

PROCYTE

C O R P O R A T I O N

2 0 0 3 A N N U A L R E P O R T

PERFECTING THE SCIENCE OF SKIN CARE



2003 HIGHLIGHTS

Years ended December 31, (in thousands, except per share amounts)

Statement of Operations Data	2003	2002	2001	2000	1999
Revenue	\$11,538	\$12,737	\$9,712	\$6,615	\$4,695
Gross profit	8,337	8,031	6,128	5,116	3,319
Operating expenses	8,272 ^(A)	6,561	7,188	7,481	8,883 ^(B)
Interest and other income	194	199	153	222	249
Income tax benefit	7,082	—	—	—	—
Net income (loss)	\$7,341	\$1,669	\$(907)	\$(2,143)	\$(5,315)
Net earnings (loss) per diluted share:	\$0.46	\$0.10	\$(0.06)	\$(0.14)	\$(0.35)
Shares used in diluted per share computation:	15,997	16,179	15,610	15,481	14,999

^(A)Includes a \$750,000 loss on asset impairment.

^(B)Includes a \$1.9 million write down of manufacturing facility.

December 31, (in thousands)

Balance Sheet Data	2003	2002	2001	2000	1999
Cash, cash equivalents	\$3,796	\$4,556	\$3,003	\$2,773	\$3,883
Current assets	8,363	7,931	6,506	6,451	5,454
Total assets	20,003	14,089	12,811	12,185	13,447
Current liabilities	692	963	1,147	1,179	416
Total liabilities	785	2,271	2,743	1,324	558
Stockholders' equity	\$19,218	\$11,818	\$10,068	\$10,861	\$12,889



DEAR SHAREHOLDERS



As I report on our results and activities for 2003, we are already three months into the following year. We accomplished a number of important milestones during 2003. We licensed a rosacea technology, acquired a spa distribution business, filed three new patent applications, revamped the sales

organization and added several new products. Overall, we have strengthened our Company and we ended the year in a stronger position than we began the year. If one thought comes to mind to describe our activities in 2003, it is that we tried to do too many things at once with too few people. Also, the significant additional reporting and compliance requirements brought on by the Sarbanes-Oxley Act and changing regulatory environment continues to require more management time and increase compliance costs.

I would like to begin my 2003 report by referring to a December 2002 meeting between the Board of Directors and Company management that discussed the overall business and strategic focus of ProCyte Corporation. At this session, a series of strategic and business goals and objectives were established. Some of the goals and objectives plus our results are as follows:

WE SAW POSITIVE RESULTS FROM OUR EFFORTS IN THE SECOND HALF OF THE YEAR.

■ **ProCyte should retain an investment banking group by the first quarter to locate and acquire synergistic businesses or products to add revenue, technology or market access.** We signed with Delafield-Hambrecht in February 2003. We reviewed a large number of companies and met with several of them during the following six months. The Delafield relationship ended in September. We retained Wells Fargo Securities in January 2004 as our new investment banking representatives and have an active program underway with them. We acquired a spa distribution business to gain direct access to the rapidly growing spa markets.

■ **ProCyte should commit the necessary resources to complete and launch a successful Infomercial.** We completed the Infomercial and initiated the first market test in March. We made a number of changes to the program and launched another test in late July and early August. When the results were still not acceptable, we made the decision to stop all work on the Infomercial. The Infomercial added over \$770,000 in expenses to our 2003 results, an impact reduction of \$.05 per diluted share.

■ **ProCyte should locate an additional technology to integrate into its marketing efforts to accelerate revenue growth.** During the year we identified the Quadrinone® technology from Cutanix Corporation being marketed under the brand Dramatic Relief™ for individuals with rosacea. We signed a distribution agreement in June 2003 and launched the products in August.

■ **ProCyte should make every effort to regain its listing on a national stock exchange.** This goal is one of our most important and perhaps the most difficult goal. We remain in compliance with all corporate governance requirements and are in position to move onto an exchange in all respects except for share price. We continue to search for appropriate ways to achieve being listed on an exchange that will enhance shareholder value.

■ **ProCyte needs to increase sales representative productivity.** We have taken a number of steps to address this issue including changing our hiring profile, increasing sales training and expanding customer education programs. Some territories were reduced in size, others were closed and new territories were formed in locations with greater potential. We saw positive results from our efforts in the second half of the year. We dedicated one of our customer service representatives to telemarketing activities in October.

■ **ProCyte should increase international activities and revenues.** We hired a dedicated Director of International Sales to focus in this area. We are already seeing progress in the international area and have positive expectations for the next several years.

■ **ProCyte needs to expand its patent portfolio.** Three new patent applications were filed in 2003. This brings the total number to 10 new patent applications filed over the last three years. We believe that these patents, when they issue, will be valuable in our efforts to protect our franchise and increase our license opportunities.

■ **ProCyte needs to sign one or more new consumer partners for skin care.**

We continue to seek partners in several distribution channels for our technology and products.



We believe that some of the development efforts that we have underway with other peptides and our patent applications could lead to new partners in market segments that we currently do not address.

We have made excellent progress in 2003 in accomplishing goals or moving the goals forward. We expect to see the benefits in terms of revenues and earnings beginning in 2004.

Revenues started slowly in the first half of 2003 based on a number of factors including a slower economy, war and general consumer uncertainty. The Women's Wear Daily, December 12, 2003 issue reported "the past two years were very difficult sales years in the prestige and mass retail markets. The combination of recession, SARs, Iraq war, and bad weather in first half of 2003 caused an unprecedented slowdown." Early signs in 2004 indicate a more favorable climate with increasing sales.

During the year, we retained a sales training consultant with the mission of upgrading our sales representatives selling skills. A product training consultant was hired in June 2003 and we re-introduced customer education seminars, with eight programs conducted in 2003. These programs were well received and filled to capacity. We have scheduled ten programs for 2004. In addition, we attended over 35 trade shows and conducted over 200 customer trainings, in-service sessions or local patient education programs during 2003. Through the actions noted above, we have seen a reversal of these trends in the second half of 2003.

We experienced turnover in the Director of International Sales position during 2003, keeping us from reaching our expected potential in the international market. Our new Director of International Sales started in December 2003, and we now seem to be back on track and see a bright future. In the last several months, we have added several new international distributors and have ongoing requests to represent our products.

In September, we introduced Neova® Therapy Creme de la Copper as a line extension to our highly successful Neova® Therapy line of anti-aging skin care products for the dispensing physician. The product has been popular and we are seeing excellent sales results. A follow-on product, Neova® Therapy Dual Action Lotion with GHK Copper Peptide Complex® + Retinol was launched on March 1st 2004. And in April 2004, we will launch Ti-Silc® Scalp Defense™, a spray sunscreen we developed specifically for individuals with thinning hair. This product is ideal for golfers and people who enjoy outdoor activities. It is a nice complement to our skin care, hair care and hair transplant products categories.



In December, we completed the acquisition of a company focused on serving the spa market. The past several years have

seen an accelerating trend of medi-spa formation blurring the line between the physician's office and the traditional day spa. A key player in all these markets is the esthetician. ProCyte's move into the spa market helps capture the patient/consumer and the esthetician at each point of contact. We look forward to increasing our revenues in this category during the year. We have already added several new sales representatives who will be responsible for building the business in high end and prestige spa locations.

In late January 2004, we were informed that Emerald Pharmaceutical, LP had experienced significant customer delays in current and expected orders and therefore revenues were not going to provide sufficient cash to last beyond the current quarter. After a review of the facts available, it was determined that the Company should record a charge against 2003 earnings of \$637,000 or \$0.04 per diluted share. The Company also recognized an income tax benefit of \$7.1 million or \$0.44 per diluted share related to the reversal of a portion of its valuation allowance to properly reflect its deferred tax asset.

Total revenues for the year decreased by \$1.2 million as a result of lower purchases of Copper Peptide compound, a reduction of \$1.5 million in sales, partially offset by an increase in royalties and virtually flat product sales for the year. Operating expenses for the year increased by \$1.8 million primarily as a result of the \$770,000 expenditure for the Infomercial and the \$637,000 asset impairment charge. Excluding these items, expenses on a year over year basis only increased by 5%.

Net earnings for the year were \$7.3 million or \$0.46 per diluted share. This figure was impacted by the \$7.1 million income tax credit benefit, \$637,000 impairment charge and the \$770,000 Infomercial costs included in the year, without which would have made 2003 results directly in line with our 2002 net earnings.

During the year there are always numerous activities that the management and employees pursue to grow the business. It is impossible to recognize everything that happens on a daily basis except to say that we are moving in the right direction, profitable, generating cash and remain debt free. We feel that we are in a very good position to maintain the second half of 2003 momentum into 2004 and beyond. I want to thank our dedicated group of employees who are focused on servicing our customers, growing the business and increasing shareholder value.

A handwritten signature in black ink that reads "Jack Clifford". The signature is written in a cursive, flowing style.

Jack Clifford
Chairman and Chief Executive Officer
March 24, 2004

CAPTURING MARKET OPPORTUNITIES

The U.S. Professional Skin Care Market is estimate at more than \$500 million at the manufacturer level, growing at nearly 10% per year over the past five years.*

Spas and Salons account for nearly 65% of the total market for professional products.*



ProCyte is in the position to capitalize on this rapidly growing market with the acquisition of Annette Hanson, Inc., a spa distribution business.

80 Million American Men and Women are affected with thinning or balding hair.

ProCyte offers consumers a clinically proven way with copper peptide to combat thinning hair.



It is estimated that there will be 95,880 new cases of Melanoma in 2004.**



ProCyte provides the physician market the preventative tool of advanced sun protection to help save lives.

BUILDING STRONG BRANDS

Healing Lifestyles & Spas, January/February 2004 'Heavy Metal Skincare'

"Beware! Not all copper peptides are the same. One cannot simply melt pennies (or copper salts) and blend them into cream. Copper must be technologically melded into a format which mimics the body's copper transport mechanisms. Healthcare authority ProCyte introduced a high-tech patented version of copper peptides to the public three years ago in three different formulas — Simple Solutions for spas, Neova for medical professionals, and Johnson & Johnson's (Neutrogena's Visibly Firm) for the mass market."

Good Housekeeping, April 2003 'Bedtime Beauty'

"Smooth Crepey Lids...Heavy creams can cause whiteheads to form on the thin skin of your eyelids. For that area, many doctors like Neova Eye Therapy, a light gel with a GHK copper peptide to help rebuild collagen..."

More, July/August 2003 'How to Hide it, Flaunt it, Fake it'

"Liz Cullumber, 55: I have very thin, fragile skin, so I use gentle, non-acid products no matter what the latest skin-care rage is. ...ProCyte Ti-Silc Sheer Sunblock SPF 45, which is creamy, is my staple."

InStyle, July 2003 '24 Summer Beauty Solutions'

"...What physical sunblock won't leave me looking pasty? Search for products with micronized zinc oxide, which delivers the broadest protection available against UVA and UVB rays and leaves little telltale white cast. We found Z-Silc Sunblock SPF 30 to be the sheerest."

Aesthetic Buyers Guide, July/August 2003 'Competition Drives Innovation in Antiaging Cosmeceuticals'

"Neova Antioxidant Therapy Serum from ProCyte Corporation is specifically formulated with the company's patented GHK Copper Peptide Complex, along with a potent combination of antioxidants to promote healthy skin while protecting it against free radicals. ..."

Cosmetic Dermatology, March 2003 'Cosmeceuticals: A Review of the Science Behind the Claims'

"...Results of industry-sponsored studies by Leyden et al showed a favorable response to topically applied creams containing copper peptides. ...a cream containing copper peptide, applied twice daily for 12 weeks, statistically significantly improved surface roughness, fine lines, wrinkles, and overall photo damage..."

Aesthetic Buyers Guide, March/April 2003 'Product Innovation Flourishes at AAD Annual Meeting'

"The Neova Copper Moisture Mask from ProCyte Corporation is an intensive GHK Copper Peptide Complex concentration designed for in-office facial treatments. 'A number of physicians are now also using the product as an application gel for facial ultrasound treatments'..."

AARP, March/April 2004 'Smoothies — These remarkable face creams really can turn back the clock'

"Copper peptide has been shown in studies to stimulate the cells to make more collagen."

SHAREHOLDER INFORMATION

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303-262-0709

SHAREHOLDER INQUIRIES

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ANNUAL MEETING OF THE SHAREHOLDERS

May 19, 2004 9:00 AM
Doubletree Hotel
300-112th Avenue Southeast
Bellevue, WA 98004

INDEPENDENT AUDITORS

Deloitte and Touche, LLP

GENERAL COUNSEL

Perkins Coie, LLP

EXECUTIVES

John F. Clifford
*Chairman of the Board and Chief
Executive Officer, Treasurer*

Robin L. Carmichael
*Vice President of Marketing,
Corporate Officer*

Robert W. Benson
Chief Financial Officer, Secretary

DIRECTORS

John M. Hammer
*Director, Chairman Nominating
Committee, Audit & Compensation
Committee Member*

Matt L. Leavitt, D.O.
*Director, Chairman Compensation
Committee, Nominating Committee
Member*

Robert E. Patterson
*Director, Chairman Audit Committee,
Nominating & Compensation
Committee Member*

TRADEMARKS

Neova, Ti-Silc, Z-Silc, Complex Cu3, GraftCyte, TricomIn, Simple Solutions, AquaSanté, NextDerm, GHK Copper Peptide Complex, AHK Copper Peptide Complex, Healing The Wounds Of Time, Ultra Copper, Pure Copper and Blemish Begone are registered trademarks of ProCyte Corporation. Ti-Tan, Scalp Defense, Triamino Copper Nutritional Complex and VitalCopper are trademarks of ProCyte Corporation.

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