not be deemed the Beneficial Owner of, or to Beneficially Own, any security if the agreement, arrangement or understanding to vote such security (1) arises solely from a revocable proxy or consent given to such Person in response to a public proxy or consent solicitation made pursuant to, and in accordance with, the applicable rules and regulations promulgated under the Exchange Act and (2) is not also then reportable on Schedule 13D under the Exchange Act (or any comparable or successor report) or

(iii) which are beneficially owned, directly or indirectly, by any other Person with which such Person or any of such Person's Affiliates or Associates has any agreement, arrangement or understanding (other than customary agreements with and between underwriters and selling group members with respect to a bona fide public offering of securities) for the purpose of acquiring, holding, voting (except to the extent contemplated by the proviso to Section 1(c)(ii)(B)) or disposing of any securities of the Company.

Notwithstanding anything in this definition of Beneficial Ownership to the contrary, the phrase "then outstanding," when used with reference to a Person's Beneficial Ownership of securities of the Company, shall mean the number of such securities then issued and outstanding together with the number of such securities not then actually issued and outstanding which such Person would be deemed to Beneficially Own hereunder.

(d) "Business Day" shall mean any day other than a Saturday, a Sunday, or a day on which banking institutions in New York are authorized or obligated by law or executive order to close.

(e) "Close of Business" on any given date shall mean 5:00 p.m., New York City time, on such date, provided, however, that, if such date is not a Business Day, it shall mean 5:00 p.m., New York City time, on the next succeeding Business Day.

(f) "Common Shares" shall mean the shares of common stock, without par value, of the Company, except that "Common Shares" when used with reference to any Person other than the Company shall mean the capital stock (or equity interest) with the greatest voting power of such other Person or, if such other Person is a Subsidiary of another Person, the Person or Persons which ultimately control such first-mentioned Person.

(g) "Company" shall have the meaning set forth in the preamble hereof.

(h) "Continuing Director" shall mean any member of the Board of Directors of the Company, while such person is a member of the Board of Directors, who is not an Acquiring Person, or an Affiliate or Associate of an Acquiring Person, or a representative or nominee of an Acquiring Person or of any such Affiliate or Associate, and who either (i) was a member of the Board of Directors on the date of this Agreement or (ii) subsequently became a member of the Board of Directors, and whose nomination for election or election to the Board of Directors was recommended or approved by a majority of the Continuing Directors then on the Board of Directors.

(i) "current per share market price" shall have the meaning set forth in Section 11(d) hereof.

(j) "Distribution Date" shall have the meaning set forth in Section 3(a) hereof.

(k) "equivalent preferred shares" shall have the meaning set forth in Section 11(b) hereof.

(l) "Exchange Act" shall mean the Securities Exchange Act of 1934.

(m) "Exchange Ratio" shall have the meaning set forth in Section 24(a) hereof.

(n) "Expiration Date" shall mean the Close of Business on July 28, 2008.

(o) "NASDAQ" shall mean the National Association of Securities Dealers, Inc. Automated Quotations System.

(p) "Person" shall mean any individual, firm, corporation, partnership or other entity, and shall include any successor (by merger or otherwise) of such entity.

(q) "Preferred Shares" shall mean shares of Series B Junior Participating Preferred Stock, without par value, of the Company having the rights and preferences set forth in the Form of Articles of Amendment attached to this Rights Agreement as Exhibit A.

(r) "Purchase Price" shall initially be $325 for each one one-thousandth of a Preferred Share purchasable pursuant to the exercise of a Right, and shall be subject to adjustment from time to time as provided in Section 11 or 13 hereof.

(s) "Record Date" shall have the meaning set forth in the second paragraph hereof.

(t) "Redemption Date" shall mean the time at which the Rights are redeemed as provided in Section 23 hereof.

(u) "Redemption Price" shall have the meaning set forth in Section 23(a) hereof.

(v) "Right" shall have the meaning set forth in the second paragraph hereof.

(w) "Right Certificate" shall have the meaning set forth in Section 3(a) hereof.

(x) "Rights Agent" shall have the meaning set forth in the preamble hereof.

(y) "Security" shall have the meaning set forth in Section 11(d)(i) hereof.

(z) "Stock Acquisition Date" shall mean the first date of public announcement (including, without limitation, by a filing under the Exchange Act) by the Company or an Acquiring Person that an Acquiring Person has become such or such earlier date as a majority of the Continuing Directors shall become aware of the existence of an Acquiring Person.

(aa) "Subsidiary" of any Person shall mean any corporation or other entity of which a majority of the voting power of the voting equity securities or equity interest is owned or otherwise controlled, directly or indirectly, by such Person.

(bb) "Trading Day" shall have the meaning set forth in Section 11(d)(i) hereof.

Section 2. Appointment of Rights Agent. The Company hereby appoints the Rights Agent to act as agent for the Company and the holders of the Rights (who, in accordance with Section 3 hereof, shall prior to the Distribution Date also be the holders

of the Common Shares) in accordance with the terms and conditions hereof, and the Rights Agent hereby accepts such appointment. The Company may from time to time appoint such co-Rights Agents as it may deem necessary or desirable.

Section 3. Issue of Right Certificates. (a) Until the Close of Business on the day (or such later date as may be determined by action of the Board of Directors, upon approval by a majority of the Continuing Directors) which is the earlier of (i) the tenth day after the Stock Acquisition Date or (ii) such date, if any, as may be determined by action of the Board of Directors of the Company (upon approval by a majority of the Continuing Directors) after the date of the commencement by any Person (other than the Company, any Subsidiary of the Company, any employee benefit plan of the Company or of any Subsidiary of the Company or any entity holding Common Shares for or pursuant to the terms of any such plan) of, or of the first public announcement of the intention of any Person (other than the Company, any Subsidiary of the Company, any employee benefit plan of the Company or of any Subsidiary of the Company or any entity holding Common Shares for or pursuant to the terms of any such plan) to commence, a tender or exchange offer the consummation of which would result in any Person becoming an Acquiring Person (including any such date which is after the date of this Rights Agreement and prior to the issuance of the Rights; the earlier of such dates being herein referred to as the "Distribution Date"), (x) the Rights will be evidenced (subject to the provisions of Section 3(b) hereof) by the certificates for Common Shares registered in the names of the holders thereof (which certificates shall also be deemed to be Right Certificates) and not by separate Right Certificates and (y) the right to receive Right Certificates will be transferable only in connection with the transfer of Common Shares. As soon as practicable after the Distribution Date, the Company will prepare and execute, the Rights Agent will countersign, and the Company will send or cause to be sent (and the Rights Agent will, if requested, send) by first-class, insured, postage-prepaid mail, to each record holder of Common Shares as of the Close of Business on the Distribution Date, at the address of such holder shown on the records of the Company, a Right Certificate, in substantially the form of Exhibit B hereto (a "Right Certificate"), evidencing one Right for each Common Share so held. As of the Distribution Date, the Rights will be evidenced solely by such Right Certificates. References in this Agreement to certificates for common shares shall include certificates for common shares as well as book-entry notations of ownership in the record book of the Company's transfer agent whether or not represented by certificates.

(b) The Company will make available, as promptly as practicable following the Record Date, a Summary of Rights to Purchase Preferred Shares, in substantially the form of Exhibit C hereto, to any holder of Rights who may so request from time to time prior to the Expiration Date. With respect to certificates for Common Shares outstanding as of the Record Date, until the Distribution Date, the Rights will be evidenced by such certificates and the registered holders of the Common Shares shall also be the registered holders of the associated Rights. Until the Distribution Date (or the earlier of the Redemption Date or the Expiration Date), the surrender for transfer of any certificate for Common Shares in respect of which Rights have been issued shall also constitute the transfer of the Rights associated with such Common Shares.

(c) Rights shall be issued in respect of all Common Shares which are issued (whether originally issued or from the Company's treasury) after the Record Date but prior to the earliest of the Distribution Date, the Redemption Date or the Expiration Date. Certificates representing such Common Shares shall bear the following legend:

> THIS CERTIFICATE ALSO EVIDENCES AND ENTITLES THE HOLDER HEREOF TO CERTAIN RIGHTS AS SET FORTH IN A RIGHTS AGREEMENT BETWEEN ELI LILLY AND COMPANY (THE "COMPANY") AND THE RIGHTS AGENT THEREUNDER (THE "RIGHTS AGREEMENT"), THE TERMS OF WHICH ARE HEREBY INCORPORATED HEREIN BY REFERENCE AND A COPY OF WHICH IS ON FILE AT THE PRINCIPAL OFFICES OF THE COMPANY. UNDER CERTAIN CIRCUMSTANCES, AS SET FORTH IN THE RIGHTS AGREEMENT, SUCH RIGHTS WILL BE EVIDENCED BY SEPARATE CERTIFICATES AND WILL NO LONGER BE EVIDENCED BY THIS CERTIFICATE. THE COMPANY WILL MAIL TO THE HOLDER OF THIS CERTIFICATE A COPY OF THE RIGHTS AGREEMENT WITHOUT CHARGE AFTER RECEIPT OF A WRITTEN REQUEST THEREFOR. UNDER CERTAIN CIRCUMSTANCES, AS SET FORTH IN THE RIGHTS AGREEMENT, RIGHTS ISSUED TO ANY PERSON WHO BECOMES AN ACQUIRING PERSON (AS DEFINED IN THE RIGHTS AGREEMENT), INCLUDING SUCH RIGHTS HELD BY A SUBSEQUENT HOLDER, MAY BECOME NULL AND VOID.

With respect to such certificates containing the foregoing legend, until the Distribution Date, the Rights associated with the Common Shares represented by such certificates shall be evidenced by such certificates alone, and the surrender for transfer of any such certificate shall also constitute the transfer of the Rights associated with the Common Shares represented thereby. In the event that the Company purchases or acquires any Common Shares after the Record Date but prior to the Distribution Date, any Rights associated with such Common Shares shall be deemed cancelled and retired so that the Company shall not be entitled to exercise any Rights associated with the Common Shares which are no longer outstanding.

Section 4. Form of Right Certificates. The Right Certificates (and the forms of election to purchase Preferred Shares and of assignment to be printed on the reverse thereof) shall be substantially the same as Exhibit B hereto and may have such marks of identification or designation and such legends, summaries or endorsements printed thereon as the Company may deem appropriate and as are not inconsistent with the provisions of this Rights Agreement, or as may be required to comply with any applicable law or with any rule or regulation made pursuant thereto or with any rule or regulation of any stock exchange or automated quotation system on which the Rights may from time to time be listed, or to conform to usage. Subject to the provisions of Sections 11 and 22 hereof, the Right Certificates shall entitle the holders thereof to purchase such number of one one-thousandths of a Preferred Share as shall be set forth

therein at the price per one one-thousandth of a Preferred Share set forth therein, but the number of one one-thousandths of a Preferred Share and the Purchase Price shall be subject to adjustment as provided herein.

Section 5. Countersignature and Registration. (a) The Right Certificates shall be executed on behalf of the Company by its Chairman of the Board, its Chief Executive Officer, its President, any of its Vice Presidents, or its Treasurer, either manually or by facsimile signature, shall have affixed thereto the Company's seal or a facsimile thereof, and shall be attested by the Secretary or an Assistant Secretary of the Company, either manually or by facsimile signature. The Right Certificates shall be countersigned by the Rights Agent, either manually or by facsimile signature, and shall not be valid for any purpose unless so countersigned. In case any officer of the Company who shall have signed any of the Right Certificates shall cease to be such officer of the Company before countersignature by the Rights Agent and issuance and delivery by the Company, such Right Certificates, nevertheless, may be countersigned by the Rights Agent and issued and delivered by the Company with the same force and effect as though the Person who signed such Right Certificates had not ceased to be such officer of the Company; and any Right Certificate may be signed on behalf of the Company by any Person who, at the actual date of the execution of such Right Certificate, shall be a proper officer of the Company to sign such Right Certificate although at the date of the execution of this Rights Agreement any such Person was not such an officer.

(b) Following the Distribution Date, the Rights Agent will keep or cause to be kept, at its principal office, books for registration and transfer of the Right Certificates issued hereunder. Such books shall show the names and addresses of the respective holders of the Right Certificates, the number of Rights evidenced on its face by each of the Right Certificates and the date of each of the Right Certificates.

Section 6. Transfer, Split Up, Combination and Exchange of Right Certificates; Mutilated, Destroyed, Lost or Stolen Right Certificates.

(a) Subject to the provisions of Section 14 hereof, at any time after the Close of Business on the Distribution Date, and at or prior to the Close of Business on the earlier of the Redemption Date or the Expiration Date, any Right Certificate or Right Certificates (other than Right Certificates representing Rights that have become void pursuant to Section 11(a)(ii) hereof or that have been exchanged pursuant to Section 24 hereof) may be transferred, split up, combined or exchanged for another Right Certificate or Right Certificates entitling the registered holder to purchase a like number of one one-thousandths of a Preferred Share as the Right Certificate or Right Certificates surrendered then entitled such holder to purchase. Any registered holder desiring to transfer, split up, combine or exchange any Right Certificate or Right Certificates shall make such request in writing delivered to the Rights Agent, and shall surrender the Right Certificate or Right Certificates to be transferred, split up, combined or exchanged at the principal office of the Rights Agent. Thereupon the Rights Agent shall countersign and deliver to the Person entitled thereto a Right Certificate or Right Certificates, as the case may be, as

so requested. The Company may require payment of a sum sufficient to cover any tax or governmental charge that may be imposed in connection with any transfer, split up, combination or exchange of Right Certificates.

(b) Upon receipt by the Company and the Rights Agent of evidence reasonably satisfactory to them of the loss, theft, destruction or mutilation of a Right Certificate, and, in case of loss, theft or destruction, of indemnity or security reasonably satisfactory to them, and, at the Company's request, reimbursement to the Company and the Rights Agent of all reasonable expenses incidental thereto, and upon surrender to the Rights Agent and cancellation of the Right Certificate if mutilated, the Company will make and deliver a new Right Certificate of like tenor to the Rights Agent for delivery to the registered holder in lieu of the Right Certificate so lost, stolen, destroyed or mutilated.

Section 7. Exercise of Rights; Purchase Price; Expiration Date of Rights.

(a) The registered holder of any Right Certificate may exercise the Rights evidenced thereby (except as otherwise provided in Sections 11, 23 and 24 hereof), in whole or in part, at any time after the Distribution Date, upon surrender of the Right Certificate, with the form of election to purchase on the reverse side thereof duly executed, to the Rights Agent at the principal office of the Rights Agent, together with payment of the Purchase Price for each one one-thousandth of a Preferred Share as to which the Rights are exercised, at or prior to the earliest of (i) the Expiration Date, (ii) the Redemption Date or (iii) the time at which such Rights are exchanged as provided in Section 24 hereof.

(b) The Purchase Price shall be payable in lawful money of the United States of America in accordance with paragraph (c) below.

(c) Upon receipt of a Right Certificate representing exercisable Rights, with the form of election to purchase duly executed, accompanied by payment of the Purchase Price for the shares to be purchased and an amount equal to any applicable transfer tax required to be paid by the holder of such Right Certificate in accordance with Section 9 hereof by certified check, cashier's check, money order or wire transfer payable to the order of the Company, the Rights Agent shall thereupon promptly (i) (A) requisition from any transfer agent of the Preferred Shares certificates for the number of Preferred Shares to be purchased and the Company hereby irrevocably authorizes any such transfer agent to comply with all such requests, or (B) requisition from the depositary agent depositary receipts representing such number of one one-thousandths of a Preferred Share as are to be purchased (in which case certificates for the Preferred Shares represented by such receipts shall be deposited by the transfer agent of the Preferred Shares with such depositary agent) and the Company hereby directs such depositary agent to comply with such request; (ii) when appropriate, requisition from the Company the amount of cash to be paid in lieu of issuance of fractional shares in accordance with Section 14 hereof; (iii) promptly after receipt of such certificates or depositary receipts, cause the same to be delivered to or upon the order of the registered holder of such Right Certificate, registered in such name or names as may be designated

by such holder; and (iv) when appropriate, after receipt, promptly deliver such cash to or upon the order of the registered holder of such Right Certificate.

(d) In case the registered holder of any Right Certificate shall exercise less than all the Rights evidenced thereby, a new Right Certificate evidencing Rights equivalent to the Rights remaining unexercised shall be issued by the Rights Agent to the registered holder of such Right Certificate or to his duly authorized assigns, subject to the provisions of Section 14 hereof.

Section 8. Cancellation and Destruction of Right Certificates. All Right Certificates surrendered for the purpose of exercise, transfer, split up, combination or exchange shall, if surrendered to the Company or to any of its agents, be delivered to the Rights Agent for cancellation or in cancelled form, or, if surrendered to the Rights Agent, shall be cancelled by it, and no Right Certificates shall be issued in lieu thereof except as expressly permitted by any of the provisions of this Rights Agreement. The Company shall deliver to the Rights Agent for cancellation and retirement, and the Rights Agent shall so cancel and retire, any other Right Certificate purchased or acquired by the Company otherwise than upon the exercise thereof. The Rights Agent shall deliver all cancelled Right Certificates to the Company, or shall, at the written request of the Company, destroy such cancelled Right Certificates, and, in such case, shall deliver a certificate of destruction thereof to the Company.

Section 9. Availability of Preferred Shares.

(a) The Company covenants and agrees that it will cause to be reserved and kept available out of its authorized and unissued Preferred Shares or any Preferred Shares held in its treasury, the number of Preferred Shares that will be sufficient to permit the exercise in full of all outstanding Rights in accordance with Section 7. The Company covenants and agrees that it will take all such action as may be necessary to ensure that all securities delivered upon exercise of Rights shall, at the time of delivery of the certificates for such securities (subject to payment of the Purchase Price), be duly and validly authorized and issued and fully paid and nonassessable.

(b) The Company further covenants and agrees that it will pay when due and payable any and all federal and state transfer taxes and charges which may be payable in respect of the issuance or delivery of the Right Certificates or of any Preferred Shares upon the exercise of Rights. The Company shall not, however, be required to pay any transfer tax which may be payable in respect of any transfer or delivery of Right Certificates to a Person other than, or the issuance or delivery of certificates or depositary receipts for the Preferred Shares in a name other than that of, the registered holder of the Right Certificate evidencing Rights surrendered for exercise or to issue or to deliver any certificates or depositary receipts for Preferred Shares upon the exercise of any Rights until any such tax shall have been paid (any such tax being payable by the holder of such Right Certificate at the time of surrender) or until it has been established to the Company's reasonable satisfaction that no such tax is due.

(c) The Company will use its best efforts to ensure that any securities issued pursuant hereto are issued in compliance with all applicable laws.

Section 10. Preferred Shares Record Date. Each Person in whose name any certificate for Preferred Shares is issued upon the exercise of Rights shall for all purposes be deemed to have become the holder of record of the Preferred Shares represented thereby on, and such certificate shall be dated, the date upon which the Right Certificate evidencing such Rights was duly surrendered and payment of the Purchase Price (and any applicable transfer taxes) was made; provided, however, that if the date of such surrender and payment is a date upon which the Preferred Shares transfer books of the Company are closed, such Person shall be deemed to have become the record holder of such shares on, and such certificate shall be dated, the next succeeding Business Day on which the Preferred Shares transfer books of the Company are open. Prior to the exercise of the Rights evidenced thereby, the holder of a Right Certificate shall not be entitled to any rights of a holder of Preferred Shares for which the Rights shall be exercisable, including, without limitation, the right to vote, to receive dividends or other distributions or to exercise any preemptive rights, and shall not be entitled to receive any notice of any proceedings of the Company, except as provided herein.

Section 11. Adjustment of Purchase Price, Number of Shares or Number of Rights. The Purchase Price, the number of Preferred Shares covered by each Right and the number of Rights outstanding are subject to adjustment from time to time as provided in this Section 11.

(a) (i) In the event the Company shall at any time after the date of this Rights Agreement (A) declare a dividend on the Preferred Shares payable in Preferred Shares, (B) subdivide the outstanding Preferred Shares, (C) combine the outstanding Preferred Shares into a smaller number of Preferred Shares or (D) issue any shares of its capital stock in a reclassification of the Preferred Shares (including any such reclassification in connection with a consolidation or merger in which the Company is the continuing or surviving corporation), except as otherwise provided in this Section 11(a), the Purchase Price in effect at the time of the record date for such dividend or of the effective date of such subdivision, combination or reclassification, and the number and kind of shares of capital stock issuable on such date, shall be proportionately adjusted so that the holder of any Right exercised after such time shall be entitled to receive the aggregate number and kind of shares of capital stock which, if such Right had been exercised immediately prior to such date and at a time when the Preferred Shares transfer books of the Company were open, he would have owned upon such exercise and been entitled to receive by virtue of such dividend, subdivision, combination or reclassification.

(ii) Subject to Section 24 of this Rights Agreement, in the event any Person becomes an Acquiring Person, each holder of a Right shall thereafter have a right to receive, upon exercise thereof at a price equal to the then current Purchase Price multiplied by the number of one one-thousandths of a Preferred Share for which a Right is then exercisable, in accordance with the terms of this Rights Agreement and in

lieu of Preferred Shares, such number of Common Shares as shall equal the result obtained by (A) multiplying the then current Purchase Price by the number of one one-thousandths of a Preferred Share for which a Right is then exercisable and dividing that product by (B) 50% of the then current per share market price of the Company's Common Shares (determined pursuant to Section 11(d) hereof) on the date of the occurrence of such event. In the event that any Person shall become an Acquiring Person and the Rights shall then be outstanding, the Company shall not take any action which would eliminate or diminish the benefits intended to be afforded by the Rights.

Notwithstanding anything in this Agreement to the contrary, from and after the time that any person becomes an Acquiring Person, any Rights that are or were acquired or Beneficially Owned by any Acquiring Person (or any Associate or Affiliate of such Acquiring Person) shall be void and any holder of such Rights shall thereafter have no right to exercise such Rights under any provision of this Rights Agreement. No Right Certificate shall be issued pursuant to Section 3 that represents Rights Beneficially Owned by an Acquiring Person whose Rights would be void pursuant to the preceding sentence or any Associate or Affiliate thereof; no Right Certificate shall be issued at any time upon the transfer of any Rights to an Acquiring Person whose Rights would be void pursuant to the preceding sentence or any Associate or Affiliate thereof or to any nominee of such Acquiring Person, Associate or Affiliate; and any Right Certificate delivered to the Rights Agent for transfer to an Acquiring Person whose Rights would be void pursuant to the preceding sentence shall be cancelled.

(iii) If there shall not be sufficient Common Shares issued but not outstanding or authorized but unissued to permit the exercise in full of the Rights in accordance with the foregoing subparagraph (ii), the Company shall take all such action as may be necessary to authorize additional Common Shares for issuance upon exercise of the Rights. If the Company shall, after good faith effort, be unable to take all such action as may be necessary to authorize such additional Common Shares, the Company shall substitute, for each Common Share that would otherwise be issuable upon exercise of a Right, a number of Preferred Shares or fraction thereof (or a security with substantially similar rights, privileges, preferences, voting power and economic rights) such that the current per share market price of one Preferred Share (or such other security) multiplied by such number or fraction is equal to the current per share market price of one Common Share as of the date of issuance of such Preferred Shares or fraction thereof (or other security).

(b) In case the Company shall fix a record date for the issuance of rights, options or warrants to all holders of Preferred Shares entitling them (for a period expiring within 45 calendar days after such record date) to subscribe for or purchase Preferred Shares (or shares having the same rights, privileges and preferences as the Preferred Shares ("equivalent preferred shares")) or securities convertible into Preferred Shares or equivalent preferred shares at a price per Preferred Share or equivalent preferred share (or having a conversion price per share, if a security convertible into Preferred Shares or equivalent preferred shares) less than the then current per share market price of the Preferred Shares on such record date, the Purchase Price to be in effect after such record

date shall be determined by multiplying the Purchase Price in effect immediately prior to such record date by a fraction, the numerator of which shall be the number of Preferred Shares outstanding on such record date plus the number of Preferred Shares which the aggregate offering price of the total number of Preferred Shares and/or equivalent preferred shares so to be offered (and/or the aggregate initial conversion price of the convertible securities so to be offered) would purchase at such current market price and the denominator of which shall be the number of Preferred Shares outstanding on such record date plus the number of additional Preferred Shares and/or equivalent preferred shares to be offered for subscription or purchase (or into which the convertible securities so to be offered are initially convertible); provided, however, that in no event shall the consideration to be paid upon the exercise of one Right be less than the aggregate par value of the shares of capital stock of the Company issuable upon exercise of one Right. In case such subscription price may be paid in a consideration part or all of which shall be in a form other than cash, the value of such consideration shall be as determined in good faith by the Board of Directors of the Company (upon the approval of a majority of the Continuing Directors), whose determination shall be described in a statement filed with the Rights Agent and shall be binding on the Rights Agent and the holders of the Rights. Preferred Shares owned by or held for the account of the Company shall not be deemed outstanding for the purpose of any such computation. Such adjustment shall be made successively whenever such a record date is fixed; and in the event that such rights, options or warrants are not so issued, the Purchase Price shall be adjusted to be the Purchase Price which would then be in effect if such record date had not been fixed.

(c) In case the Company shall fix a record date for the making of a distribution to all holders of the Preferred Shares (including any such distribution made in connection with a consolidation or merger in which the Company is the continuing or surviving corporation) of evidences of indebtedness or assets (other than a regular quarterly cash dividend or a dividend payable in Preferred Shares) or subscription rights or warrants (excluding those referred to in Section 11(b) hereof), the Purchase Price to be in effect after such record date shall be determined by multiplying the Purchase Price in effect immediately prior to such record date by a fraction, the numerator of which shall be the then current per share market price of the Preferred Shares on such record date, less the fair market value (as determined in good faith by the Board of Directors of the Company (upon the approval of a majority of the Continuing Directors), whose determination shall be described in a statement filed with the Rights Agent and shall be binding on the Rights Agent and holders of the Rights) of the portion of the assets or evidences of indebtedness so to be distributed or of such subscription rights or warrants applicable to one Preferred Share and the denominator of which shall be such current per share market price of the Preferred Shares; provided, however, that in no event shall the consideration to be paid upon the exercise of one Right be less than the aggregate par value of the shares of capital stock of the Company to be issued upon exercise of one Right. Such adjustments shall be made successively whenever such a record date is fixed; and in the event that such distribution is not so made, the Purchase Price shall again be adjusted to be the Purchase Price which would then be in effect if such record date had not been fixed.

(d) (i) For the purpose of any computation hereunder, the "current per share market price" of any security (a "Security" for the purpose of this Section 11(d)(i)) on any date shall be deemed to be the average of the daily closing prices per share of such Security for the 30 consecutive Trading Days immediately prior to such date; provided, however, that in the event that the current per share market price of the Security is determined during a period following the announcement by the issuer of such Security of (A) a dividend or distribution on such Security payable in shares of such Security or securities convertible into such shares, or (B) any subdivision, combination or reclassification of such Security and prior to the expiration of 30 Trading Days after the ex-dividend date for such dividend or distribution, or the record date for such subdivision, combination or reclassification, then, and in each such case, the current per share market price shall be appropriately adjusted to reflect the current market price per share equivalent of such Security. The closing price for each day shall be the last sale price, regular way, or, in case no such sale takes place on such day, the average of the closing bid and asked prices, regular way, in either case, as reported in the principal consolidated transaction reporting system with respect to securities listed or admitted to trading on the New York Stock Exchange or, if the Security is not listed or admitted to trading on the New York Stock Exchange, as reported in the principal consolidated transaction reporting system with respect to securities listed on the principal national securities exchange on which the Security is listed or admitted to trading or, if the Security is not listed or admitted to trading on any national securities exchange, the last quoted price or, if not so quoted, the average of the high bid and low asked prices in the over-the-counter market, as reported by the NASDAQ or such other system then in use, or, if on any such date the Security is not quoted by any such organization, the average of the closing bid and asked prices as furnished by a professional market maker making a market in the Security selected by the Board of Directors of the Company (upon the approval of a majority of the Continuing Directors). The term "Trading Day" shall mean a day on which the principal national securities exchange on which the Security is listed or admitted to trading is open for the transaction of business or, if the Security is not listed or admitted to trading on any national securities exchange, a Business Day.

(ii) For the purpose of any computation hereunder, the "current per share market price" of the Preferred Shares shall be determined in accordance with the method set forth in Section 11(d)(i). If the Preferred Shares are not publicly traded, the "current per share market price" of the Preferred Shares shall be conclusively deemed to be the current per share market price of the Common Shares as determined pursuant to Section 11(d)(i) (appropriately adjusted to reflect any stock split, stock dividend or similar transaction occurring after the date hereof), multiplied by one thousand. If neither the Common Shares nor the Preferred Shares are publicly held or so listed or traded, "current per share market price" shall mean the fair value per share as determined in good faith by the Board of Directors of the Company (upon the approval of a majority of the Continuing Directors), whose determination shall be described in a statement filed with the Rights Agent.

(e) No adjustment in the Purchase Price shall be required unless such adjustment would require an increase or decrease of at least 1% in the Purchase Price;

provided, however, that any adjustments which by reason of this Section 11(e) are not required to be made shall be carried forward and taken into account in any subsequent adjustment. All calculations under this Section 11 shall be made to the nearest cent or to the nearest one-millionth of a Preferred Share or one ten-thousandth of any other share or security as the case may be. Notwithstanding the first sentence of this Section 11(e), any adjustment required by this Section 11 shall be made no later than the earlier of (i) three years from the date of the transaction which requires such adjustment or (ii) the date of the expiration of the right to exercise any Rights.

(f) If, as a result of an adjustment made pursuant to Section 11(a) hereof, the holder of any Right thereafter exercised shall become entitled to receive any shares of capital stock of the Company other than Preferred Shares, thereafter the number of such other shares so receivable upon exercise of any Right shall be subject to adjustment from time to time in a manner and on terms as nearly equivalent as practicable to the provisions with respect to the Preferred Shares contained in Section 11(a) through (c), inclusive, and the provisions of Sections 7, 9, 10 and 13 with respect to the Preferred Shares shall apply on like terms to any such other shares.

(g) All Rights originally issued by the Company subsequent to any adjustment made to the Purchase Price hereunder shall evidence the right to purchase, at the adjusted Purchase Price, the number of one one-thousandths of a Preferred Share purchasable from time to time hereunder upon exercise of the Rights, all subject to further adjustment as provided herein.

(h) Unless the Company shall have exercised its election as provided in Section 11(i), upon each adjustment of the Purchase Price as a result of the calculations made in Sections 11(b) and (c), each Right outstanding immediately prior to the making of such adjustment shall thereafter evidence the right to purchase, at the adjusted Purchase Price, that number of one one-thousandths of a Preferred Share (calculated to the nearest one millionth of a Preferred Share) obtained by (A) multiplying (x) the number of one one-thousandths of a share covered by a Right immediately prior to this adjustment by (y) the Purchase Price in effect immediately prior to such adjustment of the Purchase Price and (B) dividing the product so obtained by the Purchase Price in effect immediately after such adjustment of the Purchase Price.

(i) The Company may elect on or after the date of any adjustment of the Purchase Price to adjust the number of Rights in substitution for any adjustment in the number of one one-thousandths of a Preferred Share purchasable upon the exercise of a Right. Each of the Rights outstanding after such adjustment of the number of Rights shall be exercisable for the number of one one-thousandths of a Preferred Share for which a Right was exercisable immediately prior to such adjustment. Each Right held of record prior to such adjustment of the number of Rights shall become that number of Rights (calculated to the nearest one millionth) obtained by dividing the Purchase Price in effect immediately prior to adjustment of the Purchase Price by the Purchase Price in effect immediately after adjustment of the Purchase Price. The Company shall make a public announcement of its election to adjust the number of Rights, indicating the record date

for the adjustment, and, if known at the time, the amount of the adjustment to be made. This record date may be the date on which the Purchase Price is adjusted or any day thereafter, but, if the Right Certificates have been issued, shall be at least 10 days later than the date of the public announcement. If Right Certificates have been issued, upon each adjustment of the number of Rights pursuant to this Section 11(i), the Company shall, as promptly as practicable, cause to be distributed to holders of record of Right Certificates on such record date Right Certificates evidencing, subject to Section 14 hereof, the additional Rights to which such holders shall be entitled as a result of such adjustment, or, at the option of the Company, shall cause to be distributed to such holders of record in substitution and replacement for the Right Certificates held by such holders prior to the date of adjustment, and upon surrender thereof, if required by the Company, new Right Certificates evidencing all the Rights to which such holders shall be entitled after such adjustment. Right Certificates so to be distributed shall be issued, executed and countersigned in the manner provided for herein and shall be registered in the names of the holders of record of Right Certificates on the record date specified in the public announcement.

(j) Irrespective of any adjustment or change in the Purchase Price or the number of one one-thousandths of a Preferred Share issuable upon the exercise of the Rights, the Right Certificates theretofore and thereafter issued may continue to express the Purchase Price and the number of one one-thousandths of a Preferred Share which were expressed in the initial Right Certificates issued hereunder.

(k) Before taking any action that would cause an adjustment reducing the Purchase Price of the Preferred Shares issuable upon exercise of the Rights, the Company shall take any corporate action which may, in the opinion of its counsel, be necessary in order that the Company may validly and legally issue fully paid and nonassessable Preferred Shares at such adjusted Purchase Price.

(l) In any case in which this Section 11 shall require that an adjustment in the Purchase Price be made effective as of a record date for a specified event, the Company may elect to defer until the occurrence of such event the issuing to the holder of any Right exercised after such record date of the Preferred Shares and other capital stock or securities of the Company, if any, issuable upon such exercise over and above the Preferred Shares and other capital stock or securities of the Company, if any, issuable upon such exercise on the basis of the Purchase Price in effect prior to such adjustment; provided, however, that the Company shall deliver to such holder a due bill or other appropriate instrument evidencing such holder's right to receive such additional shares upon the occurrence of the event requiring such adjustment.

(m) Anything in this Section 11 to the contrary notwithstanding, the Company shall be entitled to make such reductions in the Purchase Price, in addition to those adjustments expressly required by this Section 11, as and to the extent that, it, in its sole discretion, shall determine to be advisable in order that any consolidation or subdivision of the Preferred Shares, issuance wholly for cash of any Preferred Shares at less than the current market price, issuance wholly for cash of Preferred Shares or

securities which by their terms are convertible into or exchangeable for Preferred Shares, dividends on Preferred Shares payable in Preferred Shares or issuance of rights, options or warrants referred to hereinabove in Section 11(b), hereafter made by the Company to holders of its Preferred Shares shall not be taxable to such stockholders.

(n) In the event that at any time after the date of this Rights Agreement and prior to the Distribution Date, the Company shall (i) declare or pay any dividend on the Common Shares payable in Common Shares or (ii) effect a subdivision, combination or consolidation of the Common Shares (by reclassification or otherwise than by payment of dividends in Common Shares) into a greater or lesser number of Common Shares, then in any such case (A) the number of one one-thousandths of a Preferred Share purchasable after such event upon proper exercise of each Right shall be determined by multiplying the number of one one-thousandths of a Preferred Share so purchasable immediately prior to such event by a fraction, the numerator of which is the number of Common Shares outstanding immediately before such event and the denominator of which is the number of Common Shares outstanding immediately after such event, and (B) each Common Share outstanding immediately after such event shall have issued with respect to it that number of Rights which each Common Share outstanding immediately prior to such event had issued with respect to it. The adjustments provided for in this Section 11(n) shall be made successively whenever such a dividend is declared or paid or such a subdivision, combination or consolidation is effected.

Section 12. Certificate of Adjusted Purchase Price or Number of Shares. Whenever an adjustment is made as provided in Sections 11 or 13 hereof, the Company shall promptly (a) prepare a certificate setting forth such adjustment, and a brief statement of the facts accounting for such adjustment, (b) file with the Rights Agent and with each transfer agent for the Common Shares or the Preferred Shares a copy of such certificate and (c) if a Distribution Date has occurred, mail a brief summary thereof to each holder of a Right Certificate in accordance with Section 25 hereof.

Section 13. Consolidation, Merger or Sale or Transfer of Assets or Earning Power. Except for any transaction approved by the Board of Directors (upon approval by a majority of the Continuing Directors), in the event, directly or indirectly, at any time after a Person has become an Acquiring Person, (a) the Company shall consolidate with, or merge with and into, any other Person, (b) any Person shall consolidate with the Company, or merge with and into the Company and the Company shall be the continuing or surviving corporation of such merger and, in connection with such merger, all or part of the Common Shares shall be changed into or exchanged for stock or other securities of any other Person (or the Company) or cash or any other property or (c) the Company shall sell or otherwise transfer (or one or more of its Subsidiaries shall sell or otherwise transfer), in one or more transactions, assets or earning power aggregating 50% or more of the assets or earning power of the Company and its Subsidiaries (taken as a whole) to any other Person other than the Company or one or more of its wholly-owned Subsidiaries, then, and in each such case, proper provision shall be made so that

(i) each holder of a Right (except as otherwise provided herein) shall thereafter have the right to receive, upon the exercise thereof at a price equal to the then current Purchase Price multiplied by the number of one one-thousandths of a Preferred Share for which a Right is then exercisable, in accordance with the terms of this Rights Agreement and in lieu of Preferred Shares, such number of Common Shares of such other Person (including the Company as successor thereto or as the surviving corporation) as shall equal the result obtained by (A) multiplying the then current Purchase Price by the number of one one-thousandths of a Preferred Share for which a Right is then exercisable and dividing that product by (B) 50% of the then current per share market price of the Common Shares of such other Person (determined pursuant to Section 11(d) hereof) on the date of consummation of such consolidation, merger, sale or transfer;

(ii) the issuer of such Common Shares shall thereafter be liable for, and shall assume, by virtue of such consolidation, merger, sale or transfer, all the obligations and duties of the Company pursuant to this Rights Agreement;

(iii) the term "Company" shall thereafter be deemed to refer to such issuer; and

(iv) such issuer shall take such steps (including, but not limited to, the reservation of a sufficient number of its Common Shares in accordance with Section 9 hereof) in connection with such consummation as may be necessary to assure that the provisions hereof shall thereafter be applicable, as nearly as reasonably may be, in relation to the Common Shares thereafter deliverable upon the exercise of the Rights.

The Company shall not consummate any such consolidation, merger, sale or transfer unless prior thereto the Company and such issuer shall have executed and delivered to the Rights Agent a supplemental agreement so providing. The Company shall not enter into any transaction of the kind referred to in this Section 13 if at the time of such transaction there are any rights, warrants, instruments or securities outstanding or any agreements or arrangements which, as a result of the consummation of such transaction, would eliminate or substantially diminish the benefits intended to be afforded by the Rights. The provisions of this Section 13 shall similarly apply to successive mergers or consolidations or sales or other transfers.

Section 14. Fractional Rights and Fractional Shares.

(a) The Company shall not be required to issue fractions of Rights or to distribute Right Certificates which evidence fractional Rights. In lieu of such fractional Rights, there shall be paid to the registered holders of the Right Certificates with regard to which such fractional Rights would otherwise be issuable, an amount in cash equal to the same fraction of the current market value of a whole Right. For the purposes of this Section 14(a), the current market value of a whole Right shall be the closing price of the Rights for the Trading Day immediately prior to the date on which such fractional Rights would have been otherwise issuable. The closing price for any day shall be the last sale

price, regular way, or, in case no such sale takes place on such day, the average of the closing bid and asked prices, regular way, in either case, as reported in the principal consolidated transaction reporting system with respect to securities listed or admitted to trading on the New York Stock Exchange or, if the Rights are not listed or admitted to trading on the New York Stock Exchange, as reported in the principal consolidated transaction reporting system with respect to securities listed on the principal national securities exchange on which the Rights are listed or admitted to trading or, if the Rights are not listed or admitted to trading on any national securities exchange, the last quoted price or, if not so quoted, the average of the high bid and low asked prices in the over-the-counter market, as reported by NASDAQ or such other system then in use or, if on any such date the Rights are not quoted by any such organization, the average of the closing bid and asked prices as furnished by a professional market maker making a market in the Rights selected by the Board of Directors of the Company (upon the approval of a majority of the Continuing Directors). If on any such date no such market maker is making a market in the Rights, the fair value of the Rights on such date as determined in good faith by the Board of Directors of the Company (upon the approval of a majority of the Continuing Directors) shall be used.

(b) The Company shall not be required to issue fractions of Preferred Shares (other than fractions which are integral multiples of one one-thousandth of a Preferred Share) upon exercise of the Rights or to distribute certificates which evidence fractional Preferred Shares (other than fractions which are integral multiples of one one-thousandth of a Preferred Share). Fractions of Preferred Shares in integral multiples of one one-thousandth of a Preferred Share may, at the election of the Company, be evidenced by depositary receipts, pursuant to an appropriate agreement between the Company and a depositary selected by it; provided that such agreement shall provide that the holders of such depositary receipts shall have all the rights, privileges and preferences to which they are entitled as Beneficial Owners of the Preferred Shares represented by such depositary receipts. In lieu of fractional Preferred Shares that are not integral multiples of one one-thousandth of a Preferred Share, the Company shall pay to the registered holders of Right Certificates at the time such Rights are exercised as herein provided an amount in cash equal to the same fraction of the current market value of one Preferred Share. For the purposes of this Section 14(b), the current market value of a Preferred Share shall be the closing price of a Preferred Share (as determined pursuant to the second sentence of Section 11(d)(i) hereof) for the Trading Day immediately prior to the date of such exercise.

(c) The holder of a Right by the acceptance of the Right expressly waives his right to receive any fractional Rights or any fractional shares upon exercise of a Right (except as expressly provided above).

Section 15. Rights of Action. All rights of action in respect of this Rights Agreement, except the rights of action given to the Rights Agent under Section 18 hereof, are vested in the respective registered holders of the Right Certificates (and, prior to the Distribution Date, the registered holders of the Common

Shares); and any registered holder of any Right Certificate (or, prior to the Distribution Date, of the Common Shares), without the consent of the Rights Agent or of the holder of any other Right Certificate (or, prior to the Distribution Date, of the Common Shares), may, in his own behalf and for his own benefit, enforce, and may institute and maintain any suit, action or proceeding against the Company to enforce, or otherwise act in respect of, his right to exercise the Rights evidenced by such Right Certificate in the manner provided in such Right Certificate and in this Rights Agreement. Without limiting the foregoing or any remedies available to the holders of Rights, it is specifically acknowledged that the holders of Rights would not have an adequate remedy at law for any breach of this Rights Agreement and will be entitled to specific performance of the obligations under, and injunctive relief against actual or threatened violations of the obligations of any Person subject to, this Rights Agreement.

Section 16. Agreement of Right Holders. Every holder of a Right, by accepting the same, consents and agrees with the Company and the Rights Agent and with every other holder of a Right that:

(a) prior to the Distribution Date, the Rights will be transferable only in connection with the transfer of the Common Shares;

(b) after the Distribution Date, the Right Certificates are transferable only on the registry books of the Rights Agent if surrendered at the principal office of the Rights Agent, duly endorsed or accompanied by a proper instrument of transfer; and

(c) the Company and the Rights Agent may deem and treat the Person in whose name the Right Certificate (or, prior to the Distribution Date, the associated Common Shares certificate) is registered as the absolute owner thereof and of the Rights evidenced thereby (notwithstanding any notations of ownership or writing on the Right Certificate or the associated Common Shares certificate made by anyone other than the Company or the Rights Agent) for all purposes whatsoever, and neither the Company nor the Rights Agent shall be affected by any notice to the contrary.

Section 17. Right Certificate Holder Not Deemed a Stockholder. No holder, as such, of any Right Certificate shall be entitled to vote, receive dividends or be deemed for any purpose the holder of the Preferred Shares or any other securities of the Company which may at any time be issuable on the exercise of the Rights represented thereby, nor shall anything contained herein or in any Right Certificate be construed to confer upon the holder of any Right Certificate, as such, any of the rights of a stockholder of the Company or any right to vote for the election of directors or upon any matter submitted to stockholders at any meeting thereof, or to give or withhold consent to any corporate action, or to receive notice of meetings or other actions affecting stockholders (except as provided in Section 25 hereof), or to receive dividends or subscription rights, or otherwise, until the Right or Rights evidenced by such Right Certificate shall have been exercised in accordance with the provisions hereof.

Section 18. Concerning the Rights Agent.

(a) The Company agrees to pay to the Rights Agent reasonable compensation for all services rendered by it hereunder and, from time to time, on demand of the Rights Agent, its reasonable expenses and counsel fees and other disbursements incurred in the administration and execution of this Rights Agreement and the exercise and performance of its duties hereunder. The Company also agrees to indemnify the Rights Agent for, and to hold it harmless against, any loss, liability or expense incurred without negligence, bad faith or willful misconduct on the part of the Rights Agent, for anything done or omitted by the Rights Agent in connection with the acceptance and administration of this Rights Agreement, including the costs and expenses of defending against any claim of liability in the premises.

(b) The Rights Agent shall be protected and shall incur no liability for, or in respect of any action taken, suffered or omitted by it in connection with, its administration of this Rights Agreement in reliance upon any Right Certificate or certificate for the Preferred Shares or Common Shares or for other securities of the Company, instrument of assignment or transfer, power of attorney, endorsement, affidavit, letter, notice, direction, consent, certificate, statement, or other paper or document believed by it to be genuine and to be signed, executed and, where necessary, verified or acknowledged, by the proper Person or Persons, or otherwise upon the advice of counsel as set forth in Section 20 hereof.

Section 19. Merger or Consolidation or Change of Name of Rights Agent.

(a) Any corporation into which the Rights Agent or any successor Rights Agent may be merged or with which it may be consolidated, or any corporation resulting from any merger or consolidation to which the Rights Agent or any successor Rights Agent shall be a party, or any corporation succeeding to the stock transfer or corporate trust powers of the Rights Agent or any successor Rights Agent, shall be the successor to the Rights Agent under this Rights Agreement without the execution or filing of any paper or any further act on the part of any of the parties hereto; provided that such corporation would be eligible for appointment as a successor Rights Agent under the provisions of Section 21 hereof. In case at the time such successor Rights Agent shall succeed to the agency created by this Rights Agreement, any of the Right Certificates shall have been countersigned but not delivered, any such successor Rights Agent may adopt the countersignature of the predecessor Rights Agent and deliver such Right Certificates so countersigned; and, in case at that time any of the Right Certificates shall not have been countersigned, any successor Rights Agent may countersign such Right Certificates either in the name of the predecessor Rights Agent or in the name of the successor Rights Agent; and in all such cases such Right Certificates shall have the full force provided in the Right Certificates and in this Rights Agreement.

(b) In case at any time the name of the Rights Agent shall be changed and at such time any of the Right Certificates shall have been countersigned but not delivered, the Rights Agent may adopt the countersignature under its prior name and deliver Right Certificates so countersigned; and in case at that time any of the Right Certificates shall not have been countersigned, the Rights Agent may countersign such

Right Certificates either in its prior name or in its changed name; and in all such cases such Right Certificates shall have the full force provided in the Right Certificates and in this Rights Agreement.

Section 20. Duties of Rights Agent. The Rights Agent undertakes the duties and obligations imposed by this Rights Agreement upon the following terms and conditions, by all of which the Company and the holders of Right Certificates, by their acceptance thereof, shall be bound:

(a) The Rights Agent may consult with legal counsel (who may be legal counsel for the Company), and the opinion of such counsel shall be full and complete authorization and protection to the Rights Agent as to any action taken or omitted by it in good faith and in accordance with such opinion.

(b) Whenever in the performance of its duties under this Rights Agreement the Rights Agent shall deem it necessary or desirable that any fact or matter be proved or established by the Company prior to taking or suffering any action hereunder, such fact or matter (unless other evidence in respect thereof be herein specifically prescribed) may be deemed to be conclusively proved and established by a certificate signed by any one of the Chairman of the Board, the Chief Executive Officer, the President, any Vice President, the Treasurer or the Secretary of the Company and delivered to the Rights Agent; and such certificate shall be full authorization to the Rights Agent for any action taken or suffered in good faith by it under the provisions of this Rights Agreement in reliance upon such certificate.

(c) The Rights Agent shall be liable hereunder to the Company and any other Person only for its own negligence, bad faith or willful misconduct.

(d) The Rights Agent shall not be liable for or by reason of any of the statements of fact or recitals contained in this Rights Agreement or in the Right Certificates (except its countersignature thereof) or be required to verify the same, but all such statements and recitals are and shall be deemed to have been made by the Company only.

(e) The Rights Agent shall not be under any responsibility in respect of the validity of this Rights Agreement or the execution and delivery hereof (except the due execution hereof by the Rights Agent) or in respect of the validity or execution of any Right Certificate (except its countersignature thereof); nor shall it be responsible for any breach by the Company of any covenant or condition contained in this Rights Agreement or in any Right Certificate; nor shall it be responsible for any change in the exercisability of the Rights (including the Rights becoming void pursuant to Section 11(a)(ii) hereof) or any adjustment in the terms of the Rights (including the manner, method or amount thereof) provided for in Section 3, 11, 13, 23 or 24, or the ascertaining of the existence of facts that would require any such change or adjustment (except with respect to the exercise of Rights evidenced by Right Certificates after actual notice that such change or adjustment is required); nor shall it by any act hereunder be deemed to make any

representation or warranty as to the authorization or reservation of any Preferred Shares to be issued pursuant to this Rights Agreement or any Right Certificate or as to whether any Preferred Shares will, when issued, be validly authorized and issued, fully paid and nonassessable.

(f) The Company agrees that it will perform, execute, acknowledge and deliver or cause to be performed, executed, acknowledged and delivered all such further and other acts, instruments and assurances as may reasonably be required by the Rights Agent for the carrying out or performing by the Rights Agent of the provisions of this Rights Agreement.

(g) The Rights Agent is hereby authorized and directed to accept instructions with respect to the performance of its duties hereunder from any one of the Chairman of the Board, the Chief Executive Officer, the President, any Vice President, the Secretary or the Treasurer of the Company, and to apply to such officers for advice or instructions in connection with its duties, and it shall not be liable for any action taken or suffered by it in good faith in accordance with instructions of any such officer or for any delay in acting while waiting for those instructions.

(h) The Rights Agent and any stockholder, director, officer or employee of the Rights Agent may buy, sell or deal in any of the Rights or other securities of the Company or become pecuniarily interested in any transaction in which the Company may be interested, or contract with or lend money to the Company or otherwise act as fully and freely as though it were not Rights Agent under this Rights Agreement. Nothing herein shall preclude the Rights Agent from acting in any other capacity for the Company or for any other legal entity.

(i) The Rights Agent may execute and exercise any of the rights or powers hereby vested in it or perform any duty hereunder either itself or by or through its attorneys or agents, and the Rights Agent shall not be answerable or accountable for any act, default, neglect or misconduct of any such attorneys or agents or for any loss to the Company resulting from any such act, default, neglect or misconduct, provided reasonable care was exercised in the selection and continued employment thereof.

Section 21. Change of Rights Agent. The Rights Agent or any successor Rights Agent may resign and be discharged from its duties under this Rights Agreement upon 30-days' notice in writing mailed to the Company and to each transfer agent of the Common Shares or Preferred Shares by registered or certified mail, and to the holders of the Right Certificates. The Company may remove the Rights Agent or any successor Rights Agent upon 30-days' notice in writing, mailed to the Rights Agent or successor Rights Agent, as the case may be, and to each transfer agent of the Common Shares or Preferred Shares by registered or certified mail, and to the holders of the Right Certificates. If the Rights Agent shall resign or be removed or shall otherwise become incapable of acting, the Company shall appoint a successor to the Rights Agent. If the Company shall fail to make such appointment within a period of 30 days after giving notice of such removal or after it has been notified in writing of such resignation or

incapacity by the resigning or incapacitated Rights Agent or by the holder of a Right Certificate (who shall, with such notice, submit his Right Certificate for inspection by the Company), then the registered holder of any Right Certificate may apply to any court of competent jurisdiction for the appointment of a new Rights Agent. Any successor Rights Agent, whether appointed by the Company or by such a court, shall be a corporation organized and doing business under the laws of the United States or of the State of New York (or of any other state of the United States so long as such corporation is authorized to do business as a banking institution in the State of New York, in good standing, having an office in the State of New York), which is (i) authorized under such laws to exercise corporate trust or stock transfer powers and is subject to supervision or examination by federal or state authority and which has at the time of its appointment as Rights Agent a combined capital and surplus of at least $50 million or (ii) affiliated with a corporation described in clause (i) of this sentence. After appointment, the successor Rights Agent shall be vested with the same powers, rights, duties and responsibilities as if it had been originally named as Rights Agent without further act or deed; but the predecessor Rights Agent shall deliver and transfer to the successor Rights Agent any property at the time held by it hereunder, and execute and deliver any further assurance, conveyance, act or deed necessary for the purpose. Not later than the effective date of any such appointment, the Company shall file notice thereof in writing with the predecessor Rights Agent and each transfer agent of the Common Shares or Preferred Shares, and mail a notice thereof in writing to the registered holders of the Right Certificates. Failure to give any notice provided for in this Section 21, however, or any defect therein, shall not affect the legality or validity of the resignation or removal of the Rights Agent or the appointment of the successor Rights Agent, as the case may be.

Section 22. Issuance of New Right Certificates. Notwithstanding any of the provisions of this Rights Agreement or of the Rights to the contrary, the Company may, at its option, issue new Right Certificates evidencing Rights in such form as may be approved by the Board of Directors of the Company (upon the approval of a majority of the Continuing Directors) to reflect any adjustment or change in the Purchase Price and the number or kind or class of shares or other securities or property purchasable under the Right Certificates made in accordance with the provisions of this Rights Agreement.

Section 23. Redemption. (a) The Board of Directors of the Company, at its option, at any time prior to the Close of Business on the tenth day following the Stock Acquisition Date, redeem all but not less than all the then outstanding Rights at a redemption price of $.005 per Right, appropriately adjusted to reflect any stock split, stock dividend or similar transaction occurring after the date hereof (such redemption price being hereinafter referred to as the "Redemption Price"), provided, however, that during the time period relating to when the Rights may be redeemed, the Board of Directors of the Company may extend the time during which the Rights may be redeemed to be at any time as may be determined by the Board of Directors, and provided, further, that if the Board of Directors of the Company authorizes redemption of the Rights or an extension of the time period during which the Rights may be redeemed after the time that any Person becomes an Acquiring Person, then there must be Continuing Directors then in office and such authorization or extension shall require the concurrence of a majority

of such Continuing Directors. Notwithstanding anything contained in this Agreement to the contrary, the Rights shall not be exercisable after the first occurrence of the event described in Section 11(a)(ii) until such time as the Company's right of redemption hereunder has expired. The redemption of the Rights by the Board of Directors of the Company may be made effective at such time, on such basis and with such conditions as the Board of Directors of the Company, in its sole discretion, may establish. The Company may, at its option, pay the Redemption Price in cash, Common Shares (based on the current market price at the time of redemption) or any other form of consideration deemed appropriate by the Board of Directors.

(b) Immediately upon the action of the Board of Directors of the Company ordering the redemption of the Rights pursuant to paragraph (a) of this Section 23, and without any further action and without any notice, the right to exercise the Rights will terminate and the only right thereafter of the holders of Rights shall be to receive the Redemption Price. The Company shall promptly give public notice of any such redemption; provided, however, that the failure to give, or any defect in, any such notice shall not affect the validity of such redemption. Within 14 days after such action of the Board of Directors of the Company ordering the redemption of the Rights, the Company shall mail a notice of redemption to all the holders of the then outstanding Rights at their last addresses as they appear upon the registry books of the Rights Agent or, prior to the Distribution Date, on the registry books of the transfer agent for the Common Shares. Any notice which is mailed in the manner herein provided shall be deemed given, whether or not the holder receives the notice. Each such notice of redemption will state the method by which the payment of the Redemption Price will be made. Neither the Company nor any of its Affiliates or Associates may redeem, acquire or purchase for value any Rights at any time in any manner other than that specifically set forth in this Section 23 or in Section 24 hereof, and other than in connection with the purchase of Common Shares prior to the Distribution Date.

Section 24. Exchange. (a) The Board of Directors of the Company (upon the approval of a majority of the Continuing Directors) may, at its option, at any time after any Person becomes an Acquiring Person, exchange all or part of the then outstanding and exercisable Rights (which shall not include Rights that have become void pursuant to the provisions of Section 11(a)(ii) hereof) for Common Shares at an exchange ratio of one Common Share per Right, appropriately adjusted to reflect any stock split, stock dividend or similar transaction occurring after the date hereof (such exchange ratio being hereinafter referred to as the "Exchange Ratio"). Notwithstanding the foregoing, the Board of Directors of the Company shall not be empowered to effect such exchange at any time after any Person (other than the Company, any Subsidiary of the Company, any employee benefit plan of the Company or any such Subsidiary, or any entity holding Common Shares for or pursuant to the terms of any such plan), together with all Affiliates and Associates of such Person, becomes the Beneficial Owner of 50% or more of the Common Shares then outstanding.

(b) Immediately upon the action of the Board of Directors of the Company (upon the approval of a majority of the Continuing Directors) ordering the exchange of

any Rights pursuant to paragraph (a) of this Section 24 and without any further action and without any notice, the right to exercise such Rights shall terminate and the only right thereafter of a holder of such Rights shall be to receive that number of Common Shares equal to the number of such Rights held by such holder multiplied by the Exchange Ratio. The Company shall promptly give public notice of any such exchange; provided, however, that the failure to give, or any defect in, such notice shall not affect the validity of such exchange. The Company promptly shall mail a notice of any such exchange to all of the holders of such Rights at their last addresses as they appear upon the registry books of the Rights Agent. Any notice which is mailed in the manner herein provided shall be deemed given, whether or not the holder receives the notice. Each such notice of exchange will state the method by which the exchange of the Common Shares for Rights will be effected and, in the event of any partial exchange, the number of Rights which will be exchanged. Any partial exchange shall be effected pro rata based on the number of Rights (other than Rights which have become void pursuant to the provisions of Section 11(a)(ii) hereof) held by each holder of Rights.

(c) In the event that there shall not be sufficient Common Shares issued but not outstanding or authorized but unissued to permit any exchange of Rights as contemplated in accordance with this Section 24, the Company shall take all such action as may be necessary to authorize additional Common Shares for issuance upon exchange of the Rights. In the event the Company shall, after good faith effort, be unable to take all such action as may be necessary to authorize such additional Common Shares, the Company shall substitute, for each Common Share that would otherwise be issuable upon exchange of a Right, a number of Preferred Shares or fraction thereof (or a security with substantially similar rights, privileges, preferences, voting power and economic rights) such that the current per share market price of one Preferred Share (or other such security) multiplied by such number or fraction is equal to the current per share market price of one Common Share as of the date of issuance of such Preferred Shares or fraction thereof (or other such security).

(d) The Company shall not be required to issue fractions of Common Shares or to distribute certificates which evidence fractional Common Shares. In lieu of such fractional Common Shares, the Company shall pay to the registered holders of the Right Certificates with regard to which such fractional Common Shares would otherwise be issuable an amount in cash equal to the same fraction of the current market value of a whole Common Share. For the purposes of this paragraph (d), the current market value of a whole Common Share shall be the closing price of a Common Share (as determined pursuant to the second sentence of Section 11(d)(i) hereof) for the Trading Day immediately prior to the date of exchange pursuant to this Section 24.

Section 25. Notice of Certain Events. (a) In case the Company shall propose (i) to pay any dividend payable in stock of any class to the holders of its Preferred Shares or to make any other distribution to the holders of its Preferred Shares (other than a regular quarterly cash dividend), (ii) to offer to the holders of its Preferred Shares rights or warrants to subscribe for or to purchase any additional Preferred Shares or shares of stock of any class or any other securities, rights or options, (iii) to effect any

reclassification of its Preferred Shares (other than a reclassification involving only the subdivision of outstanding Preferred Shares), (iv) to effect any consolidation or merger into or with, or to effect any sale or other transfer (or to permit one or more of its Subsidiaries to effect any sale or other transfer), in one or more transactions, of 50% or more of the assets or earning power of the Company and its Subsidiaries (taken as a whole) to, any other Person, (v) to effect the liquidation, dissolution or winding up of the Company, or (vi) to declare or pay any dividend on the Common Shares payable in Common Shares or to effect a subdivision, combination or consolidation of the Common Shares (by reclassification or otherwise than by payment of dividends in Common Shares), then, in each such case, the Company shall give to each holder of a Right Certificate, in accordance with Section 26 hereof, a notice of such proposed action, which shall specify the record date for the purposes of such stock dividend, or distribution of rights or warrants, or the date on which such reclassification, consolidation, merger, sale, transfer, liquidation, dissolution, or winding up is to take place and the date of participation therein by the holders of the Common Shares and/or Preferred Shares, if any such date is to be fixed, and such notice shall be so given in the case of any action covered by clause (i) or (ii) above at least 10 days prior to the record date for determining holders of the Preferred Shares for purposes of such action, and in the case of any such other action, at least 10 days prior to the date of the taking of such proposed action or the date of participation therein by the holders of the Common Shares and/or Preferred Shares, whichever shall be the earlier.

(b) In case the event set forth in Section 11(a)(ii) hereof shall occur, then the Company shall as soon as practicable thereafter give to each holder of a Right Certificate, in accordance with Section 26 hereof, a notice of the occurrence of such event, which notice shall describe such event and the consequences of such event to holders of Rights under Section 11(a)(ii) hereof.

Section 26. Notices. Notices or demands authorized by this Rights Agreement to be given or made by the Rights Agent or by the holder of any Right Certificate to or on the Company shall be sufficiently given or made if sent by first-class mail, postage prepaid, addressed (until another address is filed in writing with the Rights Agent) as follows:

Eli Lilly and Company
Lilly Corporate Center
Indianapolis, Indiana 46285
Attention: Corporate Secretary

Subject to the provisions of Section 21 hereof, any notice or demand authorized by this Rights Agreement to be given or made by the Company or by the holder of any Right Certificate to or on the Rights Agent shall be sufficiently given or made if sent by first-class mail, postage prepaid, addressed (until another address is filed in writing with the Company) as follows:

First Chicago Trust Company of New York
Suite 4660
525 Washington Blvd.
Jersey City, New Jersey 07310
Attention: Tenders and Exchanges Administration

Notices or demands authorized by this Rights Agreement to be given or made by the Company or the Rights Agent to the holder of any Right Certificate shall be sufficiently given or made if sent by first-class mail, postage prepaid, addressed to such holder at the address of such holder as shown on the registry books of the Company.

Section 27. Supplements and Amendments. For as long as the Rights are then redeemable and except as provided in the last sentence of this Section 27, the Company may in its sole and absolute discretion, and the Rights Agent shall if the Company so directs, supplement or amend any provision of this Agreement without the approval of any holders of the Rights. At any time when the Rights are not then redeemable and except as provided in the last sentence of this Section 27, the Company may, and the Rights Agent shall if the Company so directs, supplement or amend this Rights Agreement without the approval of any holders of Rights Certificates (i) to cure any ambiguity, (ii) to correct or supplement any provision contained herein which may be defective or inconsistent with any other provisions herein or (iii) to change or supplement the provisions hereunder in any manner which the Company may deem necessary or desirable, provided that no such supplement or amendment pursuant to this clause (iii) shall materially adversely affect the interest of the holders of Rights Certificates. Upon the delivery of a certificate from an appropriate officer of the Company which states that the proposed supplement or amendment is in compliance with the terms of this Section 27, the Rights Agent shall execute such supplement or amendment. Notwithstanding anything contained in this Rights Agreement to the contrary, supplements or amendments may be made only upon approval by a majority of the Continuing Directors..

Section 28. Successors. All the covenants and provisions of this Rights Agreement by or for the benefit of the Company or the Rights Agent shall bind and inure to the benefit of their respective successors and assigns hereunder.

Section 29. Benefits of this Rights Agreement. Nothing in this Rights Agreement shall be construed to give to any Person, other than the Company, the Rights Agent and the registered holders of the Right Certificates (and, prior to the Distribution Date, the Common Shares) any legal or equitable right, remedy or claim under this Rights Agreement; but this Rights Agreement shall be for the sole and exclusive benefit of the Company, the Rights Agent and the registered holders of the Right Certificates (and, prior to the Distribution Date, the Common Shares).

Section 30. Severability. If any term, provision, covenant or restriction of this Rights Agreement is held by a court of competent jurisdiction to be invalid, void or unenforceable, the remainder of the terms, provisions, covenants and restrictions of this

Rights Agreement shall remain in full force and effect and shall in no way be affected, impaired or invalidated.

Section 31. Governing Law. This Rights Agreement and each Right Certificate issued hereunder shall be deemed to be a contract made under the laws of the State of Indiana and for all purposes shall be governed by and construed in accordance with the laws of such State applicable to contracts to be made and performed entirely within such State.

Section 32. Counterparts. This Rights Agreement may be executed in any number of counterparts and each of such counterparts shall for all purposes be deemed to be an original, and all such counterparts shall together constitute but one and the same instrument.

Section 33. Descriptive Headings. Descriptive headings of the several Sections of this Rights Agreement are inserted for convenience only and shall not control or affect the meaning or construction of any of the provisions hereof.

IN WITNESS WHEREOF, the parties hereto have caused this Rights Agreement to be duly executed and attested, all as of the day and year first above written.

ELI LILLY AND COMPANY

By: /s/ Edwin W. Miller

Name: Edwin W. Miller
Title: Vice President and Treasurer

FIRST CHICAGO TRUST COMPANY OF NEW YORK

By: /s/ Joanne Gorostiolla

Name: Joanne Gorostiolla
Title: Assistant Vice President

Exhibit A

FORM
of
ARTICLES OF AMENDMENT
setting forth terms of
SERIES B JUNIOR PARTICIPATING PREFERRED STOCK
of
ELI LILLY AND COMPANY

ARTICLE 1.

The name of the corporation filing these Articles of Amendment is ELI LILLY AND COMPANY, an Indiana corporation (the "Corporation").

ARTICLE 2.

The following sets forth the designation and number of shares, and fixes the preferences, limitations and relative voting and other rights of the Series B Junior Participating Preferred Stock of the Corporation:

Section 1. Designation and Amount. The shares of such series shall be designated as "Series B Junior Participating Preferred Stock" (the "Series B Preferred Stock") and the number of shares constituting the Series B Preferred Stock shall be 1,500,000. Such number of shares may be increased or decreased by resolution of the Board of Directors; provided that no decrease shall reduce the number of shares of Series B Preferred Stock to a number less than the number of shares then outstanding plus the number of shares reserved for issuance upon the exercise of outstanding options, rights or warrants or upon the conversion of any outstanding securities issued by the Corporation convertible into Series B Preferred Stock.

Section 2. Dividends and Distributions.

(A) Subject to the rights of the holders of any shares of any series of Preferred Stock (or any similar stock) ranking prior and superior to the Series B Preferred Stock with respect to dividends, the holders of shares of Series B Preferred Stock, in preference to the holders of Common Stock, without par value (the "Common Stock"), of the Corporation, and of any other junior stock, shall be entitled to receive, when, as and if declared by the Board of Directors out of funds legally available for the purpose, quarterly dividends payable in cash on the tenth day of March, June, September and December in each year (each such date being referred to herein as a "Quarterly Dividend Payment Date"), commencing on the first Quarterly Dividend Payment Date after the

first issuance of a share or fraction of a share of Series B Preferred Stock, in an amount per share (rounded to the nearest cent) equal to the greater of (a) $10 or (b) subject to the provision for adjustment hereinafter set forth, 1,000 times the aggregate per share amount of all cash dividends, and 1,000 times the aggregate per share amount (payable in kind) of all non- cash dividends or other distributions, other than a dividend payable in shares of Common Stock or a subdivision of the outstanding shares of Common Stock (by reclassification or otherwise), declared on the Common Stock since the immediately preceding Quarterly Dividend Payment Date or, with respect to the first Quarterly Dividend Payment Date, since the first issuance of any share or fraction of a share of Series B Preferred Stock. In the event the Corporation shall at any time declare or pay any dividend on the Common Stock payable in shares of Common Stock, or effect a subdivision or combination or consolidation of the outstanding shares of Common Stock (by reclassification or otherwise than by payment of a dividend in shares of Common Stock) into a greater or lesser number of shares of Common Stock, then in each such case the amount to which holders of shares of Series B Preferred Stock were entitled immediately prior to such event under clause (b) of the preceding sentence shall be adjusted by multiplying such amount by a fraction, the numerator of which is the number of shares of Common Stock outstanding immediately after such event and the denominator of which is the number of shares of Common Stock that were outstanding immediately prior to such event.

(B) The Corporation shall declare a dividend or distribution on the Series B Preferred Stock as provided in paragraph (A) of this Section immediately after it declares a dividend or distribution on the Common Stock (other than a dividend payable in shares of Common Stock); provided that, in the event no dividend or distribution shall have been declared on the Common Stock during the period between any Quarterly Dividend Payment Date and the next subsequent Quarterly Dividend Payment Date, a dividend of $10 per share on the Series B Preferred Stock shall nevertheless be payable on such subsequent Quarterly Dividend Payment Date.

(C) Dividends shall begin to accrue and be cumulative on outstanding shares of Series B Preferred Stock from the Quarterly Dividend Payment Date next preceding the date of issue of such shares, unless the date of issue of such shares is prior to the record date for the first Quarterly Dividend Payment Date, in which case dividends on such shares shall begin to accrue from the date of issue of such shares, or unless the date of issue is a Quarterly Dividend Payment Date or is a date after the record date for the determination of holders of shares of Series B Preferred Stock entitled to receive a quarterly dividend and before such Quarterly Dividend Payment Date, in either of which events such dividends shall begin to accrue and be cumulative from such Quarterly Dividend Payment Date. Accrued but unpaid dividends shall not bear interest. Dividends paid on the shares of Series B Preferred Stock in an amount less than the total amount of such dividends at the time accrued and payable on such shares shall be allocated pro rata on a share-by-share basis among all such shares at the time outstanding. The Board of Directors may fix a record date for the determination of holders of shares of Series B Preferred Stock entitled to receive payment of a dividend or distribution declared thereon, which record date shall be not more than 60 days prior to the date fixed for the payment thereof.

Section 3. Voting Rights. The holders of shares of Series B Preferred Stock shall have the following voting rights:

(A) Subject to the provision for adjustment hereinafter set forth, each share of Series B Preferred Stock shall entitle the holder thereof to 1000 votes on all matters submitted to a vote of the stockholders of the Corporation. In the event the Corporation shall at any time declare or pay any dividend on the Common Stock payable in shares of Common Stock, or effect a subdivision or combination or consolidation of the outstanding shares of Common Stock (by reclassification or otherwise than by payment of a dividend in shares of Common Stock) into a greater or lesser number of shares of Common Stock, then in each such case the number of votes per share to which holders of shares of Series B Preferred Stock were entitled immediately prior to such event shall be adjusted by multiplying such number by a fraction, the numerator of which is the number of shares of Common Stock outstanding immediately after such event and the denominator of which is the number of shares of Common Stock that were outstanding immediately prior to such event.

(B) Except as otherwise provided herein, in any other Articles of Amendment creating a series of Preferred Stock or any similar stock, or by law, the holders of shares of Series B Preferred Stock and the holders of shares of Common Stock and any other capital stock of the Corporation having general voting rights shall vote together as one class on all matters submitted to a vote of stockholders of the Corporation.

(C) Except as set forth herein, or as otherwise provided by law, holders of Series B Preferred Stock shall have no special voting rights and their consent shall not be required (except to the extent they are entitled to vote with holders of Common Stock as set forth herein) for taking any corporate action.

Section 4. Certain Restrictions.

(A) Whenever quarterly dividends or other dividends or distributions payable on the Series B Preferred Stock as provided in Section 2 are in arrears, thereafter and until all accrued and unpaid dividends and distributions, whether or not declared, on shares of Series B Preferred Stock outstanding shall have been paid in full, the Corporation shall not:

(i) declare or pay dividends, or make any other distributions, on any shares of stock ranking junior (either as to dividends or upon liquidation, dissolution or winding up) to the Series B Preferred Stock;

(ii) declare or pay dividends, or make any other distributions, on any shares of stock ranking on a parity (either as to dividends or upon liquidation, dissolution or winding up) with the Series B Preferred Stock, except dividends paid ratably on the Series B Preferred Stock and all such parity stock on which dividends are payable or in arrears in proportion to the total amounts to which the holders of all such shares are then entitled;

(iii) redeem or purchase or otherwise acquire for consideration shares of any stock ranking junior (either as to dividends or upon liquidation, dissolution or winding up) to the Series B Preferred Stock, provided that the Corporation may at any time redeem, purchase or otherwise acquire shares of any such junior stock in exchange for shares of any stock of the Corporation ranking junior (either as to dividends or upon dissolution, liquidation or winding up) to the Series B Preferred Stock; or

(iv) redeem or purchase or otherwise acquire for consideration any shares of Series B Preferred Stock, or any shares of stock ranking on a parity with the Series B Preferred Stock, except in accordance with a purchase offer made in writing or by publication (as determined by the Board of Directors) to all holders of such shares upon such terms as the Board of Directors, after consideration of the respective annual dividend rates and other relative rights and preferences of the respective series and classes, shall determine in good faith will result in fair and equitable treatment among the respective series or classes.

(B) The Corporation shall not permit any subsidiary of the Corporation to purchase or otherwise acquire for consideration any shares of stock of the Corporation unless the Corporation could, under paragraph (A) of this Section 4, purchase or otherwise acquire such shares at such time and in such manner.

Section 5. Reacquired Shares. Any shares of Series B Preferred Stock purchased or otherwise acquired by the Corporation in any manner whatsoever shall be retired and cancelled promptly after the acquisition thereof. All such shares shall upon their cancellation become authorized but unissued shares of Preferred Stock and may be reissued as part of a new series of Preferred Stock subject to the conditions and restrictions on issuance set forth herein, in the Articles of Incorporation, or in any other Articles of Amendment creating a series of Preferred Stock or any similar stock or as otherwise required by law.

Section 6. Liquidation, Dissolution or Winding Up. Upon any liquidation, dissolution or winding up of the Corporation, no distribution shall be made (1) to the holders of shares of stock ranking junior (either as to dividends or upon liquidation, dissolution or winding up) to the Series B Preferred Stock unless, prior thereto, the holders of shares of Series B Preferred Stock shall have received the greater of (i) $1000 per share, plus an amount equal to accrued and unpaid dividends and distributions thereon, whether or not declared, to the date of such payment, or (ii) an aggregate amount per share, subject to the provision for adjustment hereinafter set forth, equal to 1000 times the aggregate amount to be distributed per share to holders of shares of Common Stock, or (2) to the holders of shares of stock ranking on a parity (either as to dividends or upon liquidation, dissolution or winding up) with the Series B Preferred Stock, except distributions made ratably on the Series B Preferred Stock and all such parity stock in proportion to the total amounts to which the holders of all such shares are entitled upon such liquidation, dissolution or winding up. In the event the Corporation shall at any time declare or pay any dividend on the Common Stock payable in shares of Common Stock, or effect a subdivision or combination or consolidation of the outstanding shares of Common Stock (by reclassification or otherwise than by payment of a dividend in shares of Common Stock) into a greater or lesser number of shares of Common Stock, then in

each such case the aggregate amount to which holders of shares of Series B Preferred Stock were entitled immediately prior to such event under the proviso in clause (1) of the preceding sentence shall be adjusted by multiplying such amount by a fraction the numerator of which is the number of shares of Common Stock outstanding immediately after such event and the denominator of which is the number of shares of Common Stock that were outstanding immediately prior to such event.

Section 7. Consolidation, Merger, etc. In case the Corporation shall enter into any consolidation, merger, combination or other transaction in which the shares of Common Stock are exchanged for or changed into other stock or securities, cash and/or any other property, then in any such case each share of Series B Preferred Stock shall at the same time be similarly exchanged or changed into an amount per share, subject to the provision for adjustment hereinafter set forth, equal to 1000 times the aggregate amount of stock, securities, cash and/or any other property (payable in kind), as the case may be, into which or for which each share of Common Stock is changed or exchanged. In the event the Corporation shall at any time declare or pay any dividend on the Common Stock payable in shares of Common Stock, or effect a subdivision or combination or consolidation of the outstanding shares of Common Stock (by reclassification or otherwise than by payment of a dividend in shares of Common Stock) into a greater or lesser number of shares of Common Stock, then in each such case the amount set forth in the preceding sentence with respect to the exchange or change of shares of Series B Preferred Stock shall be adjusted by multiplying such amount by a fraction, the numerator of which is the number of shares of Common Stock outstanding immediately after such event and the denominator of which is the number of shares of Common Stock that were outstanding immediately prior to such event.

Section 8. No Redemption. The shares of Series B Preferred Stock shall not be redeemable.

Section 9. Rank. The Series B Preferred Stock shall rank, with respect to the payment of dividends and the distribution of assets, junior to all series of any other class of the Corporation's Preferred Stock.

Section 10. Amendment. The Amended Articles of Incorporation of the Corporation shall not be amended in any manner which would materially alter or change the powers, preferences or special rights of the Series B Preferred Stock so as to affect them adversely without the affirmative vote of the holders of at least two-thirds of the outstanding shares of Series B Preferred Stock, voting together as a single class.

Section 11. Expiration of Rights Agreement. In the event that the Rights Agreement dated as of July 20, 1998 between the Corporation and First Chicago Trust Company of New York is terminated or expires prior to the issuance of any shares of Series B Preferred Stock, all shares of Series B Preferred Stock shall become authorized but unissued shares of Preferred Stock and may be reissued as part of a new series of Preferred Stock subject to the conditions and restrictions on issuance set forth in the Articles of Incorporation or in any other Articles of Amendment creating a series of Preferred Stock or any similar stock or as otherwise required by law.

ARTICLE 3.

These Articles of Amendment were duly authorized by the Board of Directors of the Corporation at a meeting duly called and held on July 20, 1998. Pursuant to Indiana Code Sections 23-1-25-2(d) and 23-1-38-2(7), shareholder approval of the foregoing amendment is not required.

IN WITNESS WHEREOF, these Articles of Amendment are executed on behalf of the Corporation by its authorized officers this the ___ day of ____, 1998.

ELI LILLY AND COMPANY

By:_____
Name:
Title:

Attest:

By:_____
Name:
Title:

Exhibit B

Form of Right Certificate

Certificate No. R-

_____ Rights

NOT EXERCISABLE AFTER JULY 28, 2008 OR EARLIER IF REDEMPTION OR EXCHANGE OCCURS. THE RIGHTS ARE SUBJECT TO REDEMPTION AT $.005 PER RIGHT AND TO EXCHANGE ON THE TERMS SET FORTH IN THE RIGHTS AGREEMENT.

Rights Certificate

ELI LILLY AND COMPANY

This certifies that _____, or registered assigns, is the registered owner of the number of Rights set forth above, each of which entitles the owner thereof, subject to the terms, provisions and conditions of the Rights Agreement, dated as of July 20, 1998 (the "Rights Agreement"), between Eli Lilly and Company, an Indiana corporation (the "Company"), and First Chicago Trust Company of New York (the "Rights Agent"), to purchase from the Company at any time after the Distribution Date (as such term is defined in the Rights Agreement) and prior to 5:00 p.m., New York time, on July 28, 2008 at the principal office of the Rights Agent, or at the office of its successor as Rights Agent, one one-thousandth of a fully paid non-assessable share of Series B Junior Participating Preferred Stock of the Company, without par value (the "Preferred Shares"), at a purchase price of $325 per one one-thousandth of a Preferred Share (the "Purchase Price"), upon presentation and surrender of this Right Certificate with the Form of Election to Purchase duly executed. The number of Rights evidenced by this Right Certificate (and the number of one one-thousandths of a Preferred Share which may be purchased upon exercise hereof) set forth above, and the Purchase Price set forth above, are the number and Purchase Price as of July 20, 1998, based on the Preferred Shares as constituted at such date. As provided in the Rights Agreement, the Purchase Price and the number of one one-thousandths of a Preferred Share which may be purchased upon the exercise of the Rights evidenced by this Right Certificate are subject to modification and adjustment upon the happening of certain events.

This Right Certificate is subject to all of the terms, provisions and conditions of the Rights Agreement, which terms, provisions and conditions are hereby incorporated herein by reference and made a part hereof and to which Rights Agreement reference is hereby made for a full description of the rights, limitations of rights, obligations, duties and immunities hereunder of the Rights Agent, the Company and the holders of the Right Certificates. Copies of the Rights Agreement are on file at the principal executive offices of the Company.

This Right Certificate, with or without other Right Certificates, upon surrender at the principal office of the Rights Agent, may be exchanged for another Right Certificate or Right Certificates of like tenor and date evidencing Rights entitling the holder to purchase a like aggregate number of Preferred Shares as the Rights evidenced by the Right Certificate or Right Certificates surrendered shall have entitled such holder to purchase. If this Right Certificate shall be exercised in part, the holder shall be entitled to receive upon surrender hereof another Right Certificate or Right Certificates for the number of whole Rights not exercised.

Subject to the provisions of the Rights Agreement, the Rights evidenced by this Right Certificate (i) may be redeemed by the Company at a redemption price of $.005 per Right or (ii) may be exchanged, in whole or in part, for Preferred Shares or shares of the Company's Common Stock, without par value.

No fractional Preferred Shares will be issued upon the exercise of any Right or Rights evidenced hereby (other than fractions which are integral multiples of one one-thousandth of a Preferred Share, which may, at the election of the Company, be evidenced by depositary receipts), but in, lieu thereof, a cash payment will be made, as provided in the Rights Agreement.

No holder of this Right Certificate shall be entitled to vote or receive dividends or be deemed for any purpose the holder of the Preferred Shares or of any other securities of the Company which may at any time be issuable on the exercise hereof, nor shall anything contained in the Rights Agreement or herein be construed to confer upon the holder hereof, as such, any of the rights of a stockholder of the Company or any right to vote for the election of directors or upon any matter submitted to stockholders at any meeting thereof, or to give or withhold consent to any corporate action, or to receive notice of meetings or other actions affecting stockholders (except as provided in the Rights Agreement), or to receive dividends or subscription rights, or otherwise, until the Right or Rights evidenced by this Right Certificate shall have been exercised as provided in the Rights Agreement.

This Right Certificate shall not be valid or obligatory for any purpose until it shall have been countersigned by the Rights Agent.

WITNESS the facsimile signature of the proper officers of the Company and its corporate seal.

Dated as of _____ __, 1998.

ELI LILLY AND COMPANY

By:_____
Name:
Title:

COUNTERSIGNED:

By_____
Name:
Title:

[Form of Reverse Side of Right Certificate]

FORM OF ASSIGNMENT

(To be executed by the registered holder if such holder desires to transfer the Right Certificate.)

FOR VALUE RECEIVED _____ hereby sells, assigns and transfers unto_____

_____

(Please print name and address of transferee)

this Right Certificate, together with all right, title and interest therein, and does hereby irrevocably constitute and appoint _____ Attorney, to transfer the within Right Certificate on the books of the within-named Company, with full power of substitution.

Dated: _____

Signature _____

Signature Guaranteed:

Signatures must be guaranteed by a member firm of a registered national securities exchange, a member of the National Association of Securities Dealers, Inc., or a commercial bank or trust company having an office or correspondent in the United States.

Certificate

The undersigned hereby certifies that the Rights evidenced by this Right Certificate are not beneficially owned by an Acquiring Person or an Affiliate or Associate thereof (as defined in the Rights Agreement). After due inquiry and to the best knowledge of the undersigned, the Rights evidenced by this Right Certificate were not acquired or beneficially owned by an Acquiring Person or an Affiliate or Associate thereof.

Dated:_____

Signature _____

The signature to the foregoing Assignment and Certificate must correspond to the name as written upon the face of this Right Certificate in every particular, without alteration or enlargement or any change whatsoever.

FORM OF ELECTION TO PURCHASE

(To be executed if holder desires to exercise Rights represented by the Right Certificate.)

To: ELI LILLY AND COMPANY

The undersigned hereby irrevocably elects to exercise _____ Rights represented by this Right Certificate to purchase the Preferred Shares issuable upon the exercise of such Rights and requests that certificates for such Preferred Shares be issued in the name of:

Please insert social security
or other identifying number:_____

_____
(Please print name and address)

_____

If such number of Rights shall not be all the Rights evidenced by this Right Certificate, a new Right Certificate for the balance remaining of such Rights shall be registered in the name of and delivered to:

Please insert social security
or other identifying number:_____

_____
(Please print name and address)

_____

Dated:_____

Signature_____

Signature Guaranteed:

Signatures must be guaranteed by a member firm of a registered national securities exchange, a member of the National Association of Securities Dealers, Inc., or a commercial bank or trust company having an office or correspondent in the United States.

Certificate

The undersigned hereby certifies that the Rights evidenced by this Right Certificate are not beneficially owned by an Acquiring Person or an Affiliate or Associate thereof (as defined in the Rights Agreement). After due inquiry and to the best knowledge of the undersigned, the Rights evidenced by this Right Certificate were not acquired or beneficially owned by an Acquiring Person or an Affiliate or Associate thereof.

Dated:_____

Signature_____

The signature in the Form of Assignment or Form of Election to Purchase, as the case may be, must conform to the name as written upon the face of this Right Certificate in every particular, without alteration or enlargement or any change whatsoever.

In the event the certification set forth above in the Form of Assignment or the Form of Election to Purchase, as the case may be, is not completed, the Company and the Rights Agent will deem the beneficial owner of the Rights evidenced by this Right Certificate to be an Acquiring Person or an Affiliate or Associate thereof (as defined in the Rights Agreement) and such Assignment or Election to Purchase will not be honored.

SUMMARY OF RIGHTS TO PURCHASE PREFERRED SHARES

On July 20, 1998, the Board of Directors of Eli Lilly and Company (the "COMPANY") adopted a Shareholder Rights Plan (the "RIGHTS PLAN") to replace the expiring 1988 rights plan. The purpose of the Rights Plan is to deter certain coercive takeover tactics and enable the Board of Directors to represent effectively the interest of shareholders in the event of a takeover attempt. The Rights Plan does not deter negotiated mergers or business combinations that the Board of Directors determines to be in the best interests of the Company and its shareholders.

To implement the Rights Plan the Board of Directors declared a dividend of one preferred share purchase right (a "RIGHT") for each outstanding share of common stock (the "COMMON SHARES") of the Company. The dividend was paid on July 28, 1998 to the shareholders of record on that date. Each Right entitles the registered holder to purchase from the Company one one-thousandth of a share of Series B Junior Participating Preferred Stock of the Company, without par value (the "PREFERRED SHARES"), at a price of $325 per one one-thousandth of a Preferred Share, subject to adjustment. The description and terms of the Rights are set forth in a Rights Agreement (the "RIGHTS AGREEMENT") between the Company and First Chicago Trust Company of New York, as Rights Agent.

RIGHTS ATTACH TO COMMON SHARES INITIALLY

Initially and until a Distribution Date (as defined below) occurs, the Rights are attached to all Common Shares and no separate Rights certificates will be issued. During this initial period,

- the Rights are not exercisable;
- the Rights are transferred with the Common Shares and are not transferable separately from the Common Shares;
- new Common Share certificates or book entry shares issued will contain a notation incorporating the Rights Agreement by reference; and
- the transfer of any Common Shares will also constitute the transfer of the Rights associated with those Common Shares.

DISTRIBUTION OF RIGHTS

Separate certificates evidencing the Rights will be mailed to holders of record of the Common Shares on the "DISTRIBUTION DATE." The Distribution Date is the earlier to occur of the following two events (or such later date as may be determined by the Board of Directors, upon approval by a majority of Continuing Directors as defined below):

- the tenth day after a public announcement that a person or group of affiliated or associated persons has acquired 15% or more of the outstanding Common Shares (thereby becoming an "ACQUIRING PERSON" under the Rights Plan); or

- such date as may be determined by the Board of Directors of the Company, upon approval of a majority of the Continuing Directors after the commencement or announcement of a tender or exchange offer by a person or group for 15% or more of the outstanding Common Shares.

Acquisitions by the following persons will not result in the person becoming an Acquiring Person: The Company, any subsidiary or employee benefit plan of the Company, Lilly Endowment, Inc., or any other person approved in advance by the Board of Directors and the Continuing Directors.

After the Distribution Date, the Rights will be tradable separately from the Common Shares. After the Distribution Date and after the Company's right to redeem (as described below) has expired, the Rights will be exercisable in two different ways depending on the circumstances as set forth below.

RIGHT TO PURCHASE LILLY STOCK

If a person or group acquires 15% or more of the outstanding Common Shares (thereby becoming an Acquiring Person) and the Company's redemption right has expired, each holder of a Right (except those held by the Acquiring Person and its affiliates and associates) will have the right to purchase, upon exercise, Common Shares (or, in certain circumstances, Preferred Shares or other similar securities of the Company) having a value equal to two times the exercise price of the Right. In other words, the Rights holders other than the Acquiring Person may purchase Common Shares at a 50% discount.

For example, at the exercise price of $325 per Right, each Right not owned by an Acquiring Person would entitle its holder to purchase $650 worth of Common Shares (or other consideration, as noted above) for $325. Assuming a value of $65 per Common Share at such time, the holder of each valid Right would be entitled to purchase ten Common Shares for $325.

RIGHT TO PURCHASE ACQUIRING PERSON STOCK

Alternatively, if, in a transaction not approved by the Board of Directors and the Continuing Directors, the Company is acquired in a merger or other business combination or 50% or more of its assets or earning power are sold after a person or group has become an Acquiring Person, and the Company's redemption right has expired, proper provision will be made so that each holder of a Right will thereafter have the right to purchase, upon exercise, that number of shares of common stock of the acquiring company as have a market value of two times the exercise price of the Right. In other words, a Rights holder may purchase the acquiring company's common stock at a 50% discount.

EXCHANGE OF LILLY STOCK FOR RIGHTS

At any time after any person or group becomes an Acquiring Person and before the Acquiring Person acquires 50% or more of the outstanding Common Shares, the Board of Directors may exchange the Rights (other than Rights owned by the Acquiring Person which will have become void), in whole or in part, at an exchange ratio of one Common Share, or one one-thousandth of a Preferred Share (or of a share of a class or series of the Company's preferred stock having equivalent rights, preferences and privileges), per Right (subject to adjustment).

REDEMPTION

The Rights are redeemable by the Company in whole but not in part at a price of $.005 per Right at any time up to and including the tenth day after the time that a person or a group has become an Acquiring Person, subject to extension of this redemption period by the Board of Directors. Immediately upon redemption the right to exercise will terminate and the only right of holders will be to receive the redemption price.

EXPIRATION OF RIGHTS

The Rights will expire on July 28, 2008 unless the expiration date is extended by amendment as described below or unless the Rights are earlier redeemed or exchanged by the Company as described above.

AMENDMENTS

As long as the Rights are redeemable, the terms of the Rights may be amended by the Board of Directors (upon the approval of a majority of the Continuing Directors) in its discretion without the consent of the Rights holders. After that time, no amendment may adversely affect the interests of the Rights holders (other than the Acquiring Person).

MISCELLANEOUS

"CONTINUING DIRECTOR" means a member of the Board of Directors, who is not an Acquiring Person or a representative or nominee of an Acquiring Person, and who either (i) was a member of the Board of Directors on the date of the Rights Agreement or (ii) thereafter became a member of the Board of Directors, and whose nomination for election or election to the Board of Directors was recommended or approved by a majority of the Continuing Directors then on the Board of Directors.

The number of outstanding Rights and the number of one one-thousandths of a Preferred Share issuable upon exercise of each Right are subject to adjustment under certain circumstances.

Because of the nature of the Preferred Shares' dividend, liquidation and voting rights, the value of the one one-thousandth interest in a Preferred Share that may be purchased upon exercise of each Right should approximate the value of one Common Share.

Until a Right is exercised, a Rights holder, as such, will have no rights as a stockholder of the Company, including, without limitation, the right to vote or to receive dividends.

A copy of the Rights Agreement has been filed with the Securities and Exchange Commission as an Exhibit to a Registration Statement on Form 8-A dated ___ __, 1998. A copy of the Rights Agreement is available to Rights holders free of charge upon request to the Corporate Secretary of the Company.

This summary description of the Rights does not purport to be complete and is qualified in its entirety by reference to the Rights Agreement, which is hereby incorporated herein by reference.

EXHIBIT 10.6

THE LILLY DEFERRED COMPENSATION PLAN

(As Amended and Restated as of January 1, 2004)

SECTION 1. ESTABLISHMENT OF THE PLAN.

There is hereby established for the benefit of Participants an unfunded plan of voluntarily deferred compensation known as "The Lilly Deferred Compensation Plan."

SECTION 2. DEFINITIONS.

When used in the Plan, the following terms shall have the definitions set forth in this Section 2:

2.1. Base Salary. The term "Base Salary" means the base salary to which a management employee is entitled for services rendered to the Company as a management employee.

2.2. Base Salary Year. The term "Base Salary Year" means each calendar year in which Base Salary deferred under the Plan is earned by a Participant.

2.3. Beneficiary. The term "Beneficiary" means the beneficiary or beneficiaries (including any contingent beneficiary or beneficiaries) designated pursuant to subsection 6.2 hereof.

2.4. Board of Directors. The term "Board of Directors" means the Board of Directors of Eli Lilly and Company.

2.5. Bonus. The term "Bonus" means the payment to which an Eligible Employee is entitled pursuant to the Contingent Compensation Plan,the Senior Executive Bonus Plan or the Lilly Executive Bonus Plan (the EVA Bonus Plan) of the Company or any other similar compensation plan as may from time to time be designated by the Committee.

2.6. Bonus Year. The term "Bonus Year" means each calendar year in which a Bonus deferred under the Plan is earned by a Participant.

2.7. Committee. The term "Committee" means the committee designated in subsection 9.1 hereof to administer the Plan.

2.8. Company. The term "Company" means Eli Lilly and Company and its affiliates and subsidiaries.

2.9. Company Credit. The term "Company Credit" means an amount computed and credited each calendar year or part thereof to Participants' accounts as described in Section 5 at a rate that is equal to one hundred twenty percent (120%) of the applicable federal long-term rate, with compounding (as prescribed under Section 1274(d) of the Internal Revenue Code) that was in effect for the month of December immediately preceding the calendar year.

2.10. Disability. The term "Disability" means a condition that the Committee determines (i) is attributable to sickness, injury, or disease and (ii) renders a Participant incapable of engaging in any activity for remuneration or profit commensurate with the Participant's education, experience, and training.

2.11. Eligible Employee. The term "Eligible Employee" means a management employee of the Company who is designated by the Committee as eligible to defer a Bonus earned in the following year.

2.12. Lilly. The term "Lilly" means Eli Lilly and Company.

2.13. Participant. The term "Participant" means an Eligible Employee who has elected to defer all or part of a Bonus pursuant to the Plan in accordance with Section 3.1 hereof or an SEC Executive Officer who has elected to defer all or part of Base Salary pursuant to the Plan in accordance with Section 3.2 hereof.

2.14. Plan. The term "Plan" means "The Lilly Deferred Compensation Plan" as set forth herein and as it may be amended from time to time.

2.15. Retirement. The term "Retirement" means the first day of the month next following the Participant's last day of work for the Company, but only if such first day of the month occurs on or after the first to occur of (i) the day on which the Participant attains age 65 or (ii) the day on which the Participant is eligible to commence receiving a monthly retirement benefit under a funded, defined benefit retirement plan maintained by the Company and covering the Participant.

2.16. SEC Executive Officers. The term "SEC Executive Officers" shall mean those officers and employees from time to time designated as Executive Officers for purposes of the proxy statement and Form 10-K.

SECTION 3. PARTICIPATION.

3.1. Bonuses. Prior to the beginning of each Bonus Year, the Committee shall select those Eligible Employees who may elect to defer Bonuses pursuant to the Plan. Upon selection by the Committee and before the beginning of the applicable Bonus Year, an Eligible Employee may defer the receipt of a Bonus pursuant to the Plan by filing a written election with the Committee, in a form satisfactory to the Committee, that

(i) defers payment of a designated amount (of One Thousand Dollars ($1,000) or more) or percentage of the Bonus, if any, to be earned in the Bonus Year, and

(ii) specifies the payment option selected by the Participant pursuant to subsection 6.1 hereof.

The amount deferred may not exceed the amount of the Bonus. Except as provided in subsections 6.1 and 6.3 hereof, any election made pursuant to this Section 3 (including any

election made pursuant to paragraphs (i) and (ii), above) with respect to a Bonus Year shall be irrevocable when made.

Selection of an Eligible Employee for deferral of a Bonus during one year does not confer upon the Eligible Employee a right to defer Bonuses for subsequent years. The Eligible Employees who shall be permitted to defer Bonuses pursuant to the Plan shall be selected annually by the Committee. If an Eligible Employee is also an SEC Executive Officer as of the beginning of the Bonus Year, the Eligible Employee may also defer the receipt of Base Salary as provided in Section 3.2.

3.2. Base Salary. Subject to the right of the Committee to limit deferrals described below, prior to the beginning of each Compensation Year, an SEC Executive Officer may defer the receipt of up to one hundred percent (100%) of Base Salary pursuant to the Plan by filing a written election with the Committee, in a form satisfactory to the Committee, that

(i) defers payment of a designated amount of One Thousand Dollars ($1,000) or more or a percentage of Base Salary, and

(ii) specifies the payment option selected by the Participation pursuant to subsection 6.1 hereof.

The amount deferred may not exceed the amount of Base Salary. Except as provided in subsections 6.1 and 6.3 hereof, any election made pursuant to this Section 3 (including any election made pursuant to paragraphs (i) and (ii), above) with respect to a Bonus Year shall be irrevocable when made and shall not be affected by the Participant's ceasing to be an SEC Executive Officer after the beginning of the Bonus Year.

The Committee reserves the right to limit the amount of Deferrals of Base Salary to assure that the Company has sufficient funds to cover taxes, benefit payments, and other necessary and appropriate deductions.

SECTION 4. INDIVIDUAL ACCOUNT.

The Treasurer of Lilly shall maintain an account in the name of each Participant. In the year following the Bonus Year or Base Salary Year, each Participant's account shall be credited, as of the first day of the month in which Bonuses or Base Salary are paid, with the amount that the Participant has elected to defer hereunder. Each Participant shall be given an annual statement, as of December 31 of each year, showing for each year (i) the amount of Bonuses or Base Salary deferred and (ii) the amount of the Company Credit to the Participant's account.

SECTION 5. ACCRUAL OF COMPANY CREDIT.

The Treasurer of Lilly shall determine the applicable annual rate of Company Credit on or before December 31 of each calendar year. This rate shall be effective for the following calendar year. The Company Credit shall accrue monthly, at one-twelfth of the applicable annual rate, on all amounts credited to the Participant's account, including the Company Credits for prior years. The Company Credit shall not accrue on any amount distributed to the Participant (or to the Participant's Beneficiary) during the month for which the accrual is determined, except where an amount is distributed to a Beneficiary in the month of the Participant's death. The Company Credit for each year shall be credited to each Participant's account as of December 31 of that year and shall be compounded annually.

SECTION 6. PAYMENT.

6.1. Payment Options. The Participant shall select a payment election from the payment options described below. A Participant may elect that his final payment election control over all prior payment elections. The payment option selected by a Participant shall provide for payment to the Participant of the amount credited to the Participant's account in

(i) a lump sum in January of the second calendar year following the calendar year in which the Participant's employment terminates by reason of Retirement or Disability; or

(ii) annual installments over a period of two to ten years commencing in January of the second calendar year following the calendar year in which the Participant's employment terminates by reason of Retirement or Disability;

provided, that in no event shall a lump sum be paid or installment payments begin under any payment option before the first January that begins after any Bonus that has been deferred under the payment option has been determined. The Company shall pay the aggregate amounts deferred, together with a proportionate part of the aggregate Company Credit accrued to the date (or dates) of payment, in the manner and on the date(s) specified by the Participant. If a payment option described in paragraph (i), above, has been elected, the amount of the lump sum shall be equal to the amount credited to the Participant's account as of the December 31 next preceding the date of the payment. If the payment option described in paragraph (ii), above, has been elected, the amount of each installment shall be equal to the amount credited to the Participant's account as of the December 31 next preceding the date of the installment payment divided by the number of installment payments that have not yet been made. If the Participant fails to elect a payment option, the amount credited to the Participant's account shall be distributed in a lump sum in accordance with the payment option described in paragraph (i), above. If the amount credited to the Participant's account is less than $25,000 at any time following the year in which the Participant's employment terminates by reason of Retirement of Disability, the Committee, in its sole discretion, may pay out the amount credited to the Participant's account in a lump sum.

6.2. Payment upon Death. Within a reasonable period of time following the death of a Participant, the balance in the Participant's account shall be paid in a lump sum to the Participant's Beneficiary. For purposes of this subsection 6.2, the balance in the Participant's account shall be determined as of the date of payment. A Participant may designate the Beneficiary, in writing, in a form acceptable to the Committee, and filed with the Committee

before the Participant's death. A Participant may, before the Participant's death, revoke a prior designation of Beneficiary and may also designate a new Beneficiary without the consent of the previously designated Beneficiary, provided that such revocation and new designation (if any) are in writing, in a form acceptable to the Committee, and filed with the Committee before the Participant's death. If the Participant does not designate a Beneficiary, or if no designated Beneficiary survives the Participant, any amount not distributed to the Participant during the Participant's life shall be paid to the Participant's estate in a lump sum in accordance with this subsection 6.2.

6.3. Resignation or Dismissal. Within a reasonable time following termination of a Participant's employment by resignation or dismissal, the balance in the Participant's account shall be paid in a lump sum to the Participant. For purposes of this subsection 6.3, the balance in the Participant's account shall be determined as of a date determined by the Cormittee in its sole discretion.

6.4. Payment on Unforeseeable Emergency. The Administrator may, in its sole discretion, direct payment to a Participant of all or of any portion of the Participant's Account balance, notwithstanding an election under Section 6.1. above, at any time that it determines that such Participant has an unforeseeable emergency and then only to the extent reasonably necessary to meet the emergency. For purposes of this rule, "unforeseeable emergency" means severe financial hardship to the Participant resulting from a sudden and unexpected illness or accident of the Participant or of a dependent of the Participant, loss of the Participant's property due to casualty, or other similar extraordinary and unforeseeable circumstances arising as a result of events beyond the control of the Participant. The circumstances that will constitute an unforeseeable emergency will depend upon the facts of each case, but, in any case, payment may not be made to the extent that such hardship is or may be relieved --

(i) Through reimbursement or compensation by insurance or otherwise,

(ii) By liquidation of the Participant's assets, to the extent the liquidation of such assets would not itself cause severe financial hardship, or

(iii) By cessation of deferrals under the Plan.

Examples of what are not considered to be unforeseeable emergencies include the need to send a Participant's child to college or the desire to purchase a home.

6.5. Cash Payments. All payments under the Plan shall be made in cash.

SECTION 7. PROHIBITION AGAINST TRANSFER.

The right of a Participant to receive payments under the Plan may not be transferred except by will or applicable laws of descent and distribution. A Participant may not assign, sell, pledge, or otherwise transfer any amount to which he is entitled hereunder prior to transfer or payment thereof to the Participant.

SECTION 8. PARTICIPANT'S RIGHTS UNSECURED.

The Plan is unfunded. The right of any Participant to receive payments under the Plan shall be an unsecured claim against the general assets of the Company.

SECTION 9. ADMINISTRATION.

9.1. Committee. The Plan shall be administered by the Compensation and Management Development Committee of the Board of Directors,the members of which shall be selected by the Board of Directors from among its members. No member of the Committee may be a salaried employee of the Company.

9.2. Powers of the Committee. The Committee's powers shall include, but not be limited to, the power

(i) to select Eligible Employees for participation in the Plan,

(ii) to interpret the terms and provisions of the Plan and to determine any and all questions arising under the Plan, including, without limitation, the right to remedy possible ambiguities, inconsistencies, or omissions by a general rule or particular decision,

(iii) to adopt rules consistent with the Plan, and

(iv) to limit the deferrals of SEC Executive Officers to assure that the Company has sufficient funds to cover taxes, benefit payments, and other necessary or appropriate deductions.

9.3. Finality of Committee Determinations. Determinations by the Committee and any interpretation, rule, or decision adopted by the Committee under the Plan or in carrying out or administering the Plan shall be final and binding for all purposes and upon all interested persons, their heirs, and personal representatives.

9.4. Claims Procedures. Any person making a claim for benefits hereunder shall submit the claim in writing to the Committee. If the Committee denies the claim in whole or in part, it shall issue to the claimant a written notice explaining the reason for the denial and identifying any additional information or documentation that might enable the claimant to perfect the claim. The claimant may, within 60 days of receiving a written notice of denial, submit a written request for reconsideration to the Committee, together with a written explanation of the basis of the request. The Committee shall consider any such request and shall provide the claimant with a written decision together with a written explanation thereof. All interpretations, determinations, and decisions of the committee in respect of any claim shall be final and conclusive.

9.5. Withholding. The Company shall have the right to deduct from all payments hereunder any taxes required by law to be withheld from such payments. The recipients of such payments shall bear all taxes on amounts paid under the Plan to the extent that no taxes are withheld thereon, irrespective of whether withholding is required.

9.6. Incapacity. If the Committee determines that any person entitled to benefits under the Plan is unable to care for his or her affairs because of illness or accident, any payment due (unless a duly qualified guardian or other legal representative has been appointed) may be paid for the benefit of such person to such person's spouse, parent, brother, sister,or other party deemed by the Committee to have incurred expenses for such person.

9.7. Inability to Locate. If the Committee is unable to locate a person to whom a payment is due under the Plan for a period of twelve (12) months, commencing with the first day of the month as of which the payment becomes payable, the total amount payable to such person shall be forfeited.

9.8. Legal Holidays. If any day on (or on or before) which action under the Plan must be taken falls on a Saturday, Sunday,or legal holiday, such action may be taken on (or on or before) the next succeeding day that is not a Saturday, Sunday,or legal holiday; provided, that this subsection 9.8 shall not permit any action that must be taken in one calendar year to be taken in any subsequent calendar year.

SECTION 10. NO EMPLOYMENT RIGHTS.

No provision of the Plan or any action taken hereunder by the Company, the Board of Directors, or the Committee shall give any person any right to be retained in the employ of the Company, and the right and power of the Company to dismiss or discharge any Participant is specifically reserved.

SECTION 11. AMENDMENT, SUSPENSION, AND TERMINATION.

The Board of Directors shall have the right to amend, suspend, or terminate the Plan at any time. The Committee shall also have the right to amend the Plan, except for subsection 9.1 hereof and this Section 11.

SECTION 12. APPLICABLE LAW.

The Plan shall be governed by, and construed in accordance with, the laws of the State of Indiana, except to the extent that such laws are preempted by Federal law.

SECTION 13. EFFECTIVE DATE.

This amendment and restatement of the Plan is effective as of January 1, 2004. Nothing herein shall invalidate or adversely affect any previous election, designation, deferral, or accrual in accordance with the terms of the Plan that were then in effect.

EXHIBIT 10.7

THE LILLY DIRECTORS' DEFERRAL PLAN
(As amended and restated through January 1, 2004)

SECTION 1. ESTABLISHMENT OF THE PLAN AND SHARES AVAILABLE.

1.1. Establishment of Plan. This Plan was established effective January 1, 1996, to permit Directors of the Company who are not salaried employees of the Company to voluntarily defer receipt of some or all of their meeting fees and retainer and to share in the long-term growth of the Company by acquiring, on a deferred basis, an ownership interest in the Company. This amended and restated Plan is effective January 1, 2004.

1.2. Shares Available. Subject to adjustment as provided in Section 7.5, the aggregate number of shares of Eli Lilly and Company common stock that may be issued or transferred under this Plan after April 28, 2003, is 750,000. The shares may be authorized and unissued shares or treasury shares.

SECTION 2. DEFINITIONS.

The following terms shall have the definitions set forth in this Section 2:

2.1. Annual Allocation Date. The last Business Day in November of each calendar year, or such other annual date, not earlier than the third Monday in February, established by the Committee as the date as of which Shares are allocated to each Share Account in accordance with Section 6.

2.2. Beneficiary. The beneficiary or beneficiaries (including any contingent beneficiary or beneficiaries) designated pursuant to subsection 8.3 hereof.

2.3 Business Day. A day on which the Company's corporate headquarters are open for regular business.

2.4. Board of Directors. The Board of Directors of the Company.

2.5. Committee. The Directors and Corporate Governance Committee of the Board of Directors, or any successor committee of the Board of Directors that is charged with matters relating to the compensation of non-employee directors.

2.6. Company. Eli Lilly and Company.

2.7. Company Credit. For any calendar year or part thereof, an amount computed, and credited annually to a Participant's Deferred Compensation Account at an annual rate that is equal to one hundred twenty percent (120%) of the applicable federal long-term rate, with compounding (as prescribed under Section 1274(d) of the Internal Revenue Code) that was in effect for the month of December immediately preceding the calendar year.

2.8. Deferred Amount. The amount of a Monthly Deferral Participant's Monthly Compensation that the Participant elects to defer in accordance with Section 4 hereof.

2.9. Deferred Stock Participant. A Director who is not, and for the preceding 12 months has not been, a salaried employee of the Company and who becomes a Participant in the Plan in accordance with Section 3 hereof.

2.10. Director. A member of the Board of Directors.

2.11. Dividend Payment Date. The date as of which the Company pays a cash dividend on Shares.

2.12. Dividend Record Date. With respect to any Dividend Payment Date, the date established by the Board of Directors as the record date for determining shareholders entitled to the dividend.

2.13. Individual Accounts or Accounts. The separate accounts (the Deferred Compensation Account and the Share Account) described in Section 7 hereof. When used in the singular, the term shall refer to one of these two accounts, as the context requires.

2.14. Monthly Compensation. For any month, the monthly retainer and the aggregate of all meeting fees, committee fees and committee chairperson fees to which a Director is entitled for services rendered to the Company as a Director during the month, as established from time to time by resolution of the Board of Directors. For avoidance of doubt, Monthly Compensation does not include stock options granted to Directors or the Shares allocated pursuant to Section 6 of this Plan.

2.15. Monthly Deferral Participant. A Director who is not a salaried employee of the Company and who has elected to defer all or part of his or her Compensation pursuant to the Plan in accordance with Section 4 hereof.

2.16. Participant. A Director who is a Deferred Stock Participant, a Monthly Deferral Participant, or both.

2.17. Plan. The Lilly Directors' Deferral Plan, as set forth herein and as it may be amended from time to time.

2.18. Share. A share of common stock of the Company.

2.19. Valuation Date. For any month, the third Monday of the month, or if Shares are not traded on the New York Stock Exchange on such third Monday, the next day on which Shares are traded on the New York Stock Exchange.

SECTION 3. DEFERRED STOCK PARTICIPANTS.

Each Director who participated in The Lilly Non-Employee Directors' Deferred Stock Plan immediately before the effective date of this Plan shall continue as a Deferred Stock Participant on such effective date, and all elections in effect under The Lilly Non-Employee Directors' Deferred Stock Plan shall remain in effect under this Plan, unless and until amended in accordance with this Plan. Thereafter, each person who becomes a Director, and who is not, and for the preceding 12 months has not been, a salaried employee of the Company, shall become a Deferred Stock Participant.

SECTION 4. MONTHLY DEFERRAL PARTICIPANTS.

Each Director who participated in The Lilly Directors' Deferred Compensation Plan immediately before the effective date of the Plan shall continue as a Monthly Deferral Participant on such effective date, and all elections in effect under The Lilly Directors' Deferred Compensation Plan shall remain in effect under this Plan, unless and until amended in accordance with this Plan. Prior to the beginning of each calendar year, any Director who is not a salaried employee of the Company may defer the receipt of Monthly Compensation to be earned by the Director during such year by filing with the Company a written election that:

(i) defers payment of a designated amount (of one Thousand Dollars ($1,000) or more) or percentage of his or her Monthly Compensation for services attributable to the following calendar year or portion thereof (the "Deferred Amount");

(ii) specifies the payment option selected by the Participant pursuant to subsection 8.2 hereof for such Deferred Amount; and

(iii) specifies the option selected by the Participant pursuant to Section 5 hereof for such Deferred Amount.

The amount deferred may not exceed the Director's aggregate Monthly Compensation for the calendar year. Notwithstanding the foregoing, any individual who is newly elected or appointed to serve as a Director may, not later than thirty (30) days after his election or appointment becomes effective, elect in accordance with the preceding provisions of this Section 4, to defer the receipt of Monthly Compensation earned during the portion of the current calendar year that follows the filing of the election with the Company. Except as provided in subsections 8.2 and 8.4 hereof, any elections made pursuant to this Section 4 with respect to a calendar year shall be irrevocable when made. If a Participant fails to make an election under section 5 with respect to his or her Deferred Amount for a future calendar year, the Participant's previous election shall remain in effect, provided that the Participant may amend his or her election with regard to a future calendar year at any time.

SECTION 5. FORM OF DEFERRED COMPENSATION CREDITS.

5.1. Deferred Compensation Account. Except with respect to Deferred Amounts which a Monthly Deferral Participant elects to have credited in Shares in accordance with subsection 5.2 hereof, the Deferred Amount shall be denominated in U.S. dollars and credited to the Participant's Deferred Compensation Account pursuant to subsection 7.1 hereof.

5.2. Shares. Prior to the beginning of each calendar year, a Monthly Deferral Participant may elect to have all or a percentage of the Deferred Amount for the following calendar year credited in Shares and allocated to the Participant's Share Account pursuant to subsection 7.2 hereof.

SECTION 6. ANNUAL ALLOCATIONS TO SHARE ACCOUNTS.

6.1. Annual Allocation of Shares. As of the Annual Allocation Date of each calendar year, there shall be allocated to the Share Account (as described in Section 7.2 below) of each Deferred Stock Participant who is a Director on that date, as part of his or her compensation for service on the Board of Directors, seven hundred (700) Shares or such other number of Shares, not to exceed 3,000 shares, as may be specified from time to time by resolution of the Board of Directors.

SECTION 7. INDIVIDUAL ACCOUNTS.

The Company shall maintain Individual Accounts for Participants as follows:

7.1. Deferred Compensation Account. The Company shall maintain a Deferred Compensation Account in the name of each Monthly Deferral Participant who elects to defer the receipt of Monthly Compensation pursuant to Section 4 hereof for a calendar year and does not elect to have the Deferred Amount for such calendar year credited in Shares pursuant to subsection 5.2 hereof. The Deferred Compensation Account shall be denominated in U.S. dollars, rounded to the nearest whole cent. For each month, Deferred Amounts allocated to a Deferred Compensation Account pursuant to subsection 5.1 hereof shall be credited to the Deferred Compensation Account as of the last Business Day of the month.

7.2. Share Account. The Company shall maintain a Share Account for each Deferred Stock Participant and for each Monthly Deferral Participant who elects to have a Deferred Amount credited in Shares pursuant to subsection 5.2 hereof. The Share Account shall be denominated in Shares and maintained in fractions rounded to three (3) decimal places. Shares allocated to each Share Account shall be hypothetical and not issued or transferred by the Company until payment is made pursuant to Section 8 hereof.

For each month, Deferred Amounts allocated to a Share Account pursuant to subsection 5.2 hereof shall be credited to the Share Account as of the last Business Day of the month. Shares and, if necessary, fractional Shares, shall be credited based upon the average of the high and low price of Shares on the New York Stock Exchange on the Valuation Date for that month.

7.3. Accrual of Company Credit. The Treasurer of the Company shall determine the annual rate of Company Credit on or before December 31 of each calendar year. This rate shall be effective for the following calendar year. The Company Credit shall accrue monthly, at one-twelfth of the applicable annual rate, on all amounts credited to a Participant's Deferred Compensation Account, including the Company Credits for prior years. The Company Credit shall not accrue on any amount distributed to a Participant (or to the Participant's Beneficiary) during the month for which the accrual is determined, except where an amount is distributed to a Beneficiary in the month of the Participant's death. The Company Credit for each year shall be credited to each Deferred Compensation Account as of December 31 of that year and shall be compounded monthly.

7.4. Cash Dividends. Cash dividends paid on Shares shall be deemed to have been paid on the Shares allocated to each Participant's Share Account as if the allocated Shares were actual Shares issued and outstanding on the Dividend Record Date. An amount equal to the amount of such dividends shall be credited in Shares to each Share Account as of the last Business Day of each month in which a Dividend Payment Date occurs, based upon the average of the high and low prices for Shares on the New York Stock Exchange on the Valuation Date for that month.

7.5. Capital Adjustments. The number of Shares referred to in Sections 1.2 and 6 hereof and the number of Shares allocated to each Share Account shall be adjusted by the Committee, as it deems appropriate in its discretion, in the event of any subdivision or combination of Shares or any stock dividend, stock split, reorganization, recapitalization, or consolidation or merger with Eli Lilly and Company as the surviving corporation, or if additional shares or new or different shares or other securities of the Company or any other issuer are distributed with respect to Shares through a spin-off or other extraordinary distribution.

7.6. Account Statements. Within a reasonable time following the end of each calendar year, the Company shall render an annual statement to each Participant. The annual statement shall report the number of Shares credited to the Participant's Share Account as of December 31 of that year and the dollar amount, if any, credited to the Participant's Deferred Compensation Account as of December 31 of that year.

SECTION 8. PAYMENT PROVISIONS.

8.1. Method of Payment. All payments to a Participant (or to a Participant's Beneficiary) with respect to the Participant's Deferred Compensation Account shall be paid in cash. Except as provided in Section 8.5, all payments to a Participant (or to a Participant's Beneficiary) with respect to the Participant's Share Account shall be paid in Shares, at which time the Shares shall be issued or transferred on the books of the Company. All Shares to be issued or transferred hereunder may be newly issued or treasury shares. Fractional Shares shall not be issued or transferred to a Participant, provided that in the case of a final payment under the Plan with respect to a Participant, any fraction remaining in the Participant's Share Account shall be rounded up to the next whole Share and that number of whole Shares shall be issued or transferred. If Shares are not traded on the New York Stock Exchange on any day on which a

payment of Shares is to be made under the Plan, then that payment shall be made on the next day on which Shares are traded on the New York Stock Exchange.

8.2. Payment Options. Prior to each calendar year, or within 30 days after becoming a Participant, the Participant shall select a payment election with respect to the payment of one or both of the Participant's Individual Accounts from the following payment elections:

(i) a lump sum in January of the calendar year immediately following the calendar year in which the Participant ceases to be a Director;

(ii) a lump sum in January of the second calendar year following the calendar year in which the Participant ceases to be a Director;

(iii) annual (or, in the case of the Deferred Compensation Account only, monthly) installments over a period of two to ten years commencing in January of the calendar year following the calendar year during which the Participant ceases to be a Director; or

(iv) annual (or in the case of the Deferred Compensation Account only, monthly) installments over a period of two to ten years commencing in January of the second calendar year following the calendar year in which the Participant ceases to be a director.

If a payment option described in paragraphs (i) or (ii), above, has been elected, the amount of the lump sum with respect to the Participant's Deferred Compensation Account shall be equal to the amount credited to the Participant's Deferred Compensation Account as of the December 31 immediately preceding the date of the payment, and the amount of the lump sum with respect to the Participant's Share Account shall be equal to the number of Shares credited to the Share Account as of the December 31 immediately preceding the date of payment. If a payment option described in paragraphs (iii) or (iv), above, has been elected, the amount of each installment with respect to the Participant's Deferred Compensation Account shall be equal to the amount credited to the Participant's Deferred Compensation Account as of the last day of the month immediately preceding the date of a monthly installment payment, or the December 31 immediately preceding the date of an annual installment payment, divided by the number of installment payments that have not yet been made. The amount of each installment with respect to the Participant's Share Account shall be equal to the number of Shares credited to the Participant's Share Account as of the December 31 immediately preceding the date of an annual installment payment, divided by the number of installment payments that have not yet been made.

A Participant may elect that his or her final payment election may control over all prior payment elections. If the Participant fails to elect a payment option, the amount credited to the Participant's Individual Account shall be distributed in a lump sum in accordance with the payment option described in paragraph (i) above. At the time of any scheduled payment, if the amount credited to a Participant's Deferred Compensation Account or the value of Shares credited to a Participant's Share Account is less than $25,000, the Committee, in its sole discretion, may pay out the Account in a lump sum.

8.3. Payment Upon Death. Within a reasonable period of time following the death of a Participant, the amount credited to the Participant's Deferred Compensation Account and the Shares credited to the Participant's Share Account shall be paid by the Company in a lump sum to the Participant's Beneficiary. For purposes of this subsection 8.3, the amount credited to the Participant's Deferred Compensation Account and the number of Shares credited to the Participant's Share Account shall be determined as of the later of the date of death or the last Business Day of the month prior to the month in which the payment occurs.

A Participant may designate the Beneficiary, in writing, in a form acceptable to the Committee before the Participant's death. A Participant may revoke a prior designation of Beneficiary and may also designate a new Beneficiary without the consent of the previously designated Beneficiary, provided that such revocation and new designation (if any) are in writing, in a form acceptable to the Committee, and filed with the Committee before the Participant's death. If the Participant does not designate a Beneficiary, or if no designated Beneficiary survives the Participant, any amount not distributed to the Participant during the Participant's life shall be paid to the Participant's estate in a lump sum in accordance with this subsection 8.3.

8.4. Payment on Unforeseeable Emergency. The Committee may, in its sole discretion, direct payment to a Participant of all or of any portion of the Participant's Individual Account balance, notwithstanding an election under subsection 8.2 above, at any time that it determines that such Participant has an unforeseeable emergency, and then only to the extent reasonably necessary to meet the emergency. For purposes of this section, "unforeseeable emergency" means severe financial hardship to the Participant resulting from a sudden and unexpected illness or accident of the Participant or of a dependent of the Participant, loss of the Participant's property due to casualty, or other similar extraordinary and unforeseeable circumstances arising as a result of events beyond the control of the Participant. The circumstances that will constitute an unforeseeable emergency will depend upon the facts of each case, but, in any case, payment may not be made to the extent that such hardship is, or may be, relieved --

(i) through reimbursement or compensation by insurance or otherwise;

(ii) by liquidation of the Participant's assets, to the extent the liquidation of such assets would not itself cause severe financial hardship; or

(iii) by cessation of deferrals under the Plan.

Examples of what are not considered to be unforeseeable emergencies include the need to send a Participant's child to college or the desire to purchase a home.

8.5. Payment of Cash in Lieu of Shares. If at any time the Committee shall determine that payment of Shares to a Participant (or a Participant's Beneficiary) or the ownership or subsequent disposition of such Shares by such Participant or Beneficiary may violate or conflict with any applicable law or regulation, the Committee may, in its discretion, pay all or a portion of the Participant's Share Account in cash. In this case, the amount of cash shall be determined with reference to the average of the high and low trading price for Shares on the December 31

next preceding the date of payment, or if Shares are not traded on that day, the next preceding trading day.

SECTION 9. OWNERSHIP OF SHARES.

A Participant shall have no rights as a shareholder of the Company with respect to any Shares until the Shares are issued or transferred to the Participant on the books of the Company.

SECTION 10. PROHIBITION AGAINST TRANSFER.

The right of a Participant to receive payments of Shares and cash under the Plan may not be transferred except by will or applicable laws of descent and distribution. A Participant may not assign, sell, pledge, or otherwise transfer Shares or cash to which he is entitled hereunder prior to transfer or payment thereof to the Participant, and any such attempted assignment, sale, pledge or transfer shall be void.

SECTION 11. GENERAL PROVISIONS.

11.1. Director's Rights Unsecured. The Plan is unfunded. The right of any Participant to receive payments of cash or Shares under the provisions of the Plan shall be an unsecured claim against the general assets of the Company.

11.2. Administration. Except as otherwise provided in the Plan, the Plan shall be administered by the Committee, which shall have the final authority to adopt rules and regulations for carrying out the Plan, and to interpret, construe, and implement the provisions of the Plan.

11.3. Legal Opinions. The Committee may consult with legal counsel, who may be counsel for the Company or other counsel, with respect to its obligations and duties under the Plan, or with respect to any action, proceeding, or any questions of law, and shall not be liable with respect to any action taken, or omitted, by it in good faith pursuant to the advice of such counsel.

11.4. Liability. Any decision made or action taken by the Board of Directors, the Committee, or any employee of the Company or any of its subsidiaries, arising out of or in connection with the construction, administration, interpretation, or effect of the Plan, shall be absolutely discretionary, and shall be conclusive and binding on all parties. Neither the Committee nor a member of the Board of Directors and no employee of the Company or any of its subsidiaries shall be liable for any act or action hereunder, whether of omission or commission, by any other member or employee or by any agent to whom duties in connection with the administration of the Plan have been delegated or, except in circumstances involving bad faith, for anything done or omitted to be done.

11.5. Withholding. The Company shall have the right to deduct from all payments hereunder any taxes required by law to be withheld from such payments. The recipients of such

payments shall bear all taxes on amounts paid under the Plan to the extent that no taxes are withheld thereon, irrespective of whether withholding is required.

11.6. Legal Holidays. If any day on which action under the Plan must be taken falls on a Saturday, Sunday, or legal holiday, such action may be taken on the next succeeding day that is not a Saturday, Sunday, or legal holiday; provided, that this subsection 11.8 shall not permit any action that must be taken in one calendar year to be taken in any subsequent calendar year.

11.7. Participant Who Becomes Employee. If a Participant becomes an employee of the Company but remains a Director, he or she will no longer be entitled to new deferrals under the Plan as a Deferred Stock Participant or Monthly Deferral Participant. However, the individual's Account balances will continue to be administered under the Plan (including eligibility for the Company Credit and Cash Dividends under Sections 7.3 and 7.4) until they are paid out in accordance with Section 8.

SECTION 12. TERM, AMENDMENT, SUSPENSION, AND TERMINATION.

The Plan shall remain in effect until terminated by the Board of Directors. The Board of Directors shall have the right at any time, and from time to time, to amend, suspend, or terminate the Plan, subject to the following:

(i) no amendment or termination shall reduce the number of Shares or the cash balance in an Individual Account;

(ii) the number of Shares allocated annually pursuant to Section 6 hereof may not be changed more frequently than every calendar year; and

(iii) to the extent required by New York Stock Exchange listing rules or applicable law, material amendments shall be submitted to the Company's shareholders for approval.

SECTION 13. APPLICABLE LAW.

The Plan shall be governed by, and construed in accordance with, the laws of the State of Indiana, except to the extent that such laws are preempted by Federal law.

SECTION 14. EFFECTIVE DATE.

The effective date of this Plan is January 1, 1996. Nothing herein shall invalidate or adversely affect any previous election, designation, deferral, or accrual in accordance with the terms of The Lilly Directors' Deferred Compensation Plan or The Lilly Non-Employee Directors' Deferred Stock Plan that were in effect prior to the effective date of this Plan.

EXHIBIT 12. STATEMENT RE: COMPUTATION OF RATIO OF EARNINGS FROM CONTINUING OPERATIONS TO FIXED CHARGES

Eli Lilly and Company and Subsidiaries
(Dollars in millions)

	Years Ended December 31,				
	2003	2002	2001	2000	1999
Consolidated pretax income from continuing operations	$ 3,261.7	$ 3,457.7	$ 3,506.9	$ 3,858.7	$ 3,245.4
Interest from continuing operations and other fixed charges	121.9	140.0	253.3	225.4	213.1
Less interest capitalized during the period from continuing operations	(60.9)	(60.3)	(61.5)	(43.1)	(29.3)
Earnings	$ 3,322.7	$ 3,537.4	$ 3,698.7	$ 4,041.0	$ 3,429.2
Fixed charges	$ 121.9	$ 140.0	$ 253.3	$ 225.4	$ 213.2
Ratio of earnings to fixed charges	27.3	25.3	14.6	17.9	16.1

EXHIBIT 13. ANNUAL REPORT TO SHAREHOLDERS FOR THE YEAR ENDED DECEMBER 31, 2003

REVIEW OF OPERATIONS

EXECUTIVE OVERVIEW

This section provides an overview of our financial results, product launches and late-stage product pipeline developments, progress in improving our manufacturing operations, expected acquisition of Applied Molecular Evolution, Inc. (AME), in 2004, and legislative-related activities affecting the pharmaceutical industry.

Financial Summary

Net income was $2.56 billion, or $2.37 per share, in 2003 and $2.71 billion, or $2.50 per share, in 2002, decreases of 5 percent. We achieved strong worldwide sales growth of 14 percent, to $12.58 billion; however, in order to position ourselves for sustained growth in an increasingly competitive environment, we chose to significantly increase our investments in a number of areas. To ensure the successful launches of our new products discussed below, we substantially increased our sales and marketing efforts. In addition, we made substantial investments in our manufacturing operations and research and development activities. These reinvestments into the business, together with lower net other income, negatively affected earnings in 2003. In addition, comparisons between 2003 and 2002 are influenced by the impact of the following items that are reflected in the operating results (see Notes 3 and 4 to the consolidated financial statements for additional information):

2003

- We streamlined our infrastructure in the first quarter of 2003, resulting in severance-related and other charges of $52.5 million (pretax), which decreased earnings per share by $.03 in that quarter.

- We recognized asset impairments, primarily relating to manufacturing assets in the U.S., totaling $114.6 million (pretax) in the first quarter and $28.3 million (pretax) in the fourth quarter, which decreased earnings per share by approximately $.07 and $.02 in the first and fourth quarters of 2003, respectively.

- Separately, we recognized asset impairments and other charges of $186.8 million (pretax) in the first quarter of 2003 related primarily to our common stock ownership and loan agreements with Isis Pharmaceuticals, Inc. (Isis), which decreased earnings per share by $.13 in the first quarter of 2003.

- In the fourth quarter of 2003, we recorded a gain of $65.0 million (pretax) related to the sale of patent rights to dapoxetine for development in the field of genitourinary disorders to PPD, Inc., which increased earnings per share by $.04 in that quarter.

2002

- In the third quarter of 2002, we recognized a charge of $84.0 million (pretax) for acquired in-process research and development related to a collaboration arrangement with Amylin Pharmaceuticals, Inc. (Amylin), to jointly develop and commercialize exenatide, a potential new treatment for type 2 diabetes, which decreased earnings per share by approximately $.05 in that quarter.

Recent Product Launches and Late-Stage Product Pipeline Developments

Our long-term success depends, to a great extent, on our ability to continue to discover and develop innovative pharmaceutical products and acquire or collaborate on compounds currently in development by other biotechnology or pharmaceutical companies. We have achieved a number of successes with recent product launches and late-stage pipeline developments, including:

- Strattera, the first treatment approved by the U.S. Food and Drug Administration (FDA) for attention-deficit hyperactivity disorder (ADHD) that is not a stimulant, was officially launched in January 2003. We completed the European submission for Strattera in the third quarter of 2003.

- Forteo, a treatment for osteoporosis in postmenopausal women and to increase bone mass in men with primary osteoporosis, was officially launched in December 2002. We received an approval in Europe during June of 2003.

- Cialis, a new treatment for male erectile dysfunction, was launched by us and ICOS Corporation (ICOS) in several key international markets during 2003 and launched in the U.S. in early December 2003.

- Symbyax was launched in January 2004. Symbyax, a combination of olanzapine (the active ingredient in Zyprexa) and fluoxetine (the active ingredient in Prozac) is the first FDA-approved medication for bipolar depression, a notoriously difficult-to-treat condition that afflicts millions of Americans.

- Alimta, a treatment for malignant pleural mesothelioma, was approved by the FDA in February 2004. In addition, we have submitted Alimta for approval for second-line non-small-cell lung cancer (NSCLC) in the U.S. and malignant pleural mesothelioma and second-line NSCLC in Europe.

- Cymbalta, a treatment for depression, received an approvable letter from the FDA in the fall of 2003. The FDA recently indicated that it does not currently believe a preapproval inspection for Cymbalta will be necessary. However, a preapproval inspection remains at the discretion of the FDA. We have submitted our complete response to the approvable letter and our best estimate for U.S. approval and launch is the summer of 2004.

- Duloxetine for the treatment of stress urinary incontinence received an approvable letter from the FDA in the fall of 2003. Final FDA approval is contingent upon successful completion of additional acute preclinical and clinical pharmacology, label negotiations, and preapproval inspection. We currently anticipate approval in Europe in 2004 and U.S. approval in late 2004 or the first half of 2005.

Graph: Nine Key Growth Products Accounted for 66 Percent of 2003 Sales.
(See data table on page 38)

Manufacturing Update

As a result of preapproval plant inspections for Zyprexa IntraMuscular and Forteo in early 2001, the FDA informed us of a number of observations and issued a warning letter regarding adherence to current Good Manufacturing Practices (cGMP) regulations. In response, we have been implementing comprehensive, companywide improvements in our manufacturing operations. In the fall of 2002, we provided the FDA with a comprehensive plan to upgrade our manufacturing and quality operations, particularly at our injectable and dry products facilities in Indianapolis.

In late October 2003, the FDA advised us that the agency now considers our injectable and dry products facilities in Indianapolis to have reached a level of cGMP compliance that will allow for FDA preapproval site inspections for products under review. No further regulatory action is expected at this time. In December 2003, a preapproval site inspection for Zyprexa IntraMuscular was successfully completed. Although the FDA assessment is an important milestone, we still have considerable work to do to reach our ultimate goal of building and sustaining world-class manufacturing, product and process development, and quality capabilities.

Acquisition of Applied Molecular Evolution, Inc.

In November 2003, we agreed to acquire AME in a cash and stock transaction for approximately $400 million, net of the cash acquired. We expect to close the merger in the first quarter of 2004. In addition to acquiring the rights to two compounds currently under development, we expect the acquisition of AME to create synergies that will accelerate our ability to discover and optimize biotherapeutic drugs for cancer, inflammatory diseases, and critical care, as well as diabetes and obesity, areas where proteins are of great therapeutic benefit. See Note 3 to the consolidated financial statements for additional information regarding the acquisition of AME.

Legislative-Related Activity and Litigation

In the United States, prescription drugs are subject to increasing pricing pressure at both the federal and state levels. In December 2003, President Bush signed into law the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (MMA), providing a prescription drug benefit under the Medicare program beginning in 2006. This is expected to put downward pressure on prescription drug prices. This pressure may be offset by volume increases, but the business impact of this legislation will not be known until implementation in 2006. While the MMA retains the authority of the Secretary of Health and Human Services to prohibit the importation of prescription drugs, several bills have been introduced that would remove that authority and allow for the immediate importation of products into the U.S. regardless of their safety or cost. Such legislation would likely have a negative effect on our U.S. sales.

As a result of the passage of the MMA, all the aged and many of the disabled Medicaid recipients will receive their benefits through the Medicare program in the future. This should relieve some state budget pressures but is unlikely to result in less pricing pressure at the state level. A number of states have begun to implement supplemental rebates and restricted formularies in their Medicaid programs. Several states are also attempting to extend discounted Medicaid prices to non-Medicaid patients. Additionally, over 25 states are considering proposals that would result in the importation of prescription drugs for state employees, state beneficiaries, and, in some cases, state citizens. As a result, we expect pressures on pharmaceutical pricing to continue.

International operations are also generally subject to extensive price and market regulations, and there are many proposals for additional cost-containment measures, including proposals that would directly or indirectly impose additional price controls or reduce the value of our intellectual property protection.

Certain generic manufacturers have challenged

our U.S. compound patent for Zyprexa and are seeking permission to market generic versions of Zyprexa prior to the patent expiration in 2011. We expect the trial regarding the defense of these patents, which began in January 2004, to conclude in the first quarter of 2004. A ruling from the trial court is expected in the second or third quarter of 2004 with appeals expected to follow. See the Legal and Environmental Matters section for further information.

Graph: Revenues (See data table on page 39)

OPERATING RESULTS—2003

Sales

Our worldwide sales for 2003 increased 14 percent, to $12.58 billion, due primarily to the strong performance of Zyprexa, a treatment for schizophrenia, acute bipolar mania, and bipolar maintenance; diabetes care products; Gemzar, an oncolytic product; and Evista, an osteoporosis treatment and prevention agent; and the sales related to the launches of Strattera, Cialis, and Forteo. Sales in the U.S. increased 10 percent, to $7.17 billion. Sales outside the U.S. increased 19 percent, to $5.41 billion. Worldwide sales reflected a volume increase of 7 percent with global selling prices contributing 2 percent and an increase due to favorable changes in exchange rates contributing 5 percent.

Zyprexa had worldwide sales of $4.28 billion in 2003, an increase of 16 percent. Sales in the U.S. increased 4 percent, to $2.64 billion. Continuing competitive pressures contributed to slower sales growth in the U.S. In September 2003, the FDA requested updated product labeling for all atypical antipsychotics that includes a warning statement about the risk of diabetes. The FDA's decision to implement class labeling reinforces our long-standing position that the risk for diabetes should be considered among patients with severe mental illness regardless of medication choice. In early 2004, the American Diabetes Association issued an opinion paper, which states that second-generation antipsychotics differ in their diabetes risk profiles. These findings are in direct conflict with the FDA's recent class labeling language. Despite an increasingly competitive environment, we believe the product, together with Symbyax, still has sales growth potential in the U.S. We expect U.S. sales to benefit from the recent approval of a bipolar maintenance indication and the anticipated near-term approval of Zyprexa IntraMuscular. Sales outside the U.S. increased 42 percent, to $1.64 billion. Excluding the impact of exchange rates, our sales outside the U.S. grew 26 percent. The strong international sales growth of Zyprexa was primarily driven by increased unit volume attributable to the bipolar mania indication and the ongoing conversion from typical to atypical antipsychotics and, to a lesser extent, the impact of exchange rates. Zyprexa recorded strong growth in several key markets, including several major European Union countries and in Japan. We expect continued strong overseas growth of the product in 2004. Zyprexa recently received U.S. and European approvals for bipolar maintenance. Zyprexa IntraMuscular has recently been launched in Australia, Canada, and Europe, and we currently expect U.S. approval in the first half of 2004.

Diabetes care products, composed primarily of Humulin, biosynthetic human insulin; Humalog, our insulin analog; and Actos, an oral agent for the treatment of type 2 diabetes, had aggregate worldwide revenues of $2.57 billion in 2003, an increase of 12 percent. Diabetes care revenues in the U.S. increased 10 percent, to $1.57 billion. Diabetes care revenues outside the U.S. increased 17 percent, to $1.00 billion. Humulin had worldwide sales of $1.06 billion, an increase of 6 percent. Humulin sales in the U.S. decreased 2 percent, to $507.5 million. Humulin sales outside the U.S. increased 13 percent, to $552.9 million. Humalog became a billion-dollar product in 2003 with worldwide sales of $1.02 billion, an increase of 22 percent. Humalog sales in the U.S. increased 25 percent, to $658.6 million. Humalog sales outside the U.S. increased 19 percent, to $362.7 million. In 2004, we expect our worldwide insulin franchise to have little or no growth primarily due to expected continued competitive pressure on prescription volume. Actos revenues, the majority of which represent service revenues from a copromotion agreement in the U.S. with Takeda Pharmaceuticals North America (Takeda), increased 10 percent in 2003, to $431.2 million. Actos is manufactured by Takeda Chemical Industries, Ltd., and sold in the U.S. by Takeda.

Gemzar became a billion-dollar product in 2003 with worldwide sales of $1.02 billion, an increase of 17 percent. Sales in the U.S. increased 8 percent, to $522.4 million. Sales outside the U.S. increased 27 percent, to $499.3 million. We recently submitted Gemzar in the U.S. for the treatment of late-stage metastatic breast cancer.

Evista had worldwide sales of $922.1 million in

2003, an increase of 12 percent. Sales in the U.S. increased 5 percent, to $655.5 million. The U.S. growth was negatively affected by the exit of patients from the osteoporosis prevention market. In early 2004, Evista received regulatory approval in Japan. Sales outside the U.S. increased 36 percent, to $266.6 million.

Prozac, an antidepressant; Prozac Weekly™; and Sarafem®, a prescription treatment for premenstrual dysphoric disorder, a severe form of premenstrual syndrome (collectively, fluoxetine products), had combined worldwide sales of $645.1 million, a decrease of 12 percent. Fluoxetine product sales decreased 12 percent, to 398.6 million, in the U.S. and decreased 13 percent, to 246.5 million, outside the U.S. The declines were due to continuing generic competition.

Anti-infectives had worldwide sales of $489.9 million in 2003, a decrease of 15 percent. Sales outside the U.S. decreased 19 percent, to $420.1 million. Lower worldwide sales of anti-infectives were primarily due to continuing generic competition.

In November 2002, the FDA approved Strattera for the treatment of attention-deficit hyperactivity disorder in children, adolescents, and adults. Strattera sales were $370.3 million for 2003. Recently, regulatory authorities approved Strattera for marketing in Australia, Argentina, and Mexico. We expect Strattera to be a significant contributor to our sales growth in 2004.

ReoPro, a cardiovascular agent, had worldwide sales of $364.4 million in 2003, a decrease of 5 percent. Sales in the U.S. decreased 19 percent, to $201.4 million, due to continuing competitive pressures, and sales outside the U.S. increased 20 percent, to $163.0 million.

Cialis was launched in 2003 in several markets outside the U.S. by Lilly and ICOS. Cialis was launched the U.S. in early December 2003. Cialis had total sales of $203.3 million in 2003. Of this total, $73.5 million represent sales in our exclusive territories and are reported in our net sales. The remaining Cialis sales relate to the joint-venture territories of Lilly ICOS LLC (North America and Europe) and are reported in the Lilly ICOS joint-venture income statement along with related expenses. We report our 50 percent share of the operating results of the joint venture in our net other income. In early 2004, Lilly ICOS began a direct-to-consumer advertising campaign in the U.S. We will continue to increase our direct-to-consumer advertising activities in print and on television.

Xigris, a treatment for severe sepsis, had worldwide sales of $160.4 million in 2003, an increase of 60 percent compared with 2002. Sales in the U.S. were $109.2 million in 2003, an increase of 22 percent compared with 2002. Sales outside the U.S. totaled $51.2 million in 2003.

Forteo was officially launched in December 2002 and we received an approval in Europe during June 2003. Forteo sales were $65.3 million in 2003. We have implemented a staged launch of Forteo in the U.S. During the first stage in 2003, we focused on approximately 8,000 doctors who specialize in the treatment of osteoporosis. We are currently expanding our selling efforts in the next stage of our launch to encompass an additional 15,000 primary care physicians who treat osteoporosis.

Animal health products had worldwide sales of $726.6 million in 2003, an increase of 5 percent. Sales in the U.S. increased 2 percent, to $309.8 million. Sales outside the U.S. increased 7 percent, to $416.8 million.

Payments to states under federally mandated Medicaid rebate and state pharmaceutical assistance programs reduced 2003 sales by $567.6 million compared with $438.2 million in 2002. The increase is primarily due to increased U.S. sales of Zyprexa and higher use of Zyprexa among Medicaid patients.

Gross Margin, Costs, and Expenses

The 2003 gross margin decreased to 78.7 percent of sales compared with 80.4 percent for 2002. This decrease was attributed primarily to increased costs associated with quality improvements and growth in capacity of our manufacturing operations and the impact of foreign exchange rates, offset partially by favorable changes in product mix due to growth in sales of higher margin products.

Graph: Gross Margin (see data table on page 39)

Operating expenses (the aggregate of research and development and marketing and administrative expenses) increased 15 percent in 2003. Investment in research and development increased 9 percent, to $2.35 billion, due to increased clinical-trial expenses, the impact of foreign exchange rates, and milestone payments to Amylin for successful Phase III studies of exenatide. Maintaining our strong commitment to innovation, we invested approximately 19 percent of our sales in research and development efforts in 2003. Marketing and administrative expenses increased 18 percent compared with 2002, attributable primarily to increased marketing expenses in support of the

new product launches, the preparation for anticipated launches, and the impact of foreign exchange rates.

Graph: Research and Development (see data table on page 39)

Net other income for 2003 was $203.1 million, a decrease of $90.6 million. The decrease was primarily due to lower interest and miscellaneous income. We report our 50 percent share of the operating results of the Lilly ICOS joint venture in our net other income. For 2003, our net loss from the joint venture was $52.4 million, compared with $37.8 million in 2002.

The effective tax rate for 2003 was 21.5 percent compared with 21.7 percent for 2002. See Note 11 to the consolidated financial statements for additional information.

OPERATING RESULTS—2002

Financial Summary

Net income was $2.71 billion, or $2.50 per share, in 2002 and $2.78 billion, or $2.55 per share, in 2001, a decline of 3 percent and 2 percent, respectively. Comparisons between 2002 and 2001 are influenced by the impact of the 2002 items discussed in the Executive Overview and the items discussed immediately below that are reflected in our operating results. In addition to the impact of those items, net income and earnings per share for 2002 declined primarily due to the result of lower sales of Prozac partially offset by sales growth of several key products, lower interest expense, and lower operating expenses. Earnings per share for 2002 benefited slightly from a lower number of shares outstanding, resulting from our share repurchase program.

Certain items, reflected in our operating results for 2002 and 2001, should be considered in comparing the two years. The significant charge for 2002 is summarized in the Executive Overview. The 2001 items are summarized as follows (see Notes 3, 4, and 6 to the consolidated financial statements for additional information).

2001

- In the third and fourth quarters of 2001, we recognized charges of $190.5 million (pretax) for acquired in-process research and development related to collaboration arrangements with Isis Pharmaceuticals, Inc. (Isis); 3M Company; and Bioprojet, Société Civile de Recherche (Bioprojet), which decreased earnings per share by approximately $.05 in the third quarter and $.06 in the fourth quarter of 2001.

- We recognized charges of $121.4 million (pretax) associated with asset impairment and other site charges in the third quarter of 2001 due to actions taken as a result of the assessment of our worldwide manufacturing capacity, which decreased earnings per share by approximately $.07.

- We recognized a charge of $45.2 million (pretax) from the repurchase of higher interest rate debt in the third and fourth quarters of 2001, which decreased earnings per share by approximately $.02 in the third quarter and $.01 in the fourth quarter of 2001.

Sales

Our worldwide sales for 2002 decreased 4 percent, to $11.08 billion, due primarily to the decline in sales of Prozac in the U.S. resulting from the loss of patent protection in August 2001. Partially offsetting this decline was sales growth of Zyprexa, diabetes care products, Gemzar, Evista, and Xigris. Sales in the U.S. decreased 11 percent, to $6.54 billion. Sales outside the U.S. increased 9 percent, to $4.54 billion. Excluding Prozac, our worldwide and U.S. sales increased 8 percent and 7 percent, respectively. Worldwide sales reflected a volume decline of 4 percent, while global selling prices and exchange rates remained essentially flat.

Zyprexa had worldwide sales of $3.69 billion in 2002, an increase of 20 percent. Sales in the U.S. increased 16 percent, to $2.53 billion. Sales outside the U.S. increased 27 percent, to $1.16 billion, benefiting, in part, from the launch of Zyprexa in Japan during the second quarter of 2001. In 2002, our European sales forces began promoting Zyprexa for use in treating manic episodes associated with bipolar disorder.

Diabetes care products had aggregate worldwide revenues of $2.29 billion in 2002, an increase of 8 percent. Diabetes care revenues in the U.S. increased 5 percent, to $1.43 billion. Diabetes care revenues outside the U.S. increased 12 percent, to $859.2 million. Humulin had worldwide sales of $1.00 billion, a decrease of 5 percent due to the continued shift by patients to Humalog and Humalog mixture products and to increased competition. Humulin sales in the U.S. decreased 11 percent, to $515.4 million. Humulin sales outside the U.S. increased 1 percent, to $488.6 million. Humalog had worldwide sales of $834.2 million, an increase of 33 percent. Humalog sales in the U.S.

CONSOLIDATED STATEMENTS OF INCOME

Eli Lilly and Company and Subsidiaries (Dollars in millions, except per-share data) Year Ended December 31	2003	2002	2001
Net sales	**$12,582.5**	$11,077.5	$11,542.5
Cost of sales	**2,675.1**	2,176.5	2,160.2
Research and development	**2,350.2**	2,149.3	2,235.1
Marketing and administrative	**4,055.4**	3,424.0	3,417.4
Acquired in-process research and development (Note 3)	**—**	84.0	190.5
Asset impairments, restructuring, and other special charges (Note 4)	**382.2**	—	121.4
Interest expense	**61.0**	79.7	191.7
Other income—net	**(203.1)**	(293.7)	(280.7)
	9,320.8	7,619.8	8,035.6
Income before income taxes	**3,261.7**	3,457.7	3,506.9
Income taxes (Note 11)	**700.9**	749.8	726.9
Net income	**$ 2,560.8**	$ 2,707.9	$ 2,780.0
Earnings per share—basic (Note 10)	**$ 2.38**	$ 2.51	$ 2.58
Earnings per share—diluted (Note 10)	**$ 2.37**	$ 2.50	$ 2.55

See notes to consolidated financial statements.

increased 34 percent, to $528.3 million. Humalog sales outside the U.S. increased 31 percent, to $305.9 million. We received service revenues of $391.7 million in 2002, an increase of 9 percent, related to sales of Actos.

Gemzar had worldwide sales of $874.6 million in 2002, an increase of 21 percent, driven primarily by strong underlying product demand. Sales in the U.S. increased 16 percent, to $482.1 million. Sales outside the U.S. increased 28 percent, to $392.5 million.

Evista had worldwide sales of $821.9 million in 2002, an increase of 24 percent. Sales in the U.S. increased 19 percent, to $626.1 million. Sales outside the U.S. increased 41 percent, to $195.8 million. Sales benefited from strong underlying product demand driven, in part, by competitive developments in the second half of 2002.

Fluoxetine products had combined worldwide sales of $733.7 million, a decrease of 63 percent. Fluoxetine product sales in the U.S. decreased 73 percent, to $451.7 million, due to generic competition for Prozac beginning in early August 2001. Fluoxetine product sales outside the U.S. decreased 15 percent, to $282.0 million, primarily due to continuing generic competition.

Anti-infectives had worldwide sales of $577.4 million in 2002, a decrease of 23 percent. Sales of anti-infectives in the U.S. decreased 55 percent, to $58.5 million. Sales outside the U.S. decreased 16 percent, to $518.9 million. Lower sales of anti-infectives were due to continuing competitive pressures and to manufacturing and supply issues with respect to certain injectable antibiotics.

ReoPro had worldwide sales of $384.0 million in 2002, a decrease of 11 percent. Sales in the U.S. decreased 20 percent, to $248.3 million, due to continuing competitive pressures, and sales outside the U.S. increased 14 percent, to $135.7 million.

At the end of November 2001, we launched Xigris in the United States. In October 2002, we launched Xigris in a number of European countries. Worldwide Xigris sales were $100.2 million in 2002 compared with $21.2 million in 2001. Sales in the U.S. were $89.3 million in 2002.

Animal health products had worldwide sales of $693.1 million in 2002, an increase of 1 percent. Sales in the U.S. decreased 6 percent, to $304.2 million, due primarily to declines in our cattle and swine products. Sales outside the U.S. increased 7 percent, to $388.9 million.

Payments to states under federally mandated Medicaid rebate and state pharmaceutical assistance programs reduced 2002 sales by $438.2 million compared with $475.0 million in 2001.

Gross Margin, Costs, and Expenses

The 2002 gross margin decreased to 80.4 percent of sales compared with 81.3 percent for 2001. This decrease was attributed primarily to the decline in sales of Prozac, a higher margin product, and increased costs associated with cGMP improvements, costs associated with capacity increases for certain growth and new products, and higher inventory losses. These declines in gross margin were partially offset by favorable changes in product mix due to growth in sales of other higher margin products, such as Zyprexa, Gemzar, Evista, and diabetes care products, and favorable manufacturing throughput from increased volume of product manufactured.

Operating expenses decreased 1 percent in 2002. Research and development expenses decreased 4 percent, to $2.15 billion, due primarily to lower late-stage clinical-trial costs as more products were awaiting regulatory approval. Despite the decline, we invested approximately 19 percent of our sales in research and development efforts in 2002. Marketing and administrative expenses remained essentially flat compared with 2001 despite the continued expansion of our worldwide sales force and increased marketing efforts in support of our growth products and upcoming product launches. Operating expenses were also reduced due to lower incentive compensation expenses, reimbursement from collaboration partners, and cost containment, none of which were individually material.

During 2002, we expensed $84.0 million for acquired in-process research and development costs related to the exenatide collaboration arrangement with Amylin. Exenatide is in the development phase and no alternative future uses were identified.

Net other income for 2002 was $293.7 million, an increase of $13.0 million. The increase was primarily due to a combination of income recognized from upfront and milestone payments from Quintiles Transnational Corp. (Quintiles) as part of a Cymbalta commercialization agreement and income recognized from InterMune, Inc., related to out-licensing oritavancin in 2001, offset primarily by lower interest income due to lower interest rates.

Interest expense for 2002 decreased $112.0 million, to $79.7 million, primarily due to lower variable interest rates paid on our debt.

The effective tax rate for 2002 was 21.7 percent compared with 20.7 percent for 2001. See Note 11 to the consolidated financial statements for additional information.

CONSOLIDATED BALANCE SHEETS

Eli Lilly and Company and Subsidiaries (Dollars in millions) December 31	2003	2002
Assets		
Current Assets		
Cash and cash equivalents	**$ 2,756.3**	$ 1,945.9
Short-term investments	**957.0**	1,708.8
Accounts receivable, net of allowances of $79.5 (2003) and $66.4 (2002)	**1,854.7**	1,670.3
Other receivables	**477.6**	403.9
Inventories	**1,963.0**	1,495.4
Deferred income taxes (Note 11)	**500.6**	331.7
Prepaid expenses	**249.5**	248.1
Total current assets	**8,758.7**	7,804.1
Other Assets		
Prepaid pension (Note 12)	**1,613.3**	1,515.4
Investments (Note 5)	**3,374.6**	3,150.4
Sundry (Note 8)	**1,392.5**	1,279.1
	6,380.4	5,944.9
Property and Equipment	**6,539.0**	5,293.0
	$21,678.1	$19,042.0
Liabilities and Shareholders' Equity		
Current Liabilities		
Short-term borrowings (Note 6)	**$ 196.5**	$ 545.4
Accounts payable	**875.9**	676.9
Employee compensation	**387.4**	231.7
Dividends payable	**398.3**	375.8
Income taxes payable (Note 11)	**1,749.8**	1,761.9
Other liabilities (Note 8)	**1,942.7**	1,471.8
Total current liabilities	**5,550.6**	5,063.5
Other Liabilities		
Long-term debt (Note 6)	**4,687.8**	4,358.2
Other noncurrent liabilities (Note 8)	**1,674.9**	1,346.7
	6,362.7	5,704.9
Commitments and contingencies (Note 13)	**—**	—
Shareholders' Equity (Notes 7 and 9)		
Common stock–no par value		
Authorized shares: 3,200,000,000		
Issued shares: 1,124,677,097 (2003) and 1,123,451,408 (2002)	**702.3**	702.1
Additional paid-in capital	**2,610.0**	2,610.0
Retained earnings	**9,470.4**	8,500.1
Employee benefit trust	**(2,635.0)**	(2,635.0)
Deferred costs—ESOP	**(118.6)**	(123.3)
Accumulated other comprehensive loss (Note 14)	**(160.1)**	(670.8)
	9,869.0	8,383.1
Less cost of common stock in treasury		
2003—951,578 shares		
2002—1,008,292 shares	**104.2**	109.5
	9,764.8	8,273.6
	$21,678.1	$19,042.0

See notes to consolidated financial statements.

FINANCIAL CONDITION

As of December 31, 2003, cash, cash equivalents, and short-term investments totaled approximately $3.71 billion compared with $3.65 billion at December 31, 2002. The increase in cash, cash equivalents, and short-term investments was primarily due to cash generated from operations and net debt issuances, partially offset by capital expenditures, dividends paid, and share repurchases. We acquired approximately 3.0 million shares, for $276.8 million, during 2003 pursuant to our previously announced $3 billion share repurchase program. We have now completed $2.08 billion of purchases in connection with that program. We do not expect any significant share repurchases in 2004.

Our inventories increased by $467.6 million during 2003, to $1.96 billion, due primarily to exchange rate translation of overseas inventories to adjust for U.S. dollar weakness and to the buildup of inventory for new product launches and our growth products.

Graph: Capital Expenditures
(see data table on page 40)

Capital expenditures of $1.71 billion during 2003 were $575.7 million more than in 2002 as we continued to invest in manufacturing and research and development initiatives and related infrastructure. We expect near-term capital expenditures to increase from 2003 levels primarily to continue to prepare for the growth of our diabetes care products, future products, and increased research and development activities.

Total debt at December 31, 2003, was $4.88 billion, a decrease of $19.3 million from December 31, 2002. In 2003, we issued $830.0 million of long-term debt, repaid $540.0 million of long-term debt, and made net repayments of $247.3 million of short-term debt. The decrease in reported debt was caused by the decline in the SFAS 133 fair value adjustment discussed further in Note 6 to the consolidated financial statements. Our current debt ratings from Standard & Poor’s and Moody’s remain at AA and Aa3, respectively.

Graph: Dividends Paid Per Share
(see data table on page 40)

Dividends of $1.34 per share were paid in 2003, an increase of 8 percent from 2002. In the fourth quarter of 2003, effective for the first-quarter dividend in 2004, the quarterly dividend was increased to $.355 per share (a 6 percent increase), resulting in an indicated annual rate for 2004 of $1.42 per share. The year 2003 was the 119th consecutive year in which we made dividend payments and the 36th consecutive year in which dividends have been increased.

We believe that cash generated from operations, along with available cash and cash equivalents, will be sufficient to fund most of our operating needs, including debt service, capital expenditures, and dividends in 2004. We will likely issue additional debt in 2004 to fund remaining cash requirements. We believe that, if necessary, amounts available through our existing commercial paper program should be adequate to fund maturities of short-term borrowings. Our commercial paper program is also currently backed by $1.24 billion of unused committed bank credit facilities. Various risks and uncertainties, including those discussed in the Financial Expectations for 2004 section, may affect our operating results and cash generated from operations.

In the normal course of business, our operations are exposed to fluctuations in interest rates and currency values. These fluctuations can vary the costs of financing, investing, and operating. We address a portion of these risks through a controlled program of risk management that includes the use of derivative financial instruments. The objective of controlling these risks is to limit the impact on earnings of fluctuations in interest and currency exchange rates. All derivative activities are for purposes other than trading.

Our primary interest rate risk exposure results from changes in short-term U.S. dollar interest rates. In an effort to manage interest rate exposures, we strive to achieve an acceptable balance between fixed and floating rate debt positions and may enter into interest rate derivatives to help maintain that balance.

Based on our overall interest rate exposure at December 31, 2003 and 2002, including derivatives and other interest rate risk-sensitive instruments, a hypothetical 10 percent change in interest rates applied to the fair value of the instruments as of December 31, 2003 and 2002, respectively, would have no material impact on earnings, cash flows, or fair values of interest rate risk-sensitive instruments over a one-year period.

Our foreign currency risk exposure results from fluctuating currency exchange rates, primarily the U.S. dollar against the euro and the Japanese yen. We face transactional currency exposures that arise when we enter into transactions, generally on an intercompany basis, denominated in currencies other than the local currency. We also face currency exposure that arises from translating the results of our global operations to the U.S. dollar at exchange rates that have fluctuated from the beginning of the period. We use forward contracts and purchased options to manage our foreign currency exposures. Our policy outlines the minimum and maximum hedge coverage of such exposures. Gains and losses on these derivative positions offset, in part, the impact of currency fluctuations on the existing assets, liabilities, commitments, and anticipated revenues. Considering our derivative financial instruments outstanding at December 31, 2003 and 2002, a hypothetical 10 percent change in exchange rates (primarily against the U.S. dollar) as of December 31, 2003 and 2002, respectively, would have no material impact on earnings, cash flows, or fair values of foreign currency rate risk-sensitive instruments over a one-year period. These calculations do not reflect the impact of the exchange gains or losses on the underlying positions that would be offset, in part, by the results of the derivative instruments.

Graph: Return on Shareholders' Equity
(see data table on page 40)

Off-Balance Sheet Arrangements and Contractual Obligations

We have no off-balance sheet arrangements that have a material current effect or that are reasonably likely to have a material future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures, or capital resources. We do acquire assets still in development and enter into research and development arrangements with third parties that often require milestone and royalty payments to the third party contingent upon the occurrence of certain future events linked to the success of the asset in development. Milestone payments may be required contingent upon the successful achievement of an important point in the development life cycle of the pharmaceutical product (e.g., approval of the product for marketing by the appropriate regulatory agency). If required by the arrangement, we may have to make royalty payments based upon a percentage of the sales of the pharmaceutical product in the event that regulatory approval for marketing is obtained. Because of the contingent nature of these payments, they are not included in the table of contractual obligations below.

These arrangements are not material individually. However, if milestones for multiple products covered by these arrangements would happen to be reached in the same year, the aggregate charge to expense could be material to the results of operations in any one period. The risk inherent in pharmaceutical development makes it unlikely that this will occur as the failure rate for products in development is very high. In addition, these arrangements often give us the discretion to unilaterally make the decision to stop development of the product, which would allow us to avoid making the contingent payments; however, we are unlikely to cease development if the compound successfully achieves clinical testing objectives. We also note that, from a business perspective, we view these payments as positive because they signify that the product is successfully moving through development and is now generating or is more likely to generate cash flows from sales of products.

Our current noncancelable contractual obligations that will require future cash payments are as follows (in millions):

	Payments Due by Period				
	Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
Long-term debt, including interest payments[1]	$11,759.9	$ 367.6	$1,417.1	$ 894.8	$9,080.4
Capital lease obligations	174.7	26.3	39.8	28.8	79.8
Operating leases	339.5	82.5	122.6	90.2	44.2
Purchase obligations [2]	2,528.2	2,243.3	142.3	106.8	35.8
Other long-term liabilities reflected on our balance sheet under GAAP [3]	458.2	—	81.6	81.6	295.0
Other [4]	210.7	190.7	12.5	7.5	—
Total	$15,471.2	$2,910.4	$1,815.9	$1,209.7	$9,535.2

[1] Our long-term debt obligations include both our expected principal and interest obligations. The rate in effect at December 31, 2003, was used to compute the amount of the contractual obligation for the variable rate debt instruments.

[2] We have included the following:

- Purchase obligations, consisting primarily of all open purchase orders at our significant operating locations as of December 31, 2003. Some of these purchase orders may be cancelable; however, for purposes of this disclosure, we have not distinguished between cancelable and noncancelable purchase obligations.
- Contractual payment obligations with each of our significant vendors, which are noncancelable and are not contingent.

[3] We have included our long-term liabilities consisting primarily of our minimum pension funding requirements, nonqualified supplemental pension funding requirements, and deferred compensation liabilities.

[4] This category comprises primarily cash to be used in the AME acquisition and loan funding requirements to our collaboration partners. The acquisition of AME requires us to pay 20 percent of the purchase price as cash. The amount included in the other category represents an estimate of the purchase price that will be paid in cash. See Note 3 to the consolidated financial statements for additional information regarding the acquisition of AME.

The contractual obligations table above is current as of December 31, 2003. The amount of these obligations can be expected to change materially over time as new contracts are initiated and existing contracts are terminated or modified.

APPLICATION OF CRITICAL ACCOUNTING POLICIES

In preparing our financial statements in accordance with generally accepted accounting principles (GAAP), we must often make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses, and related disclosures. Some of those judgments can be subjective and complex, and consequently actual results could differ from those estimates. For any given individual estimate or assumption we make, there may also be other estimates or assumptions that are reasonable; however, we believe that, given current facts and circumstances, it is unlikely that applying any such other reasonable judgment would cause a material adverse effect on our consolidated results of operations, financial position, or liquidity for the periods presented in this report.

Our most critical accounting policies are described below. We have discussed the nature and the inherent judgment used in the application of our critical accounting policies with our audit committee.

Sales Rebate and Discount Accruals

Sales rebate and discount accruals are established in the same period as the related sales. The rebate/discount amounts are recorded as a deduction to arrive at our net sales and are included in other current liabilities. Sales rebates/discounts that require the use of judgment in the establishment of the accrual include Medicaid, managed care, long-term-care, hospital, and various other government programs. We base these accruals primarily upon our historical rebate/discount payments made to our customer segment groups. We calculate these rebates/discounts based upon a percent of our sales for each of our products as defined by the statutory rates

and the contracts with our various customer groups.

The largest of our sales rebate/discount amounts are rebates associated with sales covered by Medicaid. Although we generally accrue a liability for Medicaid rebates at the time we record the sale (when the product is shipped), the Medicaid rebate related to that sale is typically paid up to six months later. In determining the appropriate accrual amount, we consider our historical Medicaid rebate payments by product as a percent of our historical sales as well as any significant changes in sales trends, an evaluation of the current Medicaid rebate laws and interpretations, the percent of our products that are sold to Medicaid recipients, and our product pricing and current rebate/discount contracts.

We believe that the accruals we have established for sales rebates and discounts are reasonable and appropriate based on current facts and circumstances. However, it is possible that other people applying reasonable judgment to the same facts and circumstances could develop a different accrual amount for sales rebates and discounts. A 5 percent change in the Medicaid rebate expense we recognized in 2003 would lead to an approximate $28 million effect on our income before income taxes.

Product Litigation Liabilities and Other Contingencies

Product litigation liabilities and other contingencies are, by their nature, uncertain and are based upon complex judgments and probabilities. The factors we consider in developing our product litigation liability reserves and other contingent liability amounts include the merits and jurisdiction of the litigation, the nature and the number of other similar current and past litigation cases, the nature of the product and the current assessment of the science subject to the litigation, and the likelihood of settlement and current state of settlement discussions if any. In addition, we have accrued for certain product liability claims incurred, but not filed, to the extent we can formulate a reasonable estimate of their costs. We estimate these expenses based primarily on historical claims experience and data regarding product usage.

We also consider the insurance coverage we have to diminish the exposure. In assessing our insurance coverage, we consider the policy coverage limits and exclusions, the potential for denial of coverage by the insurance company, the financial position of the insurers, and the possibility of and the length of time for collection.

We believe that the accruals and related insurance recoveries we have established for product litigation liabilities and other contingencies are appropriate based on current facts and circumstances. However, it is possible that other people applying reasonable judgment to the same facts and circumstances could develop a different liability amount for product litigation liabilities and other contingencies or a different recovery amount from the insurance companies. A 5 percent change in the product litigation liabilities and other contingencies accrual would lead to an approximate $13 million effect on our income before income taxes; however, much of this effect would be expected to be offset by recoveries from our insurance coverages. A 5 percent change in the insurance recoveries estimate would lead to an approximate $4 million effect on our income before income taxes.

Pension and Retiree Medical Plan Assumptions

Pension benefit costs include assumptions for the discount rate, retirement age, and the expected return on plan assets. Retiree medical plan costs include assumptions for the discount rate, retirement age, the expected return on plan assets, and the health-care-cost trend rates. These assumptions have a significant effect on the amounts reported. In addition to the analysis below, see Note 12 to the consolidated financial statements for additional information regarding our retirement benefits.

Periodically, we evaluate the discount rate and the expected return on plan assets in our defined benefit pension and retiree health benefit plans. In evaluating these assumptions, we consider many factors, including an evaluation of the discount rates, expected return on plan assets and the health-care-cost trend rates of other companies; our historical assumptions compared with actual results; an analysis of current market conditions and asset allocations (approximately 85 to 95 percent of which are growth investments); and the views of leading financial advisers and economists. In evaluating our expected retirement age assumption, we consider the retirement ages of our past employees eligible for pension and medical benefits together with our expectations of future retirement ages.

We believe our pension and retiree medical plan assumptions are appropriate based upon the above factors. However, other people applying reasonable judgment to the same facts and circumstances could develop a different estimate of these factors. If the health-care-cost trend rates were to be increased by one percentage point each future year, the aggregate of the service cost and interest cost components of the 2003 annual expense would increase by approximately $15 million. A one-percentage-point decrease would decrease the aggregate of the 2003 service cost and interest cost by approximately $13 million. If the discount rate for 2003 were to be changed by a quarter percentage point, income before income taxes would change by approximately $17 million. If the expected return on plan assets for 2003 were to be changed by a quarter percentage point, income before income taxes would change by approximately $10 million. If our assumption regarding the expected age of future retirees for 2003 were adjusted by one year, that would affect our income before income taxes by approximately $24 million.

Valuation Allowances Recorded Against Deferred Tax Assets

We have recorded valuation allowances against certain of our deferred tax assets, primarily those that have been generated from net operating losses in certain taxing jurisdictions. In evaluating whether we would more likely than not recover these deferred tax assets, we have not assumed any future taxable income or tax planning strategies in the jurisdictions associated with these carryforwards. Implementation of tax planning strategies to recover these deferred tax assets or future income generation in these jurisdictions could lead to the reversal of these valuation allowances and a reduction of income tax expense.

We believe that our estimates for the valuation allowances reserved against the deferred tax assets are appropriate based on current facts and circumstances. However, other people applying reasonable judgment to the same facts and circumstances could develop a different estimate of these factors. A 5 percent change in the valuation allowance would result in a change in net income of approximately $21 million.

FINANCIAL EXPECTATIONS FOR 2004

For the first quarter and full year of 2004, we expect earnings per share to be in the range of $.65 to $.67 and $2.80 to $2.85, respectively. This earnings guidance excludes material unusual items and the substantial one-time charge we expect to report in the first quarter of 2004 for acquired in-process research and development related to the merger with AME, the amount of which has not been determined at this time. We are not currently aware of material unusual items that will occur in 2004. Further, this guidance reflects ongoing domestic competitive pressures on Zyprexa, which we will continue to monitor. It also includes the projected benefits for Zyprexa associated with the recently approved bipolar maintenance indication, as well as Symbyax and the anticipated near-term approval of Zyprexa IntraMuscular. For the full-year 2004, we expect low double-digit sales growth, gross margins as a percent of sales to be essentially flat compared with the prior year, marketing and administrative expenses to grow in the low double digits, and research and development expenses to grow in the mid-teens. Further, we expect that other income/deductions (net other income less interest expense) will be approximately $100 million to $120 million for 2004 and expect that the tax rate should remain essentially constant.

Actual results could differ materially and will depend on, among other things, the continuing growth of our currently marketed products; developments with competitive products; the timing and scope of regulatory approvals and the success of our new product launches; foreign exchange rates; possible regulatory actions; and the impact of state, federal, and foreign government pricing and reimbursement measures. In particular, as described below under Legal and Environmental Matters, certain generic pharmaceutical manufacturers have challenged our U.S. compound patent for Zyprexa. A trial court decision on the challenge is expected during 2004. If the decision is unfavorable and the generic companies launch generic olanzapine prior to resolution of appeals, our financial results would be very negatively affected. We undertake no duty to update these forward-looking statements.

LEGAL AND ENVIRONMENTAL MATTERS

Three generic pharmaceutical manufacturers, Zenith Goldline Pharmaceuticals, Inc. (Zenith), Dr. Reddy's Laboratories, Ltd. (Reddy), and Teva Pharmaceuticals, have submitted abbreviated new drug applications (ANDAs) seeking permission to market generic versions of Zyprexa in various dosage forms several years prior to the expiration of our U.S. patents for the product, alleging that our patents are invalid or not infringed. We filed suits against the three companies in U.S. District Court for the Southern District of Indiana seeking a ruling that the challenges to our compound patent (expiring in 2011) are without merit. The cases have been consolidated. A trial before a district court judge in Indianapolis began on January 26, 2004, and is expected to conclude in February. A ruling from the trial court is expected in the second or third quarter of 2004. Regardless of the trial court ruling, we anticipate that appeals will follow. If we are unsuccessful at the trial court level, we cannot predict whether any of the generic companies would launch generic versions of Zyprexa prior to a final resolution of any appeals. We believe that the generic manufacturers' claims are without merit and we expect to prevail in this litigation. However, it is not possible to predict or determine the outcome of this litigation and, accordingly, we can provide no assurance that we will prevail. An unfavorable outcome would have a material adverse impact on our consolidated results of operations, liquidity, and financial position.

In October 2002, we were notified that Barr Laboratories, Inc. (Barr), had submitted an ANDA to the U.S. FDA seeking permission to market a generic version of Evista several years prior to the expiration of our U.S. patents covering the product, alleging that the patents are invalid or not infringed. On November 26, 2002, we filed suit against Barr in federal district court in Indianapolis seeking a ruling that Barr's challenges to our patents claiming the method of use and pharmaceutical form (expiring from 2012 to 2017) are without merit. In June 2003, Barr added a challenge to one of our additional patents (expiring in 2017), claiming a

component in the pharmaceutical form of Evista. This patent has now been added to the lawsuit. The trial is tentatively scheduled to begin in August 2005. While we believe that Barr's claims are without merit and expect to prevail, it is not possible to predict or determine the outcome of the litigation. Therefore, we can provide no assurance that we will prevail. An unfavorable outcome could have a material adverse impact on our consolidated results of operations, liquidity, and financial position.

In July 2002, we received a grand jury subpoena for documents from the Office of Consumer Litigation, Department of Justice, related to our marketing and promotional practices and physician communications with respect to Evista. We received a second subpoena seeking additional documents in July 2003. We continue to cooperate with the government and have provided a broad range of information concerning our U.S. marketing and promotional practices, including documents relating to communications with physicians and the remuneration of physician consultants and advisers. We continue to review and enhance policies and procedures designed to assure that our marketing and promotional practices and physician communications comply with promotional laws and regulations. In recent months, several pharmaceutical companies have received subpoenas from government agencies with respect to a variety of products, including a number of neuroscience products. It is possible that other Lilly products, including Zyprexa, could become subject to investigation. It is possible that the outcome of the above matters could include criminal charges and fines and/or civil penalties. We cannot predict or determine the outcome of the above matters or reasonably estimate the amount or range of amounts of any fines or penalties that might result from an adverse outcome. It is possible, however, that an adverse outcome could have a material adverse impact on our consolidated financial position, liquidity, and results of operations.

We have been named as a defendant in numerous product liability lawsuits, involving primarily diethylstilbestrol (DES) and thimerosal. See Note 13 to the consolidated financial statements for further information on those matters.

Our worldwide operations are subject to complex and changing environmental and health and safety laws and regulations that will continue to require capital investment and operational expenses. We have also been designated a potentially responsible party with respect to fewer than 10 sites under the federal environmental law commonly known as Superfund. For more information on those matters, see Note 13 to the consolidated financial statements.

While it is not possible to predict or determine the outcome of the legal and environmental matters described above, we believe that, except as noted above in connection with the discussion of the Zyprexa patent litigation, the Evista patent litigation, and our marketing and promotional practices, the resolution of all such matters will not have a material adverse effect on our consolidated financial position or liquidity but could possibly be material to the consolidated results of operations in any one accounting period.

PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995—A CAUTION CONCERNING FORWARD-LOOKING STATEMENTS

Under the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, we caution investors that any forward-looking statements or projections made by us, including those made in this document, are based on management's expectations at the time they are made, but they are subject to risks and uncertainties that may cause actual results to differ materially from those projected. Economic, competitive, governmental, technological, legal, and other factors that may affect our operations and prospects are discussed above and in Exhibit 99 to our most recent report on Forms 10-Q and 10-K filed with the Securities and Exchange Commission.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Eli Lilly and Company and Subsidiaries
(Dollars in millions)

Year Ended December 31	2003	2002	2001
Cash Flows From Operating Activities			
Net income	**$ 2,560.8**	$ 2,707.9	$ 2,780.0
Adjustments To Reconcile Net Income to Cash Flows From Operating Activities			
Depreciation and amortization	**548.5**	493.0	454.9
Change in deferred taxes	**130.9**	346.5	273.8
Acquired in-process research and development, net of tax	**—**	54.6	123.8
Asset impairments, restructuring, and other special charges, net of tax	**261.7**	—	78.9
Other, net	**61.0**	10.8	27.6
	3,562.9	3,612.8	3,739.0
Changes in operating assets and liabilities			
Receivables—(increase) decrease	**(195.1)**	(321.1)	167.5
Inventories—increase	**(170.8)**	(285.1)	(184.2)
Other assets—increase	**(211.9)**	(667.4)	(81.1)
Accounts payable and other liabilities—increase (decrease)	**661.6**	(268.5)	20.4
	83.8	(1,542.1)	(77.4)
Net Cash Provided by Operating Activities	**3,646.7**	2,070.7	3,661.6
Cash Flows From Investing Activities			
Purchase of property and equipment	**(1,706.6)**	(1,130.9)	(884.0)
Disposals of property and equipment	**61.2**	36.8	31.6
Net change in short-term investments	**774.0**	(651.8)	(520.3)
Proceeds from sales and maturities of noncurrent investments	**6,762.4**	4,777.9	3,708.7
Purchase of noncurrent investments	**(7,005.3)**	(5,190.3)	(5,931.1)
Purchase of in-process research and development	**—**	(84.0)	(159.6)
Other, net	**(217.2)**	(232.1)	(210.1)
Net Cash Used in Investing Activities	**(1,331.5)**	(2,474.4)	(3,964.8)
Cash Flows From Financing Activities			
Dividends paid	**(1,443.0)**	(1,335.8)	(1,207.2)
Purchase of common stock and other capital transactions	**(281.1)**	(385.2)	(545.7)
Issuances of common stock under stock plans	**103.1**	64.6	109.5
Net change in short-term borrowings	**(247.3)**	(18.0)	102.0
Proceeds from issuance of long-term debt	**830.0**	1,259.6	901.3
Repayments of long-term debt	**(540.0)**	(7.2)	(408.6)
Net Cash Used for Financing Activities	**(1,578.3)**	(422.0)	(1,048.7)
Effect of exchange rate changes on cash	**73.5**	69.3	(60.7)
Net increase (decrease) in cash and cash equivalents	**810.4**	(756.4)	(1,412.6)
Cash and cash equivalents at beginning of year	**1,945.9**	2,702.3	4,114.9
Cash and cash equivalents at end of year	**$ 2,756.3**	$ 1,945.9	$ 2,702.3

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Eli Lilly and Company and Subsidiaries
(Dollars in millions)

Year Ended December 31	2003	2002	2001
Net income	**$2,560.8**	$2,707.9	$2,780.0
Other comprehensive income (loss)			
Foreign currency translation gains (losses)	**473.0**	273.6	(83.8)
Net unrealized gains (losses) on securities	**72.0**	(67.4)	47.7
Minimum pension liability adjustment	**(9.8)**	(4.6)	(95.6)
Effective portion of cash flow hedges	**(2.1)**	(217.9)	(42.0)
Other comprehensive income (loss) before income taxes	**533.1**	(16.3)	(173.7)
Provision for income taxes related to other comprehensive income (loss) items	**(22.4)**	93.9	36.5
Other comprehensive income (loss) (Note 14)	**510.7**	77.6	(137.2)
Comprehensive income	**$3,071.5**	$2,785.5	$2,642.8

See notes to consolidated financial statements.

SEGMENT INFORMATION

Eli Lilly and Company and Subsidiaries
(Dollars in millions)

We operate in one significant business segment—pharmaceutical products. Operations of the animal health business segment are not material and share many of the same economic and operating characteristics as pharmaceutical products. Therefore, they are included with pharmaceutical products for purposes of segment reporting.

Year Ended December 31	2003	2002	2001
Net sales–to unaffiliated customers			
Neurosciences	**$ 5,554.8**	$ 4,668.3	$ 5,328.2
Endocrinology	**3,926.7**	3,444.6	3,103.5
Oncology	**1,039.8**	893.1	739.1
Animal health	**726.6**	693.1	686.1
Cardiovascular	**669.3**	624.9	593.4
Anti-infectives	**489.9**	577.4	749.5
Other pharmaceutical	**175.4**	176.1	342.7
Net sales	**$12,582.5**	$11,077.5	$11,542.5
Geographic Information			
Net sales–to unaffiliated customers[1]			
United States	**$ 7,175.6**	$ 6,536.1	$ 7,364.3
Western Europe	**2,711.3**	2,155.4	1,953.1
Other foreign countries	**2,695.6**	2,386.0	2,225.1
	$12,582.5	$11,077.5	$11,542.5
Long-lived assets			
United States	**$ 5,296.0**	$ 4,725.1	$ 4,015.4
Western Europe	**1,279.1**	997.1	767.9
Other foreign countries	**1,209.2**	673.3	519.6
	$ 7,784.3	$ 6,395.5	$ 5,302.9

[1]Net sales are attributed to the countries based on the location of the customer.

The largest category of products is the neurosciences group, which includes Zyprexa, Prozac, Strattera, and Permax®. Endocrinology products consist primarily of Humulin, Humalog, Actos, Evista, Forteo, and Humatrope. Oncology products consist primarily of Gemzar. Animal health products include Tylan®, Rumensin®, Coban®, and other products for livestock and poultry. Cardiovascular products consist primarily of ReoPro and Xigris. Anti-infectives include primarily Ceclor® and Vancocin®. The other pharmaceutical product group includes Cialis, Axid®, and other miscellaneous pharmaceutical products and services.

Most of the pharmaceutical products are distributed through wholesalers that serve pharmacies, physicians and other health care professionals, and hospitals. In 2003, our three largest wholesalers each accounted for between 15 percent and 16 percent of consolidated net sales. Further, they each accounted for between 9 percent and 15 percent of accounts receivable as of December 31, 2003. Animal health products are sold primarily to wholesale distributors.

Our business segments are distinguished by the ultimate end user of the product: humans or animals. Performance is evaluated based on profit or loss from operations before income taxes. The accounting policies of the individual segments are substantially the same as those described in the summary of significant accounting policies in Note 1 to the consolidated financial statements. Income before taxes for the animal health business was approximately $204 million, $221 million, and $204 million in 2003, 2002, and 2001, respectively.

The assets of the animal health business are intermixed with those of the pharmaceutical products business and are not separately determinable. Long-lived assets disclosed above consist of property and equipment and certain sundry assets.

We are exposed to the risk of changes in social, political, and economic conditions inherent in foreign operations, and our results of operations and the value of our foreign assets are affected by fluctuations in foreign currency exchange rates.

SELECTED QUARTERLY DATA (UNAUDITED)

Eli Lilly and Company and Subsidiaries
(Dollars in millions, except per-share data)

2003	Fourth	Third	Second	First
Net sales	$3,465.5	$3,139.4	$3,088.2	$2,889.4
Cost of sales	731.5	679.3	643.0	621.3
Operating expenses	1,844.2	1,531.5	1,585.8	1,444.1
Asset impairments, restructuring, and other special charges	28.3	—	—	353.9
Other–net	(102.5)	12.7	(28.5)	(23.8)
Income before income taxes	964.0	915.9	887.9	493.9
Net income	747.2	714.4	692.2	407.0
Earnings per share–basic	.69	.66	.64	.38
Earnings per share–diluted	.69	.66	.64	.38
Dividends paid per share	.335	.335	.335	.335
Common stock closing prices				
High	73.89	70.33	69.83	67.98
Low	60.78	57.99	57.73	53.70

2002	Fourth	Third	Second	First
Net sales	$2,955.6	$2,785.6	$2,775.2	$2,561.1
Cost of sales	567.8	553.7	524.9	530.1
Operating expenses	1,495.1	1,337.4	1,460.7	1,280.1
Acquired in-process research and development	—	84.0	—	—
Other–net	(51.3)	(52.3)	(54.6)	(55.8)
Income before income taxes	944.0	862.8	844.2	806.7
Net income	736.3	683.9	658.5	629.2
Earnings per share–basic	.68	.64	.61	.58
Earnings per share–diluted	.68	.63	.61	.58
Dividends paid per share	.31	.31	.31	.31
Common stock closing prices				
High	69.00	61.84	78.34	80.28
Low	55.14	47.91	56.11	72.49

Our common stock is listed on the New York, London, and other stock exchanges.

SELECTED FINANCIAL DATA (UNAUDITED)

Eli Lilly and Company and Subsidiaries (Dollars in millions, except per-share data)	2003	2002	2001	2000	1999
Operations					
Net sales	**$ 12,582.5**	$ 11,077.5	$ 11,542.5	$ 10,862.2	$ 10,002.9
Research and development	**2,350.2**	2,149.3	2,235.1	2,018.5	1,783.6
Other costs and expenses	**6,970.6**	5,470.5	5,800.5	4,985.0	4,973.9
Income from continuing operations before taxes	**3,261.7**	3,457.7	3,506.9	3,858.7	3,245.4
Income taxes	**700.9**	749.8	726.9	800.9	698.7
Income from:					
Continuing operations	**2,560.8**	2,707.9	2,780.0	3,057.8	2,546.7
Discontinued operations	**—**	—	—	—	174.3
Net income	**2,560.8**	2,707.9	2,780.0	3,057.8	2,721.0
Income from continuing operations as a percent of sales	**20.4%**	24.4%	24.1%	28.2%	25.5%
Per-share data—diluted					
Income from:					
Continuing operations	**$ 2.37**	$ 2.50	$ 2.55	$ 2.79	$ 2.30
Discontinued operations	**—**	—	—	—	.16
Net income	**2.37**	2.50	2.55	2.79	2.46
Dividends declared per share	**1.36**	1.27	1.15	1.06	.95
Weighted-average number of shares outstanding–diluted (thousands)	**1,082,230**	1,085,088	1,090,793	1,097,725	1,106,055
Financial Position					
Current assets	**$ 8,758.7**	$ 7,804.1	$ 6,938.9	$ 7,943.0	$ 7,055.5
Current liabilities	**5,550.6**	5,063.5	5,203.0	4,960.7	3,935.4
Property and equipment—net	**6,539.0**	5,293.0	4,532.4	4,176.6	3,981.5
Total assets	**21,678.1**	19,042.0	16,434.1	14,690.8	12,825.2
Long-term debt	**4,687.8**	4,358.2	3,132.1	2,633.7	2,811.9
Shareholders' equity	**9,764.8**	8,273.6	7,104.0	6,046.9	5,013.0
Supplementary Data[1]					
Return on shareholders' equity	**28.4%**	35.2%	42.3%	55.3%	53.9%
Return on assets	**12.7%**	15.2%	17.8%	22.9%	21.3%
Capital expenditures	**$ 1,706.6**	$ 1,130.9	$ 884.0	$ 677.9	$ 528.3
Depreciation and amortization	**548.5**	493.0	454.9	435.8	439.7
Effective tax rate	**21.5%**	21.7%	20.7%	20.8%	21.5%
Number of employees	**46,100**	43,700	41,100	35,700	31,300
Number of shareholders of record	**54,600**	56,200	57,700	59,200	62,300

[1] All supplementary financial data have been computed using income from continuing operations except for capital expenditures and depreciation and amortization, which include amounts from discontinued operations. The number of employees reflects continuing operations, including controlled joint ventures.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Eli Lilly and Company and Subsidiaries
(Dollars in millions, except per-share data)

Note 1: Summary of Significant Accounting Policies

Basis of presentation: The accounts of all wholly owned and majority-owned subsidiaries are included in the consolidated financial statements. Where our ownership of consolidated subsidiaries is less than 100 percent, the outside shareholders' interests are reflected in other noncurrent liabilities. All intercompany balances and transactions have been eliminated.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses, and related disclosures at the date of the financial statements and during the reporting period. Actual results could differ from those estimates.

All per-share amounts, unless otherwise noted in the footnotes, are presented on a diluted basis, that is, based on the weighted-average number of outstanding common shares and the effect of all potentially dilutive common shares (primarily unexercised stock options).

Cash equivalents: We consider all highly liquid investments, generally with a maturity of three months or less, to be cash equivalents. The cost of these investments approximates fair value. If items meeting this definition are part of a larger investment pool, they are classified consistent with the classification of the pool.

Inventories: We state all inventories at the lower of cost or market. We use the last-in, first-out (LIFO) method for substantially all our inventories located in the continental United States, or approximately 40 percent of our total inventories. Other inventories are valued by the first-in, first-out (FIFO) method. FIFO cost approximates current replacement cost. Inventories at December 31 consisted of the following:

	2003	2002
Finished products	**$ 542.1**	$ 482.9
Work in process	**1,169.0**	816.3
Raw materials and supplies	**315.9**	242.7
	2,027.0	1,541.9
Reduction to LIFO cost	**(64.0)**	(46.5)
	$1,963.0	$1,495.4

Investments: Substantially all debt and marketable equity securities are classified as available-for-sale. Available-for-sale securities are carried at fair value with the unrealized gains and losses, net of tax, reported in other comprehensive income. Unrealized losses considered to be other-than-temporary are recognized in earnings currently. Factors we consider in making this evaluation include company-specific drivers of the decrease in stock price, status of projects in development, near-term prospects of the issuer, the length of time the value has been depressed, and the financial condition of the industry. Realized gains and losses on sales of available-for-sale securities are computed based upon specific identification of the initial cost adjusted for any other-than-temporary declines in fair value. Investments in companies over which we have significant influence but not a controlling interest are accounted for using the equity method with our share of earnings or losses reported in other income. We own no investments that are considered to be trading securities.

Derivative financial instruments: Our derivative activities are initiated within the guidelines of documented corporate risk-management policies and do not create additional risk because gains and losses on derivative contracts offset losses and gains on the assets, liabilities, and transactions being hedged. As derivative contracts are initiated, we designate the instruments individually as either a fair value hedge or a cash flow hedge. Management reviews the correlation and effectiveness of our derivatives on a quarterly basis.

For derivative contracts that are designated and qualify as fair value hedges, the derivative instrument is marked to market with gains and losses recognized currently in income to offset the respective losses and gains recognized on the underlying exposure. For derivative contracts that are designated and qualify as cash flow hedges, the effective portion of gains and losses on these contracts is reported as a component of other comprehensive income and reclassified into earnings in the same period the hedged transaction affects earnings. Hedge ineffectiveness is immediately recognized in earnings. Derivative contracts that are not designated as hedging instruments are recorded at fair value with the gain or loss recognized in current earnings during the period of change.

We enter into foreign currency forward and option contracts to reduce the effect of fluctuating currency exchange rates (principally the Japanese yen and the euro). Generally, foreign currency derivatives used for hedging are put in place using the same or like currencies and duration as the underlying exposures. Forward contracts are principally used to manage exposures arising from subsidiary trade and loan payables and receivables denominated in foreign currency. These contracts are recorded at fair value with the gain or loss recognized in current earnings. The purchased option contracts are used to hedge anticipated foreign currency transactions, primarily intercompany inventory activities expected to occur within the next year. These contracts are designated as cash flow hedges of those future transactions and the impact on earnings is included in cost of sales. We may enter into foreign currency forward contracts and currency swaps as fair value hedges of firm commitments. Forward and option contracts generally have maturities not exceeding 12 months.

In the normal course of business, our operations are exposed to fluctuations in interest rates. These fluctuations can vary the costs of financing, investing, and operating. We address a portion of these risks through a controlled program of risk management that includes the use of derivative financial instruments. The objective of controlling these risks is to limit the impact of fluctuations in interest rates on earnings. Our primary interest rate risk exposure results from changes in short-term U.S. dollar interest rates. In an effort to manage interest rate exposures, we strive to achieve an acceptable balance between fixed and floating rate debt and investment positions and may enter into interest rate swaps or collars to help maintain that balance. Interest rate swaps or collars that convert our fixed rate debt or investments to a floating rate are designated as fair value hedges of the underlying instruments. Interest rate swaps or collars that convert floating rate debt or investments to a fixed rate are designated as cash flow hedges. Interest expense on the debt is adjusted to include the payments made or received under the swap agreements.

Goodwill and other intangibles: Other intangibles with finite lives arising from acquisitions and research alliances are amortized over their estimated useful lives, ranging from 5-10 years, using the straight-line method. Beginning with our adoption of Statement of Financial Accounting Standards (SFAS) 142, Goodwill and Other Intangible Assets, on January 1, 2002, goodwill is no longer amortized. Goodwill and other intangibles are reviewed to assess recoverability at least annually and when certain impairment indicators are present. Unamortized goodwill and other intangibles with finite lives were $92.2 million and $94.7 million, respectively, at December 31, 2003 and 2002, and were included in sundry assets in the consolidated balance sheets. We currently have no other intangible assets with indefinite lives. No material impairments occurred with respect to the carrying value of our goodwill or other intangible assets in 2003, 2002, or 2001. Amortization of goodwill in 2001 was negligible.

Property and equipment: Property and equipment is stated on the basis of cost. Provisions for depreciation of buildings and equipment are computed generally by the straight-line method at rates based on their estimated useful lives (generally 12 to 50 years for buildings and 3 to 18 years for equipment).

At December 31, property and equipment consisted of the following:

	2003	2002
Land	**$ 124.8**	$ 111.0
Buildings	**3,134.7**	2,871.7
Equipment	**5,305.8**	5,148.4
Construction in progress	**2,502.7**	1,415.0
	11,068.0	9,546.1
Less allowances for depreciation	**4,529.0**	4,253.1
	$ 6,539.0	$5,293.0

Depreciation expense for 2003, 2002, and 2001 was $469.3 million, $437.8 million, and $414.9 million, respectively. Approximately $61.0 million, $60.3 million, and $61.5 million of interest costs were capitalized as part of property and equipment in 2003, 2002, and 2001, respectively. Total rental expense for all leases, including contingent rentals (not material), amounted to approximately $268.5 million, $240.8 million, and $207.1 million for 2003, 2002, and 2001, respectively. Capital leases included in property and equipment in the consolidated balance sheets, capital lease obligations entered into, and future minimum rental commitments are not material.

Revenue recognition: We recognize revenue from sales of products at the time title of goods passes to the buyer and the buyer assumes the risks and rewards of ownership. This is generally at the time products are shipped to the customer. Provisions for discounts and rebates to customers are established in the same period the related sales are recorded and are included in other current liabilities. Revenue from copromotion services (primarily Actos) is based upon net sales reported by our copromotion partner and, if applicable, the number of sales calls we perform. We immediately recognize the full amount of milestone payments due us upon the achievement

of the milestone event if the event is substantive, objectively determinable, and represents an important point in the development life cycle of the pharmaceutical product. Milestone payments earned by us are generally recorded in other income-net. Initial fees we receive from the partnering of our compounds under development are amortized through the expected product approval date. Initial fees received from out-licensing agreements that include both the sale of marketing rights to our commercialized products and a related commitment to supply the products are generally recognized as net sales over the term of the supply agreement.

Research and development: We recognize as incurred the cost of directly acquiring assets to be used in the research and development process that have not yet received regulatory approval for marketing and for which no alternative future use has been identified. If the product has obtained regulatory approval, we generally capitalize the milestones paid and amortize them over the period benefited. Milestones paid prior to regulatory approval of the product are generally expensed when the event requiring payment of the milestone occurs.

Income taxes: Deferred taxes are recognized for the future tax effects of temporary differences between financial and income tax reporting based on enacted tax laws and rates. Federal income taxes are provided on the portion of the income of foreign subsidiaries that is expected to be remitted to the United States and be taxable.

Earnings per share: We calculate basic earnings per share based on the weighted-average number of outstanding common shares and incremental shares. We calculate diluted earnings per share based on the weighted-average number of outstanding common shares plus the effect of dilutive stock options and other incremental shares.

Stock-based compensation: As discussed further in Note 7, we have elected to follow Accounting Principles Board (APB) Opinion 25, Accounting for Stock Issued to Employees, and related interpretations in accounting for our stock options and performance awards. Under APB 25, because the exercise price of our employee stock options equals the market price of the underlying stock on the date of grant, no compensation expense is recognized. However, SFAS 123, Accounting for Stock-Based Compensation, as amended by SFAS 148, Accounting for Stock-Based Compensation-Transition and Disclosure, requires us to present pro forma information as if we had accounted for our employee stock options and performance awards under the fair value method of that statement. For purposes of pro forma disclosure, the estimated fair value of the options and performance awards at the date of the grant is amortized to expense over the vesting period. The following table illustrates the effect on net income and earnings per share if we had applied the fair value recognition provisions of SFAS 123 to stock-based employee compensation.

	2003	2002	2001
Net income, as reported	**$2,560.8**	$2,707.9	$2,780.0
Add: Compensation expense for stock-based performance awards included in reported net income, net of related tax effects	—	—	5.5
Deduct: Total stock-based employee compensation expense determined under fair-value-based method for all awards, net of related tax effects	**(220.8)**	(322.1)	(215.9)
Pro forma net income	**$2,340.0**	$2,385.8	$2,569.6
Earnings per share:			
Basic, as reported	**$ 2.38**	$ 2.51	$ 2.58
Basic, pro forma	**$ 2.17**	$ 2.22	$ 2.38
Diluted, as reported	**$ 2.37**	$ 2.50	$ 2.55
Diluted, pro forma	**$ 2.16**	$ 2.20	$ 2.36

Note 2: Implementation of New Financial Accounting Pronouncements

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

In 2002, the FASB issued SFAS 145, Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB State-

ment No. 13, and Technical Corrections. SFAS 145 eliminates the classification of debt extinguishments as extraordinary items. The adoption of this statement on January 1, 2003, resulted in the reclassification of the extraordinary item resulting from debt extinguishment in 2001 to interest expense. The adoption had no impact on our net income.

In 2002, the FASB issued SFAS 146, Accounting for Costs Associated with Exit or Disposal Activities. SFAS 146 requires that a liability for a cost associated with an exit or disposal activity be recognized when the liability is incurred. Severance pay under SFAS 146, in many cases, would be recognized over the remaining service period rather than at the time the plan is communicated. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. We adopted SFAS 146 for any actions initiated after January 1, 2003, and any future exit costs or disposal activities will be subject to this statement.

In 2002, the FASB issued FASB Interpretation (FIN) 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others. FIN 45 requires an issuer of a guarantee to recognize an initial liability for the fair value of the obligations covered by the guarantee. FIN 45 also addresses the disclosures required by a guarantor in interim and annual financial statements regarding obligations under guarantees. We have adopted the requirement for recognition of liabilities for the fair value of guaranteed obligations prospectively for guarantees entered into after January 1, 2003. We adopted the disclosure provisions as of December 31, 2002.

In 2003, the FASB issued FIN 46, Consolidation of Variable Interest Entities. FIN 46 defines a variable interest entity (VIE) as a corporation, partnership, trust, or any other legal structure that does not have equity investors with a controlling financial interest or has equity investors that do not provide sufficient financial resources for the entity to support its activities. FIN 46 requires consolidation of a VIE by the primary beneficiary of the assets, liabilities, and results of activities. FIN 46 also requires certain disclosures by all holders of a significant variable interest in a VIE that are not the primary beneficiary. We do not have any material investments in variable interest entities; therefore, the adoption of this interpretation in the first quarter of 2004 is not expected to have a material impact on our consolidated financial position or results of operations.

In 2003, the FASB issued SFAS 150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity. SFAS 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. Financial instruments within the scope of SFAS 150 will now be required to be classified as a liability. This statement also requires enhanced disclosures regarding alternative methods of settling the instruments and the capital structure of entities. SFAS 150 is effective for all financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003. The adoption of this statement had no impact on our consolidated financial position or results of operations.

On January 12, 2004, the FASB issued FASB Staff Position (FSP) FAS106-1 regarding the accounting for the effects of the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (MMA). The FSP allows companies an opportunity to assess the effect of MMA on their retirement-related benefit costs and obligations and reflect the effects in the 2003 financial statements, pursuant to SFAS 106, Employer's Accounting for Postretirement Benefits Other Than Pensions. Companies are also allowed to defer accounting for the effects of MMA until authoritative guidance is issued. We have elected to defer accounting for the effects of MMA, in accordance with the FSP. As a result, the accumulated postretirement benefit obligation and net periodic postretirement benefit cost discussed in Note 12 do not reflect the effects of MMA on the plan. Specific authoritative guidance on the accounting for the federal subsidy, one of the provisions of MMA, is pending and that guidance, when issued, could require us to change previously reported information.

Note 3: Acquisition, Collaborations, and Disposition

In November 2003, we announced a merger agreement with Applied Molecular Evolution, Inc. (AME). Shareholders of AME will vote upon a proposal to adopt the merger agreement on February 11, 2004. Under terms of the agreement, AME shareholders will receive $18 for each outstanding AME share at closing. AME shareholders may elect to receive the $18 in cash or shares of Lilly common stock based on the closing price of Lilly stock on the closing date, subject to proration such that the total purchase price paid by Lilly is 80 percent stock and 20 percent cash. The purchase price of the acquisition, including transaction costs, is estimated to be approximately $400 million, net of cash acquired. The merger is expected to close in the first quarter of 2004. While the allocation of the purchase price will not be completed until after the effective date of the merger, we anticipate that a significant portion of the purchase price will be allocated to acquired in-process research and development and charged to expense in the first quarter of 2004.

In September 2002, we entered into a collaboration arrangement with Amylin Pharmaceuticals, Inc. (Amylin),

to jointly develop and commercialize Amylin's synthetic exendin-4 compound, a potential new treatment for type 2 diabetes. In 2001, we entered into collaboration arrangements with three companies. In August, we licensed from Isis Pharmaceuticals, Inc. (Isis), Affinitak™, a non-small-cell lung cancer drug candidate and entered into an agreement regarding an ongoing research collaboration. In September, we entered into a collaboration with Bioprojet, Société Civile de Recherche, to jointly develop and commercialize a vasopeptidase inhibitor (fasidotril) for hypertension and chronic heart failure. In October, we entered into a collaboration with 3M Company to jointly develop and commercialize an immune response modifier (resiquimod) for various forms of herpes. The ongoing activity with respect to each of these agreements is not material to our research and development expenses.

At the inception of these collaborations, these compounds were in the development phase and no alternative future uses were identified. As with many development phase compounds, launch of the products, if approved, was not expected in the near term. Our charge for acquired in-process research and development expense related to these arrangements totaled $84.0 million and $190.5 million in 2002 and 2001, respectively. See Note 4 for further discussion of 2003 developments regarding the Isis agreements. In 2003, based upon recent clinical results of resiquimod and fasidotril and other opportunities we have in our product pipeline, the collaboration agreements between the parties were terminated.

In conjunction with the collaboration arrangement with Amylin, we also entered into a loan agreement. Following the successful completion of the ongoing clinical trials and contingent upon certain other events, we have agreed to loan Amylin up to $110 million during the development period of the product, repayable in cash or Amylin stock at our option. As of December 31, 2003, no loans to Amylin were outstanding.

Note 4: Asset Impairments, Restructuring, and Other Special Charges

In December 2002, we initiated a plan of eliminating approximately 700 positions worldwide in order to streamline our infrastructure. While a substantial majority of affected employees were successfully placed in other positions in the company, severance expenses were incurred in the first quarter of 2003 for those employees who elected a severance package. The restructuring and other special charges incurred in the first quarter were $52.5 million, consisting primarily of voluntary severance expenses, which have been included in asset impairments, restructuring, and other special charges in our consolidated statement of income. Approximately $40.0 million of this charge was expended during 2003 with substantially all the remainder to be expended during the first quarter of 2004.

In addition, as part of our previously disclosed ongoing strategic review, management approved global manufacturing strategies across our product portfolio during 2003 to improve plant performance and efficiency, including the outsourcing of production of certain anti-infective products. These decisions resulted in the impairment of certain assets, primarily manufacturing assets in the U.S. This review did not result in any closure of facilities, but certain assets located at various manufacturing sites were affected. We have ceased using these assets and substantially all these assets have been disposed of or destruction commenced in 2003. The impairment charges were necessary to adjust the carrying value of these assets to zero. These asset impairment charges totaled $142.9 million, of which $114.6 million was incurred in the first quarter of 2003 with the remaining $28.3 million incurred in the fourth quarter of 2003, and are included in asset impairments, restructuring, and other special charges in our consolidated statement of income.

In conjunction with the Isis agreement discussed in Note 3, we purchased approximately 4.2 million shares of Isis common stock with a cost basis of approximately $68.0 million and we committed to loan Isis $100 million over the four-year term of the research agreement. The Isis loan is repayable at the end of the research agreement term in cash or Isis stock, at Isis's option, using a conversion price of $40 per share. In addition, we committed to loan Isis $21.2 million for the building of a manufacturing suite for Affinitak. On March 17, 2003, we announced, along with Isis, the results of the Phase III trial that evaluated Affinitak when combined with chemotherapy in patients with advanced non-small-cell lung cancer. No difference was observed in the overall survival of the two groups. Due to this announcement and the decline in Isis's stock price that occurred in the previous 12 months, we concluded that our investment in Isis common stock was other-than-temporarily impaired as defined by generally accepted accounting principles. For the same reasons, it was probable that the value of the consideration that we will be eligible to receive from Isis pursuant to the terms of the loan agreements will be less than the carrying amount of the loans. Therefore, in the first quarter of 2003, we recognized an impairment in our investment in Isis common stock of $55.0 million and a reserve related to the loans of $92.9 million. In addition, we recognized a charge of $38.9 million for contractual obligations related to Affinitak. The primary portion of this charge resulted from our supply agreement with Isis. The supply agreement obligated us to pay certain costs associated with work-in-process and raw materials and other costs that were triggered when we canceled our order of Affinitak. The remaining portion of the charge resulted from our contractual obligations related to the conduct of Affinitak clinical

trials. As of December 31, 2003, approximately $2.5 million remained related to the original $38.9 million charge. The remaining cash payments associated with the Affinitak trials are expected to be made through mid-2004. The stock and loan impairments and other special charges incurred in the first quarter related to this relationship totaled $186.8 million and have been included in the asset impairments, restructuring, and other special charges category in our consolidated statement of income.

As a result of a strategic review of our global manufacturing operations, we recognized asset impairment and other site charges totaling $121.4 million in the third quarter of 2001. The charges principally consist of impairments of facilities and equipment that were substantially disposed of in 2002, termination of third-party manufacturing arrangements, and a plant closure in Taiwan. The impairment charges were necessary to adjust the carrying value of certain manufacturing assets to fair value. The fair value of the assets was estimated based upon anticipated future cash flows, discounted at a rate commensurate with the risk involved. Approximately $18 million of this charge was for severance-related costs, which were fully expended during 2002.

Note 5: Financial Instruments and Investments

Financial instruments that potentially subject us to credit risk consist principally of trade receivables and interestbearing investments. Wholesale distributors of life-sciences products and managed care organizations account for a substantial portion of trade receivables; collateral is generally not required. The risk associated with this concentration is mitigated by our ongoing credit review procedures. We place substantially all our interest-bearing investments with major financial institutions, in U.S. government securities, or with top-rated corporate issuers. In accordance with documented corporate policies, we limit the amount of credit exposure to any one financial institution. We are exposed to credit-related losses in the event of nonperformance by counterparties to financial instruments but do not expect any counterparties to fail to meet their obligations given their high credit ratings.

Fair Value of Financial Instruments

A summary of our outstanding financial instruments and other investments at December 31 follows:

	2003		2002	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Short-term investments				
Debt securities	**$ 957.0**	**$ 957.0**	$1,708.8	$1,708.8
Noncurrent investments				
Marketable equity	**$ 105.5**	**$ 105.5**	$ 85.9	$ 85.9
Debt securities	**3,173.1**	**3,173.1**	2,458.6	2,458.6
Equity method and other investments	**96.0**	**N/A**	605.9	N/A
	$3,374.6		$3,150.4	
Long-term debt, including current portion	**$4,867.5**	**$5,107.8**	$4,643.6	$4,886.7

We determine fair values based on quoted market values where available or discounted cash flow analyses (principally long-term debt). The fair value of equity method investments is not readily available and disclosure is not required. The fair value and carrying amount of risk-management instruments in the aggregate were not material at December 31, 2003 and 2002. Approximately $3.6 billion of our investments in debt securities mature within five years.

A summary of the unrealized gains and losses (pretax) of our available-for-sale securities in other comprehensive income at December 31 follows:

	2003	2002
Unrealized gross gains	**$72.3**	$77.4
Unrealized gross losses	**10.6**	87.7

The net adjustment to unrealized gains and losses (net of tax) on available-for-sale securities increased (decreased) other comprehensive income by $45.4 million, ($45.0) million, and $34.3 million in 2003, 2002, and 2001, respectively. Activity related to our available-for-sale investment portfolio was as follows:

	2003	2002	2001
Proceeds from sales	**$4,903.7**	$3,724.2	$1,826.3
Realized gross gains on sales	**72.1**	57.0	14.1
Realized gross losses on sales	**26.4**	35.2	0.1

During the years ended December 31, 2003 and 2002, net losses related to ineffectiveness and net losses related to the portion of fair value and cash flow hedging instruments excluded from the assessment of effectiveness were not material.

We expect to reclassify an estimated $53.9 million of pretax net losses on cash flow hedges of anticipated foreign currency transactions and the variability in expected future interest payments on floating rate debt from accumulated other comprehensive loss to earnings during 2004. This assumes that short-term interest rates remain unchanged from the prevailing rates at December 31, 2003.

Note 6: Borrowings

Long-term debt at December 31 consisted of the following:

	2003	2002
4.50 to 7.13 percent notes (due 2012-2036)	**$1,487.4**	$1,287.4
2.90 to 8.38 percent notes (due 2003-2008)	**811.4**	711.4
Floating rate bonds (due 2008-2037)	**417.8**	666.6
Private placement bonds (due 2007-2008)	**810.5**	542.8
Floating rate capital securities (due 2029)	**525.0**	525.0
8.38 percent eurodollar bonds (due 2005)	**150.0**	150.0
Resettable coupon capital securities (due 2029)	**300.0**	300.0
6.55 percent ESOP debentures (due 2017)	**94.6**	95.6
Other, including capitalized leases	**130.3**	130.8
SFAS 133 fair value adjustment	**140.5**	234.0
	4,867.5	4,643.6
Less current portion	**179.7**	285.4
	$4,687.8	$4,358.2

In March 2003, we issued $300.0 million of 2.9 percent 5-year notes and $200.0 million of 4.5 percent 15-year notes. In July 2002 and May 2001, we issued $150.0 million and $250.0 million, respectively, of floating rate bonds that mature in 2037. The variable interest rate on these bonds is at LIBOR (1.27 percent at December 31, 2003) and beginning May 15, 2004, will adjust every six months to reflect our six-month credit spread. The interest accumulates over the life of the bonds and is payable upon maturity. We have an option to begin periodic interest payments any time after May 15, 2004. At the time of option exercise, we would owe all previously accrued interest on the bonds. Additionally, in July 2003 and July 2002, respectively, we executed a $330.0 million and $542.8 million private placement note with a financial institution. Principal and interest are due semiannually over the five-year terms of each of these notes. In conjunction with these notes, we entered into interest rate swap agreements with the same financial institution, which converts the fixed rate into a variable rate of interest at essentially LIBOR over the term of the notes. In March 2002, we issued $500.0 million of 10-year 6.0 percent notes. In addition, in 2001, we issued $400.0 million of 5.5 percent notes due July 2006 and $249.5 million of floating rate bonds due October 2008.

The floating rate capital securities and the resettable coupon capital securities are subordinated to the notes, bonds, and debentures listed above. The floating rate capital securities pay cumulative interest at an annual rate equal to LIBOR plus a predetermined spread, reset quarterly. The rates at December 31, 2003 and 2002, were 2.37 percent and 2.86 percent, respectively. The securities may be redeemed any time on or after August 5, 2004, for a defined redemption price. The resettable coupon capital securities pay cumulative interest at an annual rate of 7.72 percent until August 1, 2004. At this date and every fifth anniversary thereafter, the interest rate will be reset equal to the weekly average interest rate of U.S. treasury securities having an index maturity of five years for the week immediately preceding the reset date plus a predetermined spread. The securities may be redeemed on August 1,

2004, and anytime thereafter for a defined redemption price.

The 6.55 percent Employee Stock Ownership Plan (ESOP) debentures are obligations of the ESOP but are shown on the consolidated balance sheet because we guarantee them. The principal and interest on the debt are funded by contributions from us and by dividends received on certain shares held by the ESOP. Because of the amortizing feature of the ESOP debt, bondholders will receive both interest and principal payments each quarter.

In 2001, we repurchased $188.6 million of 8.38 percent notes due in 2006, $14.0 million of 6.77 percent notes due in 2036, and $198.6 million of 7.13 percent notes due in 2025. As a result of this early extinguishment of debt, we recognized a charge of $45.2 million. As a result of our adoption of SFAS 145 in 2003 (see Note 2), this charge was reclassified from an extraordinary charge to interest expense. In 2003, we repurchased $257.1 million of floating rate debt securities due in 2008.

The aggregate amounts of maturities on long-term debt for the next five years are as follows: 2004, $179.7 million; 2005, $360.3 million; 2006, $719.4 million; 2007, $207.4 million; and 2008, $389.6 million.

At December 31, 2003 and 2002, short-term borrowings included $16.8 million and $260.0 million, respectively, of notes payable to banks. Included in short-term borrowings in 2002 are $250.0 million of 4.23 percent one-year resettable notes issued in March 2001. These notes were repaid in 2003. At December 31, 2003, unused committed lines of credit totaled approximately $1.24 billion. Compensating balances and commitment fees are not material, and there are no conditions that are probable of occurring under which the lines may be withdrawn.

We have converted substantially all fixed rate debt to floating rates through the use of interest rate swaps. The weighted-average effective borrowing rate based on debt obligations and interest rates at December 31, 2003 and 2002, including the effects of interest rate swaps for hedged debt obligations, was 2.7 percent and 3.5 percent, respectively.

Cash payments of interest on borrowings totaled $44.7 million, $54.6 million, and $171.6 million in 2003, 2002, and 2001, respectively.

In accordance with the requirements of SFAS 133, the portion of our fixed-rate debt obligations that is hedged is reflected in the consolidated balance sheet as an amount equal to the sum of the debt's carrying value plus the fair value adjustment representing changes in fair value of the hedged debt attributable to movements in market interest rates subsequent to the inception of the hedge.

Note 7: Stock Plans

Stock options are granted to employees at exercise prices equal to the fair market value of the company's stock at the dates of grant. Generally, options vest 100 percent 3 years from the grant date and have a term of 10 years. Performance awards are granted to officers and key employees and are payable in shares of our common stock. The number of performance award shares actually issued, if any, varies depending upon the achievement of certain earnings-per-share targets. In general, performance awards vest 100 percent at the end of the second fiscal year following the grant date. No performance awards were granted in 2002.

We issued a grant under the GlobalShares program in 2001. Essentially all employees were given an option to buy 125 shares of our stock at a price equal to the fair market value of our stock on the date of the grant. Options to purchase approximately 4.3 million shares were granted as part of the program in 2001. Individual grants generally become exercisable on or after the third anniversary of the grant date and have a term of 10 years.

We also issued a special stock option grant in 2001 to global management and all employees in the U.S. and Puerto Rico. This option grant was designed to retain and motivate employees affected by the compensation changes due to the Prozac patent expiration. Options to purchase approximately 10.0 million shares were granted as part of this program at a price equal to the fair market value on the date of the grant. Approximately 7.3 million of these options vested in 2002 with the remainder vesting in 2003.

We have elected to follow APB Opinion 25 and related interpretations in accounting for our stock options and performance awards. See Note 1 for a calculation of our net income and earnings per share under the fair value method pursuant to SFAS 123.

The weighted-average per-share fair values of the individual options and performance awards granted during 2003, 2002, and 2001 were as follows on the date of grant:

	2003	2002	2001
Employee stock options	**$20.59**	$25.98	$26.59
Performance awards	**63.51**	N/A	78.86

The fair values of the options calculated in accordance with SFAS 123 were determined using a Black-Scholes option-pricing model with the following assumptions:

	2003	2002	2001
Dividend yield	**1.50%**	1.54%	1.80%
Volatility	**35.10%**	35.00%	33.10%
Risk-free interest rate	**3.32%**	3.14%	4.58%
Forfeiture rate	**0**	0	0
Expected life	**7 years**	7 years	7 years

Stock option activity during 2001-2003 is summarized below:

	Shares of Common Stock Attributable to Options (in thousands)	Weighted-Average Exercise Price of Options
Unexercised at January 1, 2001	45,125	$48.28
Granted	26,883	76.10
Exercised	(4,298)	26.72
Forfeited	(612)	71.20
Unexercised at December 31, 2001	67,098	60.60
Granted	14,133	74.33
Exercised	(3,357)	21.18
Forfeited	(1,819)	70.95
Unexercised at December 31, 2002	76,055	64.65
Granted	14,361	57.36
Exercised	(4,379)	22.65
Forfeited	(3,227)	70.03
Unexercised at December 31, 2003	82,810	65.39

The following table summarizes information concerning outstanding and exercisable options at December 31, 2003 (shares in millions, contractual life in years):

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price
$10–$25	6.76	1.52	$ 21.29	6.76	$ 21.29
$25–$65	21.37	7.23	56.14	7.97	53.27
$65–$75	31.51	6.25	71.93	21.34	71.03
$75–$95	23.17	7.91	77.90	12.59	79.44

Shares exercisable at December 31, 2003, 2002, and 2001, were 48.7 million, 44.6 million, and 35.2 million, respectively.

As noted above, the number of shares ultimately issued for the performance award program is dependent upon the earnings achieved during the vesting period. Pursuant to this plan, approximately 0.4 million shares and 0.8 million shares were issued in 2002 and 2001, respectively. No shares were issued in 2003 and none will be issued in 2004.

At December 31, 2003, additional options, performance awards, or restricted stock grants may be granted under the 2002 Lilly Stock Plan and the Lilly GlobalShares Stock Plan for not more than 74.5 million shares and 2.1 million shares, respectively.

Note 8: Other Assets and Other Liabilities

Our sundry assets include our capitalized computer software, prepaid retiree health benefit (Note 12), goodwill and other intangibles (Note 1), estimated insurance recoveries from our product litigation and environmental contingencies (Note 13), and a variety of other items. The increase in sundry assets is primarily attributable to an

increase in capitalized computer software and prepaid retiree health benefits, offset partially by lower long-term deferred income tax assets.

Our other current liabilities include our sales discount and rebate accruals, including our Medicaid rebate accrual, deferred income from our collaboration and out-licensing arrangements, other taxes, interest payable, and a variety of other items. Major contributors to the increase in other current liabilities are interest payable, deferred income from our collaboration and out-licensing arrangements, and the Medicaid rebate accrual.

Our other noncurrent liabilities include the accrued liabilities from our pension and retiree health plans (Note 12), deferred income taxes (Note 11), product liability litigation and environmental accruals (Note 13), deferred income from our collaboration and out-licensing arrangements, and a variety of other items. The increase in other noncurrent liabilities is primarily attributable to deferred income taxes, deferred income from collaboration and out-licensing arrangements, and accrued liabilities from our pension and retiree health plans.

None of the components of sundry assets exceeds 5 percent of total assets and none of the components of other current liabilities or other noncurrent liabilities exceeds 5 percent of total liabilities.

Note 9: Shareholders' Equity

Changes in certain components of shareholders' equity were as follows:

				Common Stock in Treasury	
	Additional Paid-in Capital	Retained Earnings	Deferred Costs—ESOP	Shares (in thousands)	Amount
Balance at January 1, 2001	$2,610.0	$ 6,223.2	$(135.0)	1,007	$ 109.5
Net income		2,780.0			
Cash dividends declared per share: $1.15		(1,232.8)			
Retirement of treasury shares	(581.8)			(7,368)	(586.7)
Purchase for treasury	(24.8)			7,176	571.0
Issuance of stock under employee stock plans	229.0			170	13.6
ESOP transactions	18.4		5.9		
Other	0.1	(0.1)			
Reclassification	359.1	(359.1)			
Balance at December 31, 2001	2,610.0	7,411.2	(129.1)	985	107.4
Net income		2,707.9			
Cash dividends declared per share: $1.27		(1,370.7)			
Retirement of treasury shares	(393.9)			(4,677)	(396.8)
Purchase for treasury				4,532	389.2
Issuance of stock under employee stock plans	131.8			168	9.7
ESOP transactions	13.8		5.8		
Reclassification	248.3	(248.3)			
Balance at December 31, 2002	2,610.0	8,500.1	(123.3)	1,008	109.5
Net income		2,560.8			
Cash dividends declared per share: $1.36		(1,465.4)			
Retirement of treasury shares	(289.1)			(3,180)	(291.2)
Purchase for treasury				2,976	276.8
Issuance of stock under employee stock plans	150.4			148	9.1
ESOP transactions	13.6		4.7		
Reclassification	125.1	(125.1)			
Balance at December 31, 2003	$2,610.0	$ 9,470.4	$(118.6)	952	$ 104.2

As of December 31, 2003, we have purchased $2.08 billion of our announced $3.0 billion share repurchase program. We acquired approximately 3.0 million, 4.5 million, and 7.2 million shares in 2003, 2002, and 2001, respectively, under our share repurchase programs. As previously disclosed, in connection with the share repurchase program, we entered into agreements to purchase shares of our stock. During the second quarter of 2003, we satisfied all our remaining obligations under the agreements.

We have 5 million authorized shares of preferred stock. As of December 31, 2003 and 2002, no preferred stock has been issued.

We have funded an employee benefit trust with 40 million shares of Lilly common stock to provide a source of

funds to assist us in meeting our obligations under various employee benefit plans. The funding had no net impact on shareholders' equity as we consolidated the employee benefit trust. The cost basis of the shares held in the trust was $2.64 billion and is shown as a reduction in shareholders' equity, which offset the resulting increases of $2.61 billion in additional paid-in capital and $25 million in common stock. Any dividend transactions between us and the trust are eliminated. Stock held by the trust is not considered outstanding in the computation of earnings per share. The assets of the trust were not used to fund any of our obligations under these employee benefit plans in 2003, 2002, or 2001.

We have an ESOP as a funding vehicle for the existing employee savings plan. The ESOP used the proceeds of a loan from us to purchase shares of common stock from the treasury. The ESOP issued $200 million of third-party debt, repayment of which was guaranteed by us (see Note 6). The proceeds were used to purchase shares of our common stock on the open market. Shares of common stock held by the ESOP will be allocated to participating employees annually through 2017 as part of our savings plan contribution. The fair value of shares allocated each period is recognized as compensation expense.

Under a Shareholder Rights Plan adopted in 1998, all shareholders receive, along with each common share owned, a preferred stock purchase right entitling them to purchase from the company one one-thousandth of a share of Series B Junior Participating Preferred Stock (the Preferred Stock) at a price of $325. The rights are exercisable only after the Distribution Date, which is generally the 10th business day after the date of a public announcement that a person (the Acquiring Person) has acquired ownership of 15 percent or more of our common stock. We may redeem the rights for $.005 per right up to and including the Distribution Date. The rights will expire on July 28, 2008, unless we redeem them earlier.

The plan provides that, if an Acquiring Person acquires 15 percent or more of our outstanding common stock and our redemption right has expired, generally each holder of a right (other than the Acquiring Person) will have the right to purchase at the exercise price the number of shares of our common stock that have a value of two times the exercise price.

Alternatively, if, in a transaction not approved by the board of directors, we are acquired in a business combination transaction or sell 50 percent or more of our assets or earning power after a Distribution Date, generally each holder of a right (other than the Acquiring Person) will have the right to purchase at the exercise price the number of shares of common stock of the acquiring company that have a value of two times the exercise price.

At any time after an Acquiring Person has acquired 15 percent or more but less than 50 percent of our outstanding common stock, the board of directors may exchange the rights (other than those owned by the Acquiring Person) for our common stock or Preferred Stock at an exchange ratio of one common share (or one one-thousandth of a share of Preferred Stock) per right.

Note 10: Earnings per Share

The following is a reconciliation of the denominators used in computing earnings per share:

	2003	2002	2001
		(Shares in thousands)	
Income available to common shareholders	**$ 2,560.8**	$ 2,707.9	$ 2,780.0
Basic earnings per share			
Weighted-average number of common shares outstanding, including incremental shares	**1,076,547**	1,076,922	1,077,497
Basic earnings per share	**$ 2.38**	$ 2.51	$ 2.58
Diluted earnings per share			
Weighted-average number of common shares outstanding	**1,076,547**	1,076,873	1,077,390
Stock options and other incremental shares	**5,683**	8,215	13,403
Weighted-average number of common shares outstanding—diluted	**1,082,230**	1,085,088	1,090,793
Diluted earnings per share	**$ 2.37**	$ 2.50	$ 2.55

Note 11: Income Taxes

Following is the composition of income taxes:

	2003	2002	2001
Current			
Federal	**$ 391.2**	$140.1	$ 297.6
Foreign	**284.7**	306.3	247.9
State	**(6.2)**	(13.4)	16.6
	669.7	433.0	562.1
Deferred			
Federal	**(112.9)**	366.1	240.5
Foreign	**138.2**	(47.3)	34.6
State	**5.9**	(2.0)	0.2
	31.2	316.8	275.3
Utilization of capital loss carryforwards	**—**	—	(110.5)
Income taxes	**$ 700.9**	$749.8	$ 726.9

Significant components of our deferred tax assets and liabilities as of December 31 are as follows:

	2003	2002
Deferred tax assets		
Sale of intangibles	**$ 415.0**	$ 485.3
Other carryforwards	**411.7**	398.4
Inventory	**353.5**	61.3
Compensation and benefits	**275.9**	250.0
Tax credit carryforwards and carrybacks	**105.9**	93.6
Asset purchases	**62.2**	103.0
Other	**527.5**	467.6
	2,151.7	1,859.2
Valuation allowances	**(415.3)**	(382.2)
Total deferred tax assets	**1,736.4**	1,477.0
Deferred tax liabilities		
Prepaid employee benefits	**(701.5)**	(626.6)
Property and equipment	**(564.5)**	(480.4)
Unremitted earnings	**(204.6)**	(115.6)
Other	**(153.3)**	(84.7)
Total deferred tax liabilities	**(1,623.9)**	(1,307.3)
Deferred tax assets–net	**$ 112.5**	$ 169.7

At December 31, 2003, we had other carryforwards for international and U.S. income tax purposes of $266.4 million: $150.0 million will expire within five years and $70.6 million thereafter; $45.8 million of the carryforwards will never expire. The primary component of the remaining portion of the deferred tax asset for other carryforwards is related to net operating losses for state income tax purposes that are fully reserved. We also have tax credit carryforwards and carrybacks of $105.9 million available to reduce future income taxes: $46.3 million will be carried back, $0.3 million expires after five years, and $9.3 million of the tax credit carryforwards will never expire. The remaining portion of the tax credit carryforwards is related to state tax credits that are fully reserved.

Domestic and Puerto Rican companies contributed approximately 22 percent, 28 percent, and 55 percent in 2003, 2002, and 2001, respectively, to consolidated income before income taxes. At December 31, 2003, we had an aggregate of $9.5 billion of unremitted earnings of foreign subsidiaries that have been or are intended to be permanently reinvested for continued use in foreign operations and that, if distributed, would result in taxes at approximately the U.S. statutory rate. We have a subsidiary operating in Puerto Rico under a tax incentive grant that begins to expire at the end of 2007.

Cash payments of income taxes totaled $614.0 million, $864.0 million, and $320.0 million in 2003, 2002, and 2001, respectively. The increase in cash payments of income taxes in 2002 is primarily attributable to the resolution of an IRS examination.

Following is a reconciliation of the effective income tax rate applicable to income before income taxes:

	2003	2002	2001
United States federal statutory tax rate	**35.0%**	35.0%	35.0%
Add (deduct)			
International operations, including Puerto Rico	**(15.7)**	(12.6)	(13.9)
General business credits	**(0.7)**	(0.7)	(1.1)
Sundry	**2.9**	—	0.7
Effective income tax rate	**21.5%**	21.7%	20.7%

Note 12: Retirement Benefits

We used a measurement date of December 31 to develop the change in benefit obligation, change in plan assets, funded status, and amounts recognized in the consolidated balance sheets at December 31 for our defined benefit pension and retiree health benefit plans, which were as follows:

	Defined Benefit Pension Plans		Retiree Health Benefits	
	2003	2002	2003	2002
Change in benefit obligation				
Benefit obligation at beginning of year	**$3,941.1**	$3,598.7	**$ 911.6**	$ 928.2
Service cost	**196.2**	170.2	**38.2**	34.0
Interest cost	**266.1**	254.3	**60.4**	64.5
Actuarial loss	**105.7**	61.8	**136.8**	104.6
Benefits paid	**(247.3)**	(234.9)	**(75.5)**	(73.5)
Retiree health plan changes	—	—	—	(151.0)
Reduction in discount rate, foreign currency exchange rate changes, and other adjustments	**386.8**	91.0	**87.3**	4.8
Benefit obligation at end of year	**4,648.6**	3,941.1	**1,158.8**	911.6
Change in plan assets				
Fair value of plan assets at beginning of year	**3,161.3**	3,182.1	**415.0**	373.4
Actual return on plan assets	**579.2**	(224.9)	**75.3**	(46.1)
Employer contribution	**149.1**	402.7	**139.1**	161.1
Benefits paid	**(247.3)**	(234.9)	**(75.5)**	(73.5)
Foreign currency exchange rate changes and other adjustments	**57.8**	36.3	—	0.1
Fair value of plan assets at end of year	**3,700.1**	3,161.3	**553.9**	415.0
Funded status	**(948.5)**	(779.8)	**(604.9)**	(496.6)
Unrecognized net actuarial loss	**2,286.1**	2,028.0	**847.4**	698.9
Unrecognized prior service cost (benefit)	**72.1**	78.3	**(132.6)**	(148.6)
Net amount recognized	**$1,409.7**	$1,326.5	**$ 109.9**	$ 53.7
Amounts recognized in the consolidated balance sheet consisted of				
Prepaid pension	**$1,613.3**	$1,515.4	**$ 192.3**	$ 127.3
Accrued benefit liability	**(422.6)**	(398.1)	**(82.4)**	(73.6)
Accumulated other comprehensive income before income taxes	**219.0**	209.2	—	—
Net amount recognized	**$1,409.7**	$1,326.5	**$ 109.9**	$ 53.7

(Percents)	Defined Benefit Pension Plans 2003	2002	Retiree Health Benefits 2003	2002
Weighted-average assumptions as of December 31				
Discount rate for benefit obligation	**6.2**	6.8	**6.2**	6.9
Discount rate for net benefit costs	**6.8**	7.2	**6.9**	7.4
Rate of compensation increase for benefit obligation	**3.0–5.5**	3.0–5.5	—	—
Rate of compensation increase for net benefit costs	**3.0–5.5**	3.5–8.0	—	—
Expected return on plan assets for net benefit costs	**9.27**	10.5	**9.25**	10.5

In evaluating the expected return on plan assets, we have considered our historical assumptions compared with actual results, an analysis of current market conditions, asset allocations, and the views of leading financial advisers and economists. Including the investment losses due to overall market conditions in 2001 and 2002, our 10- and 20-year annualized rate of return on our U.S. defined benefit pension plans and retiree health benefit plan was approximately 9.2 percent and 11.5 percent, respectively, as of December 31, 2003. Health-care-cost trend rates were assumed to increase at an annual rate of 10 percent in 2003, decreasing 1 percent per year to 6 percent in 2007 and thereafter.

The total accumulated benefit obligation for all our defined benefit pension plans was $3.93 billion and $3.47 billion at December 31, 2003 and 2002, respectively. The projected benefit obligation, accumulated benefit obligation, and fair value of the plan assets for the defined benefit pension plans with projected benefit obligations in excess of plan assets were $4.65 billion, $3.93 billion, and $3.70 billion, respectively, as of December 31, 2003, and $3.94 billion, $3.47 billion, and $3.16 billion, respectively, as of December 31, 2002.

Net pension and retiree health benefit expense included the following components:

	Defined Benefit Pension Plans 2003	2002	2001	Retiree Health Benefits 2003	2002	2001
Components of net periodic benefit cost						
Service cost	**$ 196.2**	$ 170.2	$ 156.0	**$ 38.2**	$ 34.0	$ 28.7
Interest cost	**266.1**	254.3	242.4	**60.4**	64.5	53.8
Expected return on plan assets	**(382.0)**	(398.0)	(382.3)	**(53.6)**	(50.8)	(40.1)
Amortization of prior service cost	**11.9**	16.1	19.3	**(15.6)**	(0.7)	0.1
Recognized actuarial loss	**52.0**	21.9	9.8	**50.6**	36.0	23.6
Net periodic benefit cost	**$ 144.2**	$ 64.5	$ 45.2	**$ 80.0**	$ 83.0	$ 66.1

If the health-care-cost trend rates were to be increased by one percentage point each future year, the December 31, 2003, accumulated postretirement benefit obligation would increase by 11.3 percent and the aggregate of the service cost and interest cost components of the 2003 annual expense would increase by 15.3 percent. A one-percentage-point decrease in these rates would decrease the December 31, 2003, accumulated postretirement benefit obligation by 10.1 percent and the aggregate of the 2003 service cost and interest cost by 13.2 percent.

We have defined contribution savings plans that cover our eligible employees worldwide. The purpose of these defined contribution plans is generally to provide additional financial security during retirement by providing employees with an incentive to save. Our contributions to the plan are based on employee contributions and the level of our match. Expenses under the plans totaled $72.9 million, $41.7 million, and $39.3 million for the years 2003, 2002, and 2001, respectively.

We provide certain other postemployment benefits primarily related to disability benefits and accrue for the related cost over the service lives of employees. Expenses associated with these benefit plans in 2003, 2002, and 2001 were not significant.

Our plan assets in our U.S. defined benefit pension and retiree health plans comprise approximately 86 percent of our worldwide benefit plan assets. Our U.S. defined benefit pension and retiree health benefit plan investment allocation strategy currently comprises approximately 85 percent to 95 percent growth investments and 5 percent to 15 percent fixed-income investments. Within the growth investment classification, the plan asset strategy encompasses equity and equity-like instruments that are expected to represent approximately 75 percent of our plan asset portfolio of both public and private market investments. The largest component of these equity and equity-like instruments is public equity securities that are well diversified and invested in U.S. and international small-to-large companies. The remaining portion of the growth investment classification is represented by other alternative growth investments.

Our U.S. defined benefit pension plan and retiree health plan asset allocations as of December 31 are as follows:

(Percents)	Percentage of Pension Plan Assets		Percentage of Retiree Health Plan Assets	
	2003	2002	2003	2002
Asset Category				
Equity securities and equity-like instruments	**77%**	86%	**81%**	85%
Debt securities	**10**	10	**12**	12
Real estate	**2**	3	**1**	1
Other	**11**	1	**6**	2
Total	**100%**	100%	**100%**	100%

In 2004, we expect to contribute approximately $26.0 million to our defined benefit pension plans to satisfy minimum funding requirements in 2004. In addition, we expect to contribute approximately an additional $300.0 million of discretionary funding in 2004 to our defined benefit plans. We also expect to contribute approximately $125.0 million of discretionary funding to our postretirement health benefit plans during 2004.

Note 13: Contingencies

Three generic pharmaceutical manufacturers, Zenith Goldline Pharmaceuticals, Inc. (Zenith), Dr. Reddy's Laboratories, Ltd. (Reddy), and Teva Pharmaceuticals, have submitted abbreviated new drug applications (ANDAs) seeking permission to market generic versions of Zyprexa in various dosage forms several years prior to the expiration of our U.S. patents for the product, alleging that our patents are invalid or not infringed. We filed suits against the three companies in U.S. District Court for the Southern District of Indiana seeking a ruling that the challenges to our compound patent (expiring in 2011) are without merit. The cases have been consolidated. A trial before a district court judge in Indianapolis began on January 26, 2004, and is expected to conclude in February. A ruling from the trial court is expected in the second or third quarter of 2004. Regardless of the trial court ruling, we anticipate that appeals will follow. If we are unsuccessful at the trial court level, we cannot predict whether any of the generic companies would launch generic versions of Zyprexa prior to a final resolution of any appeals. We believe that the generic manufacturers' claims are without merit and we expect to prevail in this litigation. However, it is not possible to predict or determine the outcome of this litigation and, accordingly, we can provide no assurance that we will prevail. An unfavorable outcome would have a material adverse impact on our consolidated results of operations, liquidity, and financial position.

In October 2002, we were notified that Barr Laboratories, Inc. (Barr), had submitted an ANDA to the U.S. FDA seeking permission to market a generic version of Evista several years prior to the expiration of our U.S. patents covering the product, alleging that the patents are invalid or not infringed. On November 26, 2002, we filed suit against Barr in federal district court in Indianapolis seeking a ruling that Barr's challenges to our patents claiming the method of use and pharmaceutical form (expiring from 2012 to 2017) are without merit. In June 2003, Barr added a challenge to one of our additional patents (expiring in 2017) claiming a component in the pharmaceutical form of Evista. This patent has now been added to the lawsuit. The trial is tentatively scheduled to begin in August 2005. While we believe that Barr's claims are without merit and expect to prevail, it is not possible to predict or determine the outcome of the litigation. Therefore, we can provide no assurance that we will prevail. An unfavorable outcome could have a material adverse impact on our consolidated results of operations, liquidity, and financial position.

In July 2002, we received a grand jury subpoena for documents from the Office of Consumer Litigation, Department of Justice, related to our marketing and promotional practices and physician communications with respect to Evista. We received a second subpoena seeking additional documents in July 2003. We continue to cooperate with the government and have provided a broad range of information concerning our U.S. marketing and promotional practices, including documents relating to communications with physicians and the remuneration of physician consultants and advisers. We continue to review and enhance policies and procedures designed to assure that our marketing and promotional practices and physician communications comply with promotional laws and regulations. In recent months, several pharmaceutical companies have received subpoenas from government agencies with respect to a variety of products, including a number of neuroscience products. It is possible that other Lilly products, including Zyprexa, could become subject to investigation. It is possible that the outcome of the above matters could include criminal charges and fines and/or civil penalties. We cannot predict or determine the outcome of the above matters or reasonably estimate the amount or range of amounts of any fines or penalties that might result from an adverse outcome. It is possible, however, that an adverse outcome could have a material adverse impact on our consolidated financial position, liquidity, and results of operations.

We have been named as a defendant in numerous product liability lawsuits involving primarily two products, diethylstilbestrol (DES) and thimerosal. We have accrued for the estimated exposure with respect to all current product liability claims. In addition, we have accrued for certain claims incurred, but not filed, to the extent we can formulate a reasonable estimate of their costs. We estimate these expenses based primarily on historical claims experience and data regarding product usage. We expect the cash amounts related to the accruals to be paid out over the next several years. A portion of the costs associated with defending and disposing of these suits is covered by insurance. We estimate insurance recoverables based on existing deductibles, coverage limits, and the existing and projected future level of insolvencies among the insurance carriers.

Under the Comprehensive Environmental Response, Compensation, and Liability Act, commonly known as Superfund, we have been designated as one of several potentially responsible parties with respect to fewer than 10 sites. Under Superfund, each responsible party may be jointly and severally liable for the entire amount of the cleanup. We also continue remediation of certain of our own sites. We have accrued for estimated Superfund cleanup costs, remediation, and certain other environmental matters, taking into account, as applicable, available information regarding site conditions, potential cleanup methods, estimated costs, and the extent to which other parties can be expected to contribute to payment of those costs. We have reached a settlement with our liability insurance carriers providing for coverage for certain environmental liabilities.

The environmental liabilities and litigation accruals have been reflected in our consolidated balance sheet at the gross amount of approximately $258.7 million at December 31, 2003. Estimated insurance recoverables of approximately $83.2 million at December 31, 2003, have been reflected as assets in the consolidated balance sheet.

While it is not possible to predict or determine the outcome of the patent, product liability, or other legal actions brought against us or the ultimate cost of environmental matters, we believe that, except as noted above in this note in connection with the discussion of the Zyprexa patent litigation, the Evista patent litigation, and our marketing and promotional practices, the resolution of all such matters will not have a material adverse effect on our consolidated financial position or liquidity but could possibly be material to the consolidated results of operations in any one accounting period.

Note 14: Other Comprehensive Income (Loss)

The accumulated balances related to each component of other comprehensive income (loss) were as follows:

	Foreign Currency Translation	Unrealized Gains (Losses) on Securities	Minimum Pension Liability Adjustment	Effective Portion of Cash Flow Hedges	Accumulated Other Comprehensive Income (Loss)
Beginning balance at January 1, 2003	$(356.5)	$ (2.9)	$(137.8)	$(173.6)	$(670.8)
Other comprehensive income (loss)	473.2	45.4	(6.4)	(1.5)	510.7
Balance at December 31, 2003	$ 116.7	$42.5	$(144.2)	$(175.1)	$(160.1)

The amounts above are net of income taxes. The income taxes related to other comprehensive income were not significant as income taxes were generally not provided for foreign currency translation.

The unrealized gains (losses) on securities is net of reclassification adjustments of $37.4 million, $11.3 million, and $12.3 million, net of tax, in 2003, 2002, and 2001, respectively, for net realized gains on sales of securities included in net income. The effective portion of cash flow hedges is net of reclassification adjustments of $27.2 million in 2003, net of tax, for realized losses on foreign currency options and $14.2 million and $6.5 million, net of tax, in 2003 and 2002, respectively, for interest expense on interest rate swaps designated as cash flow hedges. In 2001, reclassification adjustments were $16.5 million, net of tax, for realized gains on foreign currency options.

Generally, the assets and liabilities of foreign operations are translated into U.S. dollars using the current exchange rate. For those operations, changes in exchange rates generally do not affect cash flows; therefore, resulting translation adjustments are made in shareholders' equity rather than in income.

RESPONSIBILITY FOR FINANCIAL STATEMENTS

Eli Lilly and Company and Subsidiaries

Management of Eli Lilly and Company is responsible for the fair presentation of the financial statements and has full responsibility for their accuracy and integrity. The statements have been prepared in accordance with generally accepted accounting principles in the United States and include amounts based on judgments and estimates by management.

We have global financial policies that govern critical areas, including internal controls, financial accounting and reporting, fiduciary accountability, and safeguarding of corporate assets. Our internal accounting control systems are designed to provide reasonable assurance that assets are safeguarded, that transactions are executed in accordance with management's authorization and are properly recorded, and that accounting records are adequate for preparation of financial statements and other financial information. The design, monitoring, and revision of internal accounting control systems involve, among other things, management's judgments with respect to the relative cost and expected benefits of specific control measures. A staff of internal auditors regularly monitors, on a worldwide basis, the adequacy and effectiveness of internal accounting controls. The general auditor reports directly to the audit committee of the board of directors.

In addition to the system of internal accounting controls, we maintain a code of conduct (known as *The Red Book*) that applies to all employees worldwide, requiring proper overall business conduct, avoidance of conflicts of interest, compliance with laws, and confidentiality of proprietary information. *The Red Book* is reviewed on a periodic basis with employees worldwide and all employees are required to report suspected violations. A hotline number is published in *The Red Book* to enable employees to report suspected violations anonymously. Employees who report suspected violations are protected from discrimination or retaliation by the company. In addition to *The Red Book*, the CEO and all financial management must agree, in writing, to a financial code of ethics, which further reinforces their fiduciary responsibilities.

The financial statements have been audited by Ernst & Young LLP, independent auditors. Their responsibility is to examine our consolidated financial statements in accordance with generally accepted auditing standards in the United States and to express their opinion with respect to the fairness of presentation of the statements. Ernst & Young reports directly to the audit committee of the board of directors.

Our audit committee comprises four nonemployee members of the board of directors, all of whom are independent from our company. The committee charter, which is published in the proxy statement, outlines the members' roles and responsibilities and is consistent with the recently enacted corporate reform laws and regulations. It is the audit committee's responsibility to appoint independent auditors subject to shareholder ratification, approve both audit and nonaudit services performed by the independent auditors, and review the reports submitted by them. The audit committee meets several times during the year with management, the internal auditors, and the independent auditors to discuss audit activities, internal controls, and financial reporting matters, including reviews of our externally published financial results. The internal auditors and the independent auditors have full and free access to the committee.

We are dedicated to ensuring that we maintain the high standards of financial accounting and reporting that we have established. We are committed to providing financial information that is transparent, timely, complete, relevant, and accurate. Our culture demands integrity and an unyielding commitment to strong internal practices and policies. Finally, we have the highest confidence in our financial reporting, underlying system of internal controls, and our people, who are objective in their responsibilities and operate under a code of conduct and the highest level of ethical standards.

Sidney Taurel
Chairman of the Board, President, and Chief Executive Officer

Charles E. Golden
Executive Vice President and Chief Financial Officer
February 2, 2004

REPORT OF INDEPENDENT AUDITORS

Board of Directors and Shareholders
Eli Lilly and Company

We have audited the accompanying consolidated balance sheets of Eli Lilly and Company and subsidiaries as of December 31, 2003 and 2002, and the related consolidated statements of income, cash flows, and comprehensive income for each of the three years in the period ended December 31, 2003. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. 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 statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Eli Lilly and Company and subsidiaries at December 31, 2003 and 2002, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2003, in conformity with accounting principles generally accepted in the United States.

Indianapolis, Indiana
February 2, 2004

Ernst & Young LLP

Graphs in Annual Report to Shareholders
for the Year Ended December 31, 2003

Set forth below, converted to tabular format, are the graphs contained in the paper format of the Company's Annual Report to Shareholders.

Graph #1 (contained in Chairman's letter to shareholders) —Nine Key Growth Products Collectively Delivered 24 Percent Increase in Net Sales

($ millions; percentages represent changes from 2002)

Product	Amount	Percent
Established Growth Products		
Zyprexa	$588	16
Humalog	187	22
Gemzar	147	17
Evista	100	12
Actos	40	10

Product	Amount	Percent
Newly Launched Growth Products		
Strattera	$368	NM
Cialis	74	NM
Forteo	60	NM
Xigris	60	60

The company's established key growth products — Zyprexa, Humalog, Gemzar, Evista, and Actos — generated $1.1 billion of incremental net sales and $7.7 billion of total net sales in 2003. In addition, our newly launched growth products — Strattera, Cialis, Forteo, and Xigris — generated $670 million of net sales in 2003. Combined, all our key growth products grew 24 percent for the year.

Graph #2—Nine Key Growth Products Accounted for 66 Percent of 2003 Sales

($ millions)

Year	Amount
99	$10,002.9
00	10,862.2
01	11,542.5
02	11,077.5
03	12,582.5

Year	Prozac/Sarafem/ Prozac Weekly	Other	Newly Launched Growth Products (Strattera, Cialis, Forteo, and Xigris)	Established Growth Products (Zyprexa, Humalog, Gemzar, Evista, and Actos)
99	26%	45%	0%	29%
00	24%	40%	0%	37%
01	17%	35%	0%	47%
02	7%	33%	1%	60%
03	5%	29%	5%	61%

Combined net sales of the company's key growth products — Zyprexa, Humalog, Gemzar, Evista, Actos, Strattera, Cialis, Forteo, and Xigris — increased by 24 percent over 2002, representing $8.3 billion, or 66 percent of total net sales, compared with $6.7 billion, or 61 percent in 2002.

Graph #3—Revenues

($ millions)

Product	Amount
Zyprexa	$4,277
Humulin	1,060
Gemzar	1,022
Humalog	1,021
Evista	922
Prozac/Sarafem/Prozac Weekly	645
Actos	431
Humatrope	371
Strattera	370
ReoPro	364

With the launch of Strattera, we now have 10 products with annual net revenues in excess of $300 million. Four of these products — Zyprexa, Humulin, Gemzar, and Humalog — had net revenues in excess of $1 billion in 2003 and Zyprexa became our first product with net sales in excess of $4 billion.

Graph #4—Gross Margin

(as a percent of total net sales)

Year	Percent
99	79.0%
00	81.1%
01	81.3%
02	80.4%
03	78.7%

Gross margin as a percent of sales decreased by 1.7 percentage points to 78.7 percent. This decline was primarily due to continued quality improvements, capacity growth in our manufacturing operations, and the impact of foreign exchange rates, offset partially by favorable changes in product mix due to growth in higher margin products such as Zyprexa, Gemzar, Evista, and the newly launched Strattera.

Graph #5—Research and Development

($ millions; percent of net sales)

Year	Amount	Percent
94	$ 838.7	14.7
95	1,042.3	16.0
96	1,189.5	17.0
97	1,370.2	17.2
98	1,738.9	18.8
99	1,783.6	17.8
00	2,018.5	18.6
01	2,235.1	19.4
02	2,149.3	19.4
03	2,350.2	18.7

Research and development expenditures increased by 9 percent, to $2.4 billion, in 2003. At 19 percent of net sales, we continue to lead our industry peer group in reinvesting proceeds from sales in further research and development. This significant financial investment in our pipeline of products supports our commitment to develop best-in-class and first-in-class medicines to provide answers for the unmet medical needs of our customers.

Graph #6—Capital Expenditures

($ millions)

Year	Amount
99	$ 528.3
00	677.9
01	884.0
02	1,130.9
03	1,706.6

Capital expenditures increased 51 percent from 2002. The continued heavy investment supported various manufacturing and research initiatives and related infrastructure. In 2004, the company expects near-term capital expenditures to increase from 2003 levels to prepare for the growth of our diabetes care products, future products in development, and expanded research and development activities.

Graph #7—Dividends Paid Per Share

(dollars)

Year	Amount
99	$0.92
00	1.04
01	1.12
02	1.24
03	1.34

Dividends paid during 2003 increased to $1.34 per share. This constitutes the 36th consecutive increase in annual dividends. The company also continues this tradition into 2004 by declaring a first-quarter 2004 dividend of $.355 per share, a 6 percent increase over first-quarter 2003. This record clearly reflects the company’s continued commitment to delivering outstanding shareholder value.

Graph #8—Return on Shareholders’ Equity

(based on income from continuing operations divided by average shareholders’ equity)

Year	Percent
94	23.8%
95	26.1%
96	28.2%
97	37.5%
98	46.0%
99	53.9%
00	55.3%
01	42.3%
02	35.2%
03	28.4%

Return on shareholders’ equity declined in 2003, to 28.4 percent. This decline is primarily attributable to significant investments in sales and marketing activities in support of our existing key growth products and to prepare for anticipated product launches. We also made substantial investments in our manufacturing operations and research and development activities.

EXHIBIT 21-LIST OF SUBSIDIARIES AND AFFILIATES

THE FOLLOWING ARE THE SUBSIDIARIES AND AFFILIATED CORPORATIONS OF THE COMPANY AT DECEMBER 31, 2003
CERTAIN SUBSIDIARIES HAVE BEEN OMITTED SINCE THEY ARE NOT SIGNIFICANT IN THE AGGREGATE.

	STATE OR JURISDICTION OF INCORPORATION OR ORGANIZATION
ELI LILLY AND COMPANY	INDIANA
ELI LILLY INTERAMERICA, INC.	INDIANA
ELI LILLY DO BRASIL LIMITADA	BRAZIL
ELANCO QUIMICA LIMITADA	BRAZIL
ELI LILLY INTERAMERICA INC., Y COMPANIA LIMITADA	CHILE
STC PHARMACEUTICALS, INC.	INDIANA
LILLY ICOS L.L.C.	DELAWARE
SCIENTEUR CORPORATION	INDIANA
INNOCENTIVE, INC	DELAWARE
LE HESTON ENERGY, LLC	DELAWARE
DISTA, INC.	INDIANA
ELI LILLY DE CENTRO AMERICA, S.A.	GUATEMALA
ELI LILLY DE CENTRO AMERICA, SOCIEDAD ANONIMA	COSTA RICA
ELI LILLY Y COMPANIA DE MEXICO, S.A. DE C.V.	MEXICO
DISTA MEXICANA, S.A. DE C.V.	MEXICO
ELI LILLY DE MEXICO, S.A. DE C.V.	MEXICO
ELI LILLY INDUSTRIES, INC.	DELAWARE
DEL SOL FINANCIAL SERVICES, INC.	BRITISH V.I.
LILLY DEL CARIBE, INC.	CAYMAN ISLS.
VOLIRA INVESTMENT CO.	CAYMAN ISLS.
GENESIS MERGER SUB, INC.	DELAWARE
CONTROL DIABETES SERVICES, INC.	INDIANA
INTEGRATED MEDICAL SYSTEMS, INC.	COLORADO
ELCO DOMINICANA, S.A.	DOMINICAN REP.
ELCO INTERNATIONAL SALES CORPORATION	VIRGIN IS.-US
ELI LILLY FINANCE S.A.	SWITZERLAND
LILLY DEL MAR, INC.	BRITISH VIRGIN ISLANDS
LILLY GLOBAL SERVICES, INC.	INDIANA
LILLY SYSTEMS BIOLOGY PTE LTD	SINGAPORE
ELI LILLY SPAIN HOLDING ETVE, S.L.	SPAIN
ELI LILLY NEDERLAND HOLDING B.V.	NETHERLANDS
ELI LILLY AND COMPANY (TAIWAN), INC.	TAIWAN
ELI LILLY HOLDING COMPANY LTD.	UK
ELI LILLY HOLDING GMBH	GERMANY
ELI LILLY FUNDING LTD.	HONG KONG
ELI LILLY INTERNATIONAL CORPORATION	INDIANA
ELI LILLY IRAN, S.A.	IRAN
ELCO INSURANCE COMPANY, LTD.	BERMUDA
ELI LILLY HOLDINGS LTD	ENGLAND
ELI LILLY GROUP LIMITED	ENGLAND
ELI LILLY & CO. LTD.	ENGLAND
DISTA PRODUCTS LIMITED	ENGLAND
ELI LILLY & CO (IRELAND) TRUSTEE LIMITED	IRELAND
LILLY INDUSTRIES LIMITED	ENGLAND
LILLY RESEARCH CENTRE LIMITED	ENGLAND
ELANCO PRODUCTS LIMITED	ENGLAND
CREATIVE PACKAGING LIMITED	ENGLAND
GREENFIELD PHARMACEUTICALS LIMITED	ENGLAND
ELI LILLY (BASINGSTOKE) LIMITED	ENGLAND
ELI LILLY LEASING LIMITED	ENGLAND
LILLY RESOURCES LIMITED	ENGLAND
ELI LILLY RESOURCES LIMITED	ENGLAND
LILLY PROPERTY LIMITED	ENGLAND
ELI LILLY PROPERTY LIMITED	ENGLAND
ELI LILLY AND COMPANY SPEKE OPERATIONS LLP	ENGLAND
ELI LILLY GROUP PENSION TRUSTEES LIMITED	ENGLAND
LILLY PHARMA HOLDING GMBH	GERMANY
LILLY DEUTSCHLAND GMBH	GERMANY

LILLY PHARMA FERTIGUNG & DISTRIBUTION GMBH	GERMANY
LILLY PHARMA PRODUKTION GMBH & CO. KG	GERMANY
LILLY FORSCHUNG GMBH	GERMANY
ELI LILLY GES.M.B.H.	AUSTRIA
LILLY GMBH	GERMANY

EXHIBIT 21-LIST OF SUBSIDIARIES AND AFFILIATES

THE FOLLOWING ARE THE SUBSIDIARIES AND AFFILIATED CORPORATIONS OF THE COMPANY AT DECEMBER 31, 2003
CERTAIN SUBSIDIARIES HAVE BEEN OMITTED SINCE THEY ARE NOT SIGNIFICANT IN THE AGGREGATE.

	STATE OR JURISDICTION OF INCORPORATION OR ORGANIZATION
ELI LILLY AND COMPANY (CONTINUED)	
ELI LILLY INTERNATIONAL CORPORATION (CONTINUED)	
ELI LILLY HOLDINGS LTD (CONTINUED)	
ELI LILLY DANMARK A/S	DENMARK
OY ELI LILLY FINLAND AB	FINLAND
ELI LILLY NORGE A.S.	NORWAY
ELI LILLY & CO. (IRELAND) LIMITED	IRELAND
ELI LILLY SWEDEN AB	SWEDEN
LILLY TURKEY A.S.	TURKEY
LILLY HK FINANCE I, LLC	HONG KONG
LILLY HK FINANCE II, LLC	HONG KONG
ELI LILLY FUNDING PARTNERSHIP	HONG KONG
ELI LILLY FUNDING PARTNERSHIP II	HONG KONG
ELI LILLY ASIA, INC.	DELAWARE
ELI LILLY AUSTRALIA PTY. LIMITED	AUSTRALIA
ELI LILLY AUSTRALIA CUSTODIAN PTY. LIMITED	AUSTRALIA
ELI LILLY AND COMPANY (N.Z.) LIMITED	NEW ZEALAND
ELI LILLY (NZ)STAFF BENEFITS CUSTODIAN LIMITED	NEW ZEALAND
INTEGRATED DISEASE MANAGEMENT (NZ) LIMITED	NEW ZEALAND
E L MANAGEMENT INCORPORATED	DELAWARE/NOVA SCOTIA
ELI LILLY CANADA INC.	CANADA
ELI LILLY S.A.	SWITZERLAND
ELI LILLY EXPORT S.A.	SWITZERLAND
GEMS SERVICES, S.A.	BELGIUM
ELANCO TRUSTEES LIMITED	IRELAND
KINSALE FINANCIAL SERVICES, LTD.	IRELAND
ELI LILLY (SUISSE) S.A.	SWITZERLAND
ELI LILLY VOSTOK SA, GENEVA	SWITZERLAND
OLDFIELDS FINANCIAL MANAGEMENT S.A.	SWITZERLAND
ELI LILLY SUZHOU PHARMACEUTICAL COMPANY LIMITED	CHINA
ELGO INSURANCE COMPANY LIMITED	BERMUDA
ELI LILLY NEDERLAND B.V.	NETHERLANDS
LILLY DEVELOPMENT CENTRE S.A.	BELGIUM
LILLY SERVICES S.A.	BELGIUM
LILLY CLINICAL OPERATIONS S.A.	BELGIUM
ELI LILLY CR S.R.O.	CZECH REPUB.
ELI LILLY SLOVAKIA S.R.O.	SLOVAKIA
ELI LILLY REGIONAL OPERATIONS GMBH	AUSTRIA
ELI LILLY EGYPT	EGYPT
ELCO FOR TRADE AND MARKETING SAE	EQYPT
PARXNER B.V.	NETHERLANDS
DISTA ILAC TICARET LTD STI	TURKEY
ELCO PARTICIPATION, SARL	FRANCE
LILLY FRANCE S.A.S	FRANCE
ELSA FRANCE, S.A.	FRANCE
LICO SARL	FRANCE
ELI LILLY ITALIA S.P.A.	ITALY
ELI LILLY BENELUX, S.A.	BELGIUM
DISTA-PRODUTOS QUIMICOS & FARMACEUTICOS,LDA	PORTUGAL
LILLY-FARMA, PRODUTOS FARMACEUTICOS, LDA.	PORTUGAL
VITAL FARMA PRODUCTOS FARMACEUTICOS	PORTUGAL
DISTA ITALIA S.R.L.	ITALY
PHARMASERVE - LILLY S.A.C.I.	GREECE
PHARMABRAND, S.A.C.I.	GREECE
PRAXICO LTD.	HUNGARY
LILLY HUNGARIA KFT	HUNGARY
ELI LILLY (PHILIPPINES), INCORPORATED	PHILIPPINES
ELI LILLY AND COMPANY (INDIA) PVT. LTD.	INDIA
ELI LILLY ISRAEL LTD.	ISRAEL

ELI LILLY JAPAN K.K.	JAPAN
ELI LILLY ASIAN OPERATIONS, LIMITED	HONG KONG, PRC
LILLY KOREA LTD.	KOREA
ELANCO ANIMAL HEALTH, KOREA, LTD.	KOREA
ELI LILLY MALAYSIA SDN BHD.	MALAYSIA
ELI LILLY MAROC S.A.R.L.	MOROCCO

EXHIBIT 21-LIST OF SUBSIDIARIES AND AFFILIATES

THE FOLLOWING ARE THE SUBSIDIARIES AND AFFILIATED CORPORATIONS OF THE COMPANY AT DECEMBER 31, 2003
CERTAIN SUBSIDIARIES HAVE BEEN OMITTED SINCE THEY ARE NOT SIGNIFICANT IN THE AGGREGATE.

	STATE OR JURISDICTION OF INCORPORATION OR ORGANIZATION
ELI LILLY AND COMPANY (CONTINUED)	
E L MANAGEMENT INCORPORATED (CONTINUED)	
ELI LILLY S.A. (CONTINUED)	
ELI LILLY NEDERLAND B.V. (CONTINUED)	
TDM BV	NETHERLANDS
ANDEAN TECHNICAL OPERATIONS CENTER	PERU
LILLY PHARMA LTD.	RUSSIA
ELI LILLY PAKISTAN (PVT.) LTD.	PAKISTAN
ELI LILLY POLSKA SP. Z.O.O. (LTD.)	POLAND
VITALIA PHARMA SP. Z.O.O.	POLAND
ELI LILLY SINGAPORE PTE. LTD.	SINGAPORE
LILLY-NUS CENTRE FOR CLINICAL PHARMACOLOGY PTE. LTD.	SINGAPORE
ELI LILLY (S.A.) (PROPRIETARY) LIMITED	SOUTH AFRICA
ELANCO-VALQUIMICA, S.A.	SPAIN
DISTA, S.A.	SPAIN
LILLY, S.A.	SPAIN
SPALY BIOQUIMICA, S.A.	SPAIN
IRISFARMA S.A.	SPAIN
ELI LILLY NIGERIA LTD.	NIGERIA
ELI LILLY Y COMPANIA DE VENEZUELA, S.A.	VENEZUELA
DISTA PRODUCTS & COMPANIA VENEZUELA S.A.	VENEZUELA

EXHIBIT 23. CONSENT OF INDEPENDENT AUDITORS

We consent to the incorporation by reference in this Annual Report (Form 10-K) of Eli Lilly and Company of our report dated February 2, 2004, included in the 2003 Annual Report to Shareholders of Eli Lilly and Company.

We also consent to the incorporation by reference in the following registration statements of our report dated February 2, 2004, with respect to the consolidated financial statements incorporated by reference in the 2003 Annual Report (Form 10-K) of Eli Lilly and Company:

Registration Statement No.	Type of Statement	Date
33-29482	S-8	June 23, 1989
33-37341	S-8	October 17, 1990
33-58466	S-3	February 17, 1993
33-50783	S-8	October 27, 1993
33-56141	S-8	October 24, 1994
333-02021	S-8	March 28, 1996
333-62015	S-8	August 21, 1998
333-66113	S-8	October 26, 1998
333-90397	S-8	November 5, 1999
333-35248	S-3	April 20, 2000
333-70308	S-8	September 27, 2001
333-104057	S-8	March 27, 2003
333-106478	S-3/A	September 16, 2003

/s/ Ernst & Young LLP

Ernst & Young LLP

Indianapolis, Indiana
March 12, 2004

EXHIBIT 31.1 Rule 13a-14(a) Certification of Sidney Taurel, Chairman of the Board, President, and Chief Executive Officer

CERTIFICATIONS

I, Sidney Taurel, chairman of the board, president, and chief executive officer, certify that:

1. I have reviewed this report on Form 10-K of Eli Lilly and Company;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: March 11, 2004

By: /s/ SIDNEY TAUREL

Sidney Taurel
Chairman of the Board, President,
and Chief Executive Officer

EXHIBIT 31.2 Rule 13a-14(a) Certification of Charles E. Golden, Executive Vice President and Chief Financial Officer

CERTIFICATIONS

I, Charles E. Golden, executive vice president and chief financial officer, certify that:

1. I have reviewed this report on Form 10-K of Eli Lilly and Company;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: March 11, 2004

By: /s/ CHARLES E. GOLDEN

Charles E. Golden
Executive Vice President
and Chief Financial Officer

EXHIBIT 32. Section 1350 Certification

Pursuant to section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of section 1350, chapter 63 of title 18, United States Code), each of the undersigned officers of Eli Lilly and Company, an Indiana corporation (the "Company"), does hereby certify that, to the best of their knowledge:

The Annual Report on Form 10-K for the year ended December 31, 2003 (the "Form 10-K") of the Company fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 and information contained in the Form 10-K fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date March 11, 2004

/S/ Sidney Taurel

Sidney Taurel
Chairman of the Board, President, and
Chief Executive Officer

Date March 11, 2004

/S/ Charles E. Golden

Charles E. Golden
Executive Vice President and
Chief Financial Officer

A signed original of this written statement required by Section 906 has been provided to Eli Lilly and Company and will be retained by Eli Lilly and Company and furnished to the Securities and Exchange Commission or its staff upon request.

EXHIBIT 99. Cautionary Statement Under Private Securities Litigation Reform Act of 1995 – “Safe Harbor” for Forward-Looking Disclosures

Certain forward-looking statements are included in this Form 10-K and may be made by spokespersons based on then-current expectations of management. All forward-looking statements made by us are subject to risks and uncertainties. One can identify forward-looking statements by the use of words such as “expects,” “plans,” “will,” “estimates,” “forecasts,” “projects,” “believes,” “anticipates,” and other words of similar meaning. One can also identify them by the fact that they do not relate strictly to historical or current facts. These statements are likely to address our growth strategy, financial results, regulatory issues, and status of product approvals, development programs, litigation, and investigations.

Certain factors, including but not limited to those listed below, may cause actual results to differ materially from current expectations and historical results.

- competitive factors, including new patented products or expanded indications for existing products introduced by competitors, which can lead to declining demand for our products; generic competition as patents on key products expire; and pricing pressures, both in the U.S. and abroad, primarily from managed care groups and government agencies

- governmental factors, including federal, state, and foreign laws and regulations that affect pharmaceutical pricing, such as Medicaid, Medicare, pharmaceutical importation laws, and other laws and regulations that could, directly or indirectly, impose governmental controls on the prices at which our products are sold

- the difficulties and uncertainties inherent in new product development and introduction of new products. New product candidates that appear promising in development may fail to reach the market or may have only limited commercial success because of efficacy or safety concerns, inability to obtain necessary regulatory approvals, difficulty or excessive costs to manufacture, or infringement of the patents or intellectual property rights of others. In addition, it can be very difficult to predict sales growth rates of new products

- delays and uncertainties in the FDA approval process and the approval processes in other countries, resulting in delays in product launches and lost market opportunity

- unexpected safety or efficacy concerns arising with respect to marketed products, whether or not scientifically justified, leading to product recalls, withdrawals, or declining sales

- changes in inventory levels maintained by pharmaceutical wholesalers that can cause reported sales for a particular period to differ significantly from underlying prescriber demand

- patent challenges, including challenges to our patents by generic pharmaceutical manufacturers under the Hatch Waxman Act or patent infringement suits brought against us by other patent holders, that could cause us to lose market exclusivity for, or preclude commercialization of, our products

- regulatory issues concerning compliance with current Good Manufacturing Practice (cGMP) regulations for pharmaceutical products that can lead to product recalls and seizures, interruption of production, and delays in the approvals of new products pending resolution of the cGMP issues

- other legal factors, including product liability or other liability claims, marketing and promotional practices investigations, antitrust and pricing litigation, and environmental matters

- changes in tax laws, including laws related to the remittance of foreign earnings or investments in foreign countries with favorable tax rates, and settlements of federal, state, and foreign tax audits

- economic factors over which we have no control, including changes in inflation, interest rates and foreign currency exchange rates, and overall economic conditions in volatile areas, such as Latin America

- changes in accounting standards promulgated by the Financial Accounting Standards Board, the Securities and Exchange Commission, the American Institute of Certified Public Accountants, and the Emerging Issues Task Force

- internal factors, such as changes in business strategies and the impact of restructurings, asset impairments, technology acquisition and disposition transactions, and business combinations.

We undertake no duty to update forward-looking statements.