This English translation has been prepared for convenience only. The original German version is the only version that is legally binding.

Listing Memorandum

for admission to trading on the official market segment (*amtlicher Markt*) and, simultaneously, the
official market sub-segment entailing additional post-admission obligations (Prime Standard)
of the Frankfurt Stock Exchange

of

73,034,192 no par value ordinary bearer shares (no-par shares)
(entire capital stock),

each such no-par share currently representing a €1.00 portion of the capital stock and carrying full dividend rights from 1 January 2004

consisting of

50,000 no par value ordinary bearer shares (no-par shares)
(existing capital stock)

and

72,984,192 no par value ordinary bearer shares (no-par shares)
issued in connection with the capital increase against contribution in kind, which was resolved upon at the Stockholders' Meeting on 21 December 2004, in order to implement the spin-off (expected to be registered with the Commercial Register on 28 January 2005) of Bayer Aktiengesellschaft's equity interest in LANXESS Deutschland GmbH, in which (directly and through subsidiaries) certain chemicals and polymers activities of the Bayer Group were combined, and of other assets and liabilities of Bayer Aktiengesellschaft to LANXESS Aktiengesellschaft pursuant to resolutions of the Extraordinary Stockholders' Meeting of Bayer Aktiengesellschaft held on 17 November 2004 and of LANXESS Aktiengesellschaft held on 21 December 2004
(Spin-off pursuant to the German Transformation Act)

of

LANXESS Aktiengesellschaft
Leverkusen

International Securities Identification Number (ISIN): DE0005470405
German Securities Identification Code (WKN): 547040
Common Code: 020904992

18 January 2005

Deutsche Bank **Morgan Stanley**

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General Information

Creation of LANXESS

LANXESS is a corporate group newly formed as a result of the spin-off (hereinafter referred to as the ''Spin-off'') from Bayer Aktiengesellschaft, Leverkusen (''Bayer AG''). The ultimate parent company of this group is LANXESS Aktiengesellschaft (hereinafter also referred to as the ''Company'' or ''LANXESS AG'' and referred to as ''LANXESS'', the ''LANXESS Group'' or the ''Group'' together with its direct and indirect consolidated holdings within the group structure after the Spin-off from Bayer AG to LANXESS AG takes effect), the operating business of which has been consolidated into LANXESS Deutschland GmbH, Leverkusen (hereinafter referred to as ''LANXESS GmbH'') and its subsidiaries.

At present, LANXESS AG is still a wholly-owned subsidiary of Bayer AG. LANXESS GmbH — in which the majority of the Bayer Group's chemicals activities and approximately one third of the Bayer Group's polymers activities were consolidated either directly or through subsidiaries — is also currently a wholly-owned subsidiary of Bayer AG. By virtue of a spin-off and acquisition agreement dated 22 September 2004 (hereinafter referred to as the ''Spin-off Agreement''), Bayer AG, as the transferring entity, and LANXESS AG, as the acquiring entity, agreed to transfer to LANXESS AG the equity interests of Bayer AG in LANXESS GmbH and LANXESS AG, together with other assets and liabilities, by way of a spin-off pursuant to section 123 (2) No. 1 of the German Transformation Act (*Umwandlungsgesetz,* hereinafter also referred to as ''UmwG''). In return for this transfer, all of LANXESS AG's no par value ordinary bearer shares (no-par shares) will be granted to the stockholders of Bayer AG. One ordinary bearer share of LANXESS AG will be issued for every ten Bayer AG shares. The Extraordinary Stockholders' Meetings of Bayer AG and LANXESS AG approved the Spin-off Agreement on 17 November 2004 and 21 December 2004, respectively. The Spin-off will become effective once it is registered in the Commercial Register (*Handelsregister*) for Bayer AG at the Local Court of Cologne (*Amtsgericht Köln*), which is anticipated to occur on 28 January 2005. See also ''*Further Details and Explanation of the LANXESS Spin-off*''.

Responsibility for the Content of the Listing Memorandum

LANXESS AG, Deutsche Bank Aktiengesellschaft, Frankfurt am Main (''Deutsche Bank'') and Morgan Stanley Bank AG, Frankfurt am Main (''Morgan Stanley'', also referred to jointly with Deutsche Bank as the ''Global Co-ordinators'') assume responsibility pursuant to sections 44 *et seq.* of the German Stock Exchange Act (*Börsengesetz*) for the contents of this listing memorandum (the ''Listing Memorandum'') and hereby declare that, to their knowledge, the information set forth in this Listing Memorandum is correct and that no material facts have been omitted.

Inspection of Documents

The joint spin-off report of the Boards of Management of Bayer AG and of LANXESS AG (the ''Joint Spin-off Report''), the auditor's report on the spin-off by the court-appointed joint spin-off auditor Stüttgen & Haeb AG, Wirtschaftsprüfungsgesellschaft, Dusseldorf, the report of PwC Deutsche Revision Aktiengesellschaft, Wirtschaftsprüfungsgesellschaft, with respect to audits on the post-formation acquisition (*Nachgründung*) and the capital increase conducted at LANXESS Aktiengesellschaft, as well as the documents to be made available pursuant to section 18 No. 6 of the German Stock Exchange Listing Regulations (*Börsenzulassungsverordnung*), may be inspected during regular business hours at the offices of the Company located at Building K 10, Kaiser-Wilhelm-Allee 1, 51369 Leverkusen, at the offices of Deutsche Bank located at Taunusanlage 12, 60325 Frankfurt am Main and at the offices of Morgan Stanley located at Junghofstrasse 13-15, 60311 Frankfurt am Main. The Company's future annual reports and interim reports will be available from the Company and the paying agent named in this Listing Memorandum (see ''*General Information on LANXESS Aktiengesellschaft — Notices, Paying Agent and Depository Agent*'').

Subject Matter of the Listing Memorandum

The subject matter of this Listing Memorandum is 73,034,192 no par value ordinary bearer shares (no-par shares) numbered 1 to 50,000 and 50,001 to 73,034,192 (the entire capital stock in the amount of €73,034,192.00) of the Company, each representing a €1.00 portion of the capital stock and carrying full dividend rights from 1 January 2004 (the ''LANXESS Shares'').

72,984,192 of the LANXESS Shares originate from a capital increase (hereinafter referred to as the ''Capital Increase''), by which LANXESS AG's capital stock will be increased by €72,984,192.00 from €50,000.00 to €73,034,192.00 through the issuance of 72,984,192 no par value ordinary bearer shares, in exchange for a contribution in kind consisting of the assets and liabilities of Bayer AG to be transferred from Bayer AG to LANXESS AG by way of spin-off pursuant to the Spin-off Agreement. The registration of the Capital Increase, which occurred on 10 January 2005, is, pursuant to section 125 sentence 1, section 66 and section 130 (1) UmwG, a prerequisite for the registration of the Spin-off in the Commercial Registers for LANXESS AG and Bayer AG.

In addition to the shares issued in the context of LANXESS AG's Capital Increase for purposes of implementing the Spin-off, the 50,000 no par value ordinary bearer shares transferred by Bayer AG to LANXESS AG by way of the Spin-off will also be issued to the stockholders of Bayer AG.

Forward-looking Statements

This Listing Memorandum contains forward-looking statements. All statements in this Listing Memorandum that do not relate to historical facts and events constitute forward-looking statements. This applies, in particular, to the statements set forth in the sections entitled ''*Summary of the Listing Memorandum*'', ''*Risk Factors*'', ''*Management's Discussion and Analysis of Financial Condition and Results of Operations*'', ''*Information Concerning the Business of LANXESS*'' and ''*Information Relating to Recent Business Developments and Outlook for LANXESS*'' and in those other sections of the Listing Memorandum that contain information on the future financial results, plans and expectations with regard to LANXESS' business or information on growth, profitability and the general economic conditions to which LANXESS is subject. Forward-looking statements may be identified by the use of the words ''should'', ''may'', ''will'', ''believes'', ''assumes'', ''expects'', ''estimates'', ''plans'', ''intends'', ''is of the opinion'', ''to the knowledge of'', ''according to estimates'' or similar phrases. Forward-looking statements are based on current evaluations made by the Company to the best of its knowledge. They are based on assumptions and factors and are subject to risks and uncertainties, the non-occurrence or occurrence of which could cause the actual results, including the financial condition and profitability of LANXESS, to differ materially from or be more negative than those expressed or implied by such forward-looking statements. For this reason, investors are strongly advised to read the sections entitled ''*Risk Factors*'', ''*Management's Discussion and Analysis of Financial Condition and Results of Operations*'' and ''*Information Concerning the Business of LANXESS*'', which include a more detailed description of those factors that could have an impact on the Company's business development and on the industry sectors in which the Company operates. These factors include the volatility and cyclical nature of the global chemicals and polymers markets, intense competition, pending and future antitrust proceedings, obligations under environmental laws and regulations, exchange rate fluctuations, the establishment of new functions at LANXESS and the enforceability and success of planned restructuring steps, liability arising from the Spin-off and its preparatory steps, tax consequences of the Spin-off, long-term supply and service agreements, the behaviour of stockholders directly following the admission to trading and other factors mentioned in this Listing Memorandum.

In light of the risks, uncertainties and assumptions, the possibility that the future events referred to in this Listing Memorandum may not occur cannot be excluded. This also applies to the forward-looking estimates and projections derived from studies conducted by third parties (see also ''— *Notice Regarding Sources of Market Information and Technical Terms*'').

Consequently, neither the Company nor its management can give any assurance regarding the future accuracy of the opinions set forth in this Listing Memorandum or the actual occurrence of the projected developments. Furthermore, neither the Company nor the Global Co-ordinators assume any obligation to update such forward-looking statements and to adjust them in light of future events or developments, save as required by law.

Notice Regarding Sources of Market Information and Technical Terms

A selective, industry-wide definition of the chemicals and polymers markets and their individual markets and segments is not available due to the large number of different products, their varied fields of application and the divergent market structures. For this reason and for purposes of this Listing Memorandum, the segmentation of LANXESS sales markets corresponds to the product offerings of the respective LANXESS business units. The information set forth in this Listing Memorandum concerning the respective competitive positions of the business units is also based on such segmentation. External studies by well-known market research institutes are, as a rule, available only for specific market sectors of a certain size. For other market sectors (e.g., niche segments), the Company is therefore dependent on its own market analyses. Consequently, use of the term ''market'' does not constitute a geographical or product market definition that could be used as a basis for merger regulatory analysis.

Unless stated otherwise, the information set forth in this Listing Memorandum concerning the market environment, market developments, growth rates, market trends, market position and the competitive environment in the respective market sectors in which LANXESS operates is based largely on assessments by the Company. These, in turn, are based partly on internal market observations and partly on market studies commissioned by the Company (e.g., analyses by JHC Partnership, Denbighshire, England, and Rabih Srour, Paris, France). This applies, in particular, to the description of the market environment in the Performance Chemicals and Chemical Intermediates segments. Other assessments by the Company — in particular, in the Chemical Intermediates, Performance Rubber and, to some extent, Engineering Plastics segments — are based on published data or figures from external and publicly-accessible sources. These include, for example, various studies by SRI International, a non-profit company having its principal place of business in Menlo Park, California, U.S.A. (hereinafter referred to as ''SRI''), The Freedonia Group Inc., Cleveland, Ohio, U.S.A. (hereinafter referred to as ''Freedonia Group''), the International Institute of Synthetic Rubber Producers Inc., Houston, Texas, U.S.A. (hereinafter referred to as ''IISRP'') and Chemical Market Associates Inc., Houston, Texas, U.S.A. (hereinafter referred to as ''CMAI''), including:

- various SRI studies from ''Specialty Chemicals Update Program (SCUP)'': ''Electronic Chemicals'' (November 2004), ''Cosmetic Chemicals'' (August 2004), ''Specialty Paper Chemicals'' (December 2003), ''Antioxidants'' (September 2003), ''Rubber-Processing Chemicals'' (July 2003), ''Plastic Additives'' (June 2003), ''Textile Chemicals'' (December 2001) and ''Active Pharmaceutical Ingredients'' (July 2001);
- various SRI studies from ''Chemical Economic Handbook (CEH)'', such as ''Nylon Resins'' (October 2004), ''Benzyl Chloride'' (September 2004), ''Styrene-Butadiene Elastomers'' (June 2004), ''Phthalic Anhydride'' (April 2004), ''Toluenes'' (November 2003), ''Benzene'' (September 2003), ''Polybutadiene Elastomers'' (May 2003), ''Chlorobenzenes'' (January 2003), ''Neopentyl Polyhydric Alcohols'' (December 2002), ''Oxo Chemicals'' (November 2002), ''Maleic Anhydride'' (August 2002), ''Cresols Xylenols and Cresylic Acid'' (June 2002) and ''Butyl Elastomers'' (January 2002);
- various SRI studies from ''China Report 2004'', ''Chemical Product Trends — Plastic Additives'' (2004) and ''— ABS Resins'' (2004);
- World Rubber Processing Chemicals — Study 1592 (Freedonia Group, September 2002);
- Worldwide Rubber Statistics (IISRP, 2003); and
- Capacity Database of CMAI (2004).

The studies mentioned are updated at varying intervals. The most current issues were used in each case.

The market information contained in this Listing Memorandum was largely summarised and derived by the Company from a range of studies. Individual studies are cited only where the relevant information may be drawn directly from the relevant study.

The Company has not verified the figures, market data and other information on which third parties have based their studies or the internal and external sources upon which the Company's assessments are based. The Company therefore makes no representation or warranty as to the accuracy of any information in this Listing Memorandum which is derived from third-party studies on market environment, market developments, growth rates, market trends and the competitive environment or the accuracy of the information upon which its assessments are based.

A glossary of technical terms and abbreviations is included at the end of this Listing Memorandum.

Notice Regarding Financial Information in this Listing Memorandum

Unless stipulated otherwise, the financial data (including employee data) of the LANXESS Group contained in this Listing Memorandum for the years 2002 and 2003 as well as for the first nine months of the years 2003 and 2004 have been derived from the Combined Financial Statements. The assets and liabilities to be transferred to the LANXESS Group were recognised and valued in the Combined Financial Statements in accordance with the standards issued by the International Accounting Standards Board (''IASB''), London, in effect as of the closing date of the financial statements. The determination of the LANXESS Group's financial data presented in this section is based on certain assumptions with respect to the accounting and valuation methods described elsewhere in this Listing Memorandum and in the Notes to the Combined Financial Statements. The Combined Financial Statements generally present LANXESS as if the Group had already existed in the past and had the structure defined for the Spin-off. Underlying the selected financial data is an assumption that the role of LANXESS AG as the Group parent company and the legal structure below this Company in effect after the Spin-off of the LANXESS Group takes effect had already been in place as of 1 January 2002. In preparing the Combined Financial Statements, several assumptions and estimates had to be made which have an effect on the amounts and presentation of assets and liabilities, income and expenses and contingent liabilities. Actual figures could differ from the estimates. The section ''*Basis for Financial Statement Reporting*'' in the Notes to the Combined Financial Statements in the financial section contains a more detailed description of the material allocation procedures and their limitations.

Summary of the Listing Memorandum

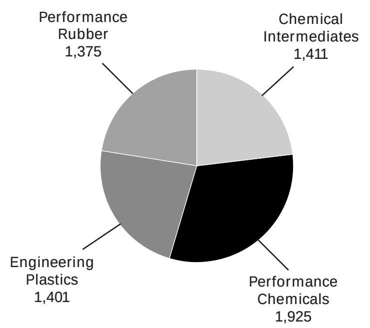
The following summary is supplemented by the information provided in other parts of this Listing Memorandum and, in particular, by information set forth in the financial section and ''Management's Discussion and Analysis of Financial Condition and Results of Operations'', and should be read in conjunction with this additional information. The summary does not contain all of the information of importance to the investor. Therefore, investors should read the entire Listing Memorandum carefully. With respect to certain considerations relevant to an investment in the shares of LANXESS Aktiengesellschaft, reference is made to the section entitled ''Risk Factors''. A glossary of technical terms and abbreviations used herein is set forth at the end of the Listing Memorandum.

LANXESS Aktiengesellschaft

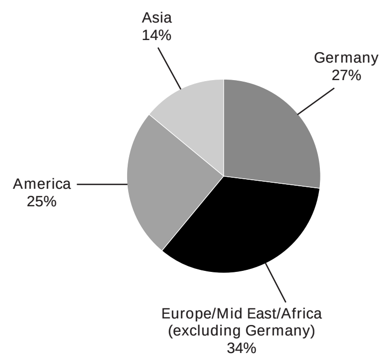
LANXESS is one of Europe's major providers of polymers and chemicals with a comprehensive product portfolio in the fields of polymers and basic, specialty and fine chemicals. With more than 50 operating companies, LANXESS generated sales of approximately €6.3 billion in fiscal year 2003 (sales figures based on the Combined Financial Statements). As of 30 September 2004, the Group employed approximately 19,600 employees worldwide, of which approximately 10,100 were based in Germany. The global business activities of LANXESS are structured into 17 operating business units combined into the four segments Performance Rubber, Engineering Plastics, Chemical Intermediates and Performance Chemicals.

The following two diagrams show the LANXESS Group's net sales in fiscal year 2003, broken down by segment and by the geographical regions in which LANXESS operates.

Net Sales in Fiscal Year 2003 in € millions broken down by segment



Net Sales in Fiscal Year 2003 broken down by geographical region as a percentage of total sales



Competitive Strengths

The Company believes that LANXESS distinguishes itself from the competition with the following competitive strengths:

Strong market position: With sales of €6.3 billion in 2003, LANXESS is expected to be the sixth-largest publicly-listed chemicals company in Europe. The Company estimates that, based on sales revenue or volume, in some two thirds of its business units, LANXESS holds one of the leading positions in the respective markets worldwide.

Global presence: Represented by its foreign affiliates, LANXESS has a presence in all major global chemicals and polymers markets and has production sites in 50 locations in 18 countries, in particular in Germany, Belgium, the United States, Canada and the People's Republic of China, most of which have the necessary critical mass and leading processes and technologies at their disposal. In the Asian market, which is currently experiencing particularly dynamic growth, LANXESS already has more than ten distribution and application technology centres as well as eight production sites at its disposal. In all, nearly 50% of LANXESS employees are employed internationally and approximately three quarters of LANXESS' sales are generated outside of Germany.

Diversified product portfolio: LANXESS has an extensive product portfolio ranging from solid rubbers, plastics and synthetic fibres to high quality basic and fine chemicals as well as chemicals for the leather, textile and paper industries. LANXESS' customers include well-known manufacturers particularly in the polymer processing and chemicals industry, the fields of electronics and electrical engineering, the automobile and tyre industry, the construction industry, life sciences companies, and the leather, textile and paper industries.

High level of customer orientation: Due to the close cooperation it enjoys with its customers and the comprehensive know-how of its employees in the area of application technology, LANXESS is able to offer its customers tailor-made products and thus meet their particular needs. The Group's research and development activities are also focused on the specific requirements of its business activities and customers.

Performance-oriented corporate structure: The independence resulting from the Spin-off will provide LANXESS with more flexibility and greater transparency, and enable it to strategically restructure its product portfolio. The clear organisational structure consisting of business units that have independent business responsibilities on a worldwide basis, as well as the planned introduction of performance-oriented compensation schemes, will create the foundations LANXESS needs for this purpose.

Corporate Strategy

The Company plans to use its new corporate independence intensively to increase the profitability of the LANXESS Group. The earnings potential of all business activities will thus be reviewed, and concerted cost-reduction, efficiency-enhancement and restructuring measures will be implemented.

The four cornerstones of the Company's strategy are:

- **Short-term measures for improving operational productivity** through continued efforts to reduce costs, optimisation of processes, improvement of the product and customer mix and development of a new price-quantity strategy.

- **Systematic restructuring** through, for example, consolidation, relocation or closure of facilities, and measures to reduce personnel costs, particularly in those businesses and product lines which are unlikely to attain a satisfactory level of profitability on the basis of an implementation of the planned measures for improving operational productivity alone.

- **Active portfolio management** through a review of cooperative ventures and divestitures primarily in those business sectors where the Company is unable with its own resources to attain, within a given timeframe, the strategic or financial position it desires.

- **Selective organic growth** in profitable businesses with attractive growth potential (e.g., the expansion of production capacities in butyl rubber) and in Asia, particularly in China.

Moreover, LANXESS intends to adapt its organisational and corporate legal structure to enable better management of its strategic goals and, in particular, of the optimisation of its portfolio, such adaptive measures to include the carve-out of individual units into separate independent entities and, where appropriate, modifications to LANXESS' national organisations.

The Board of Management will also review whether profitability may be further increased by the carving-out or outsourcing of services, existing distribution structures or other parts of the value chain.

Through the consistent implementation of this strategy, the Company seeks to achieve — assuming sales at the level of those in fiscal year 2004 — a 9 to 10% EBITDA margin before exceptional items for fiscal year 2006. At the same time, the Company intends to limit capital expenditures by LANXESS to approximately 4% of Group sales *per annum* by 2006, by means of a systematic allocation of resources.

Selected Consolidated Financial Data

The selected consolidated financial data set forth below are merely a summary of the Combined Financial Statements for the years 2002 and 2003 as well as for the first nine months of 2003 and 2004. These data should be read in conjunction with the section entitled ''*Management's Discussion and Analysis of Financial Condition and Results of Operations*'' and the LANXESS Group's Combined Financial Statements and the Notes thereto included in the financial section of this Listing Memorandum.

The following selected financial data for the years 2002 and 2003 as well as for the first nine months of 2003 and 2004 have been derived from the Combined Financial Statements. The assets and liabilities to be transferred to the LANXESS Group were recognised and valued in the Combined Financial Statements in accordance with the standards issued by the International Accounting Standards Board (''IASB''), London, in effect as of the closing date of the financial statements. There are several material differences between the International Financial Reporting Standards (''IFRS'') and U.S. Generally Accepted Accounting Principles (''U.S. GAAP'').

The Combined Financial Statements generally present LANXESS as if the Group had already existed in the past and had the structure defined for the Spin-off. Underlying the selected financial data is an assumption that the role of LANXESS AG as the Group parent company and the legal structure below this company in effect after the Spin-off of the LANXESS Group takes effect had already been in place as of 1 January 2002. IFRS do not contain any rules for allocating assets and liabilities in the Combined Financial Statements. The allocation of business activities to the LANXESS Group was authoritatively based on the relevant provisions of the agreements executed for the formation of LANXESS. The legal entities to be transferred (so-called ''Share Deals'') were accordingly reported in the Combined Financial Statements on the basis of their respective legal structure. Business activities (so-called ''Asset Deals'') were generally reported on the basis of the reporting structures of the Bayer Group authoritative for financial controlling purposes having regard to the contractual arrangements between LANXESS and the Bayer Group. In preparing the Combined Financial Statements, additional assumptions and projections had to be made which affect the amounts and the presentation of assets and liabilities, income and expenses and contingent liabilities. Actual figures could differ from the estimates. The section ''*Basis for Financial Statement Reporting*'' in the Notes to the Combined Financial Statements appearing in the financial section contains a more detailed description of those allocation procedures and their limitations that are material in this context.

In the 2002 Combined Financial Statements contained in the Joint Spin-off Report, a portion of property, plant and equipment already existing as of 1 January 2002 was erroneously reported as additions, thus leading to an error amounting to €94 million in the presentation of 2002 capital expenditures and amounting to €40 million in the presentation of 2002 depreciation and write-downs of property, plant and equipment. This technical error was corrected in the following financial data and the 2002 Combined Financial Statements contained in the financial section of this Listing Memorandum and did not have an effect on either the 2002 balance sheet and income statement, or on the financial data and financial reports for subsequent periods. The correction of this error led most importantly to a decrease of €40 million in net cash provided by operating activities, a decrease of €94 million in net cash used in investing activities and a decrease of €54 million in net cash provided by (used in) financial activities. Segment data were changed accordingly. The group financial statements (Combined Financial Statements according to IFRS) of the LANXESS Group as of 31 December 2003 were audited and issued with an unqualified audit opinion by PwC Deutsche Revision Aktiengesellschaft, Wirtschaftsprüfungsgesellschaft, Essen.

Consolidated Income Statement Data

All figures in € millions	Fiscal year ending 31 December - audited - 2002	2003	1 January to 30 September - unaudited - 2003	2004
Net sales	6,763	6,315	4,828	5,047
Cost of goods sold	(5,285)	(5,211)	(3,919)	(3,937)
Gross profit	1,478	1,104	909	1,110
Selling expenses	(985)	(935)	(683)	(638)
Research and development expenses	(149)	(168)	(118)	(95)
General and administrative expenses	(202)	(257)	(162)	(196)
Other operating expenses, less other operating income	(261)	(1,041)	(23)	(105)
Operating result	(119)	(1,297)	(77)	76
Non-operating result	(89)	(111)	(92)	(58)
Income (loss) before income taxes	(208)	(1,408)	(169)	18
Income taxes	90	412	60	(21)
Income (loss) after taxes	(118)	(996)	(109)	(3)
Minority stockholders' interest	(1)	(1)	(4)	(5)
Net income (loss)	(119)	(997)	(113)	(8)

Consolidated Balance Sheet Data

All figures in € millions	As of 31 December - audited - 2002	2003	As of 30 September - unaudited - 2003	2004
Non-current assets	3,021	1,690	2,724	1,675
Current assets (including prepaid expense items and deferred taxes)	2,598	2,841	2,793	3,008
of which liquid assets	10	13	14	80
Stockholders' equity	2,465	1,358	2,294	1,366
Liabilities (including deferred income items and deferred taxes)	2,427	2,317	2,404	2,359
of which long-term financial obligations	446	209	173	336
Provisions	688	813	778	924
of which provisions for pensions and other post-employment benefits	324	408	361	412

Consolidated Cash Flow Data

All figures in € millions	Fiscal year ending 31 December - audited - 2002	2003	1 January to 30 September - unaudited - 2003	2004
Cash inflow/(outflow) from operating activities	369	346	205	40
Cash inflow/(outflow) from investing activities	(347)	(300)	(148)	85
Cash inflow/(outflow) from financing activities	(25)	(46)	(56)	(59)
Change in cash and cash equivalents due to business activities	(3)	0	1	66

Other Financial Data

All figures in € millions	Fiscal year ending 31 December - audited - 2002	2003	1 January to 30 September - unaudited - 2003	2004
Operating result (EBIT)	(119)	(1,297)	(77)	76
of which exceptional items*	(244)	(1,178)	(42)	(81)
EBITDA*	507	180	300	325
of which exceptional items*	(80)	(131)	(25)	(60)
Capital expenditures	393	312	193	158

* EBITDA is defined as operating result (EBIT) plus depreciation and amortisation. EBITDA and exceptional items are not financial data defined under IFRS and should not be considered in isolation as a substitute for net income, operating result or other measures of financial performance under IFRS. Potential investors should be aware that EBITDA and exceptional items are not consistently applied or standardised, that there may be material differences in the way in which companies calculate them and that they, considered in isolation, do not establish a basis for comparison with similarly-named performance measures of other companies.

Transfer of the Major Parts of the Chemicals Business and of Parts of the Polymers Business from Bayer AG to LANXESS AG by Way of Spin-off *(Abspaltung zur Aufnahme)*

The LANXESS Group, headed by LANXESS AG, will continue to operate the majority of the chemicals activities and approximately one third of the polymers activities of the Bayer Group. As a first step, the relevant chemicals and polymers activities were combined within the Bayer Group and will be transferred to LANXESS AG by way of spin-off.

First Step — Consolidation of the Major Parts of the Chemicals and of Parts of the Polymers Activities

As a first preparatory step, Bayer Chemicals Aktiengesellschaft (hereinafter referred to as ''Bayer Chemicals AG'') and Bayer MaterialScience Aktiengesellschaft (hereinafter referred to as ''Bayer MaterialScience AG'') transferred virtually all domestic business activities of the LANXESS Group to LANXESS GmbH by way of a spin-off (*Abspaltung zur Aufnahme*) pursuant to section 123 (2) No. 1 of the German Transformation Act (UmwG). In return therefor, Bayer AG was in each case granted one share in LANXESS GmbH, which is currently 100% owned by Bayer AG. The spin-offs were executed with economic effect as of 1 July 2004. Both spin-offs took effect upon their registration in the Commercial Registers (*Handelsregister*) for Bayer MaterialScience AG and Bayer Chemicals AG, respectively, on 30 September 2004.

The significant foreign chemicals and polymers activities were transferred to LANXESS GmbH and its subsidiaries in the individual countries using legally different methods on the basis of applicable local law. Each of the parties has, from an economic perspective, as a rule adopted the same position as if the transfers had been effected as of 1 July 2004.

At the same time, certain operating units of the Bayer service companies were transferred to LANXESS GmbH and its subsidiaries. On the basis of a previously-concluded but not yet effective land purchase agreement between LANXESS GmbH and Bayer AG, LANXESS GmbH will acquire virtually all of the domestic real property used by it. LANXESS GmbH acquired a 40% interest in Bayer Industry Services GmbH & Co. OHG, the on-site management company of the Bayer Group.

Second Step — The Spin-off

As a second step, the separation from the Bayer Group will be consummated by way of a spin-off (*Abspaltung zur Aufnahme*) pursuant to section 123 (2) No. 1 UmwG. In this regard, Bayer AG, as transferring entity, will transfer its entire equity interest in LANXESS GmbH and certain other portions of its assets in their entirety to the acquiring entity, LANXESS AG. In return for the spin-off of the assets and liabilities to it, the latter will issue 73,034,192 shares to the stockholders of Bayer AG. For purposes of implementing the Spin-off, Bayer AG and LANXESS AG entered into a spin-off and acquisition agreement. The Stockholders' Meetings of the companies approved the agreement on 17 November and on 21 December, 2004, respectively. The Spin-off will become effective once it is registered in the Commercial Register (*Handelsregister*) for Bayer AG, which is anticipated to occur on 28 January 2005.

Stock Exchange Listing

Subject Matter of the Stock Exchange Listing, Timetable, Publications

On 22 December 2004, the Company filed an application for the admission to trading on the official market segment (*amtlicher Markt*) and, simultaneously, the official market sub-segment entailing additional post-admission obligations (Prime Standard) of the Frankfurt Stock Exchange of all 73,034,192 no par value ordinary bearer shares (no-par shares) (entire capital stock) of the Company — which will be created upon registration of the Spin-off in the Commercial Register for Bayer AG — each such no-par share currently representing a €1.00 portion of the capital stock. It is expected that the Frankfurt Stock Exchange will issue the order approving the admission of the shares to trading on 28 January 2005. Trading in the shares on the stock exchange is expected to commence on 31 January 2005.

At present, the timetable for the stock exchange listing and the issuance of the Company's shares is as follows:

28 January 2005	Registration of the Spin-off in the Commercial Register for Bayer AG
28 January 2005	Order approving the admission of the shares to trading issued by the Frankfurt Stock Exchange
29 January 2005	Publication regarding the entry into effect of the Spin-off and the order approving the admission of the shares to trading (supplement) in the *Frankfurter Allgemeine Zeitung* and, at a later date, in the Federal Gazette (*Bundesanzeiger*)
29 January 2005	Publication of the allotment notice in the *Frankfurter Allgemeine Zeitung* and, at a later date, in the Federal Gazette
31 January 2005	First day of listing

The German-language version of the Listing Memorandum (*Börsenzulassungsprospekt*) is expected to be available starting 19 January 2005 at no charge from the Company as a download from the Company's web site (www.lanxess.com), from the Global Co-coordinators and from the paying and depository agent disclosed in this Listing Memorandum (see ''*General Information on LANXESS Aktiengesellschaft — Notices, Paying Agent and Depository Agent*'') as well as from the admission office of the Frankfurt Stock Exchange.

Capital stock following registration of the Spin-off

Following registration of the Spin-off in the Commercial Register for Bayer AG, the Company's capital stock will amount to €73,034,192.00.

General and Specific Information Regarding the Shares

Voting rights

Each share carries the right to one vote at the Company's Stockholders' Meeting. Voting rights are not subject to any restrictions.

Dividend rights

The shares carry full dividend rights from 1 January 2004, *i.e.*, for the entire fiscal year 2004 and for each subsequent fiscal year.

Form of shares and share certificates

All shares of the Company will be issued as no par value ordinary bearer shares (no-par shares). Pursuant to section 5 (1) of the Company's articles of association, the stockholders are not entitled to receive share certificates. The shares will be represented by one or more permanent global certificates which will be deposited with Clearstream Banking AG, Frankfurt am Main, as depositary bank.

ISIN/WKN/common code/ticker symbol

International Securities Identification Number (ISIN)	DE0005470405
German Securities Identification Code (WKN)	547040
Common Code	020904992
Ticker symbol	LXS

Selling Restrictions, Transferability

The Company's shares are freely transferable and are not subject to any selling restrictions.

Designated Sponsors

Deutsche Bank and Morgan Stanley has each assumed the role of Designated Sponsor. By setting binding prices for the purchase and sale of the shares, the Designated Sponsors, in particular, provide for greater liquidity in the stock.

Allotment Procedure

The Spin-off will enter into effect upon its registration in the Commercial Register (*Handelsregister*) for Bayer AG at the Local Court (*Amtsgericht*) of Cologne, which is anticipated to occur on 28 January 2005. Once the Spin-off enters into effect, all 73,034,192 shares of LANXESS AG will be issued to the stockholders of Bayer AG at an allotment ratio of 10:1. 72,984,192 of these shares will originate from the Capital Increase of LANXESS AG to be effected for purposes of implementing the Spin-off and pursuant to a resolution passed on 21 December 2004. The remaining 50,000 of these shares will be transferred by way of the Spin-off from Bayer AG to LANXESS AG. Once the Spin-off becomes effective, the interest held by any given stockholder in LANXESS AG will correspond to such stockholder's interest in Bayer AG (a spin-off maintaining proportionality of ownership).

Allotment ratio

Once the Spin-off enters into effect, Bayer AG stockholders will be issued one no par value ordinary bearer share (no-par share) of LANXESS AG (ISIN DE0005470405/WKN 547040) — each such no-par share currently representing a €1.00 portion of the capital stock and carrying full dividend rights from 1 January 2004 — for every ten no par value ordinary bearer shares of Bayer AG (ISIN DE0005752000/WKN 575200).

Fractional rights

By virtue of the 10:1 allotment ratio, those stockholders who hold Bayer shares in their securities account in an amount not evenly divisible by ten will receive fractional rights in a LANXESS AG share (fractional share). Stockholders cannot exercise stockholders' rights on the basis of fractional shares. The depositary banks and Deutsche Bank will endeavour to arrange for an offset of fractional rights between the holders thereof. Stock exchange trading in fractional rights is not planned. In the course of the LANXESS share allotment, stockholders of Bayer AG will be requested by their depositary banks to indicate within two months of the Spin-off taking effect whether they wish to sell the fractional rights that will be assigned to them or whether they wish to acquire further fractional rights in order to convert their fractional rights into a full share. Should a request concerning fractional rights not be made within two months of the Spin-off taking effect, or should an offset of fractional rights not prove to be possible, the entire account balance of fractional rights in shares of LANXESS AG will be consolidated after said date and sold through a broker at the relevant stock market price for LANXESS shares. The net proceeds of the sale will be credited to the holders of the relevant fractional rights in proportion to the fractional rights held.

Trustee

Bayer AG has appointed Deutsche Bank AG to handle the allotment as trustee pursuant to section 125 sentence 1 and section 71 (1) UmwG. Prior to the Spin-off taking effect, Deutsche Bank will hold the LANXESS shares to be issued in trust and, promptly upon registration of the Spin-off, will allocate these to Bayer stockholders according to the 10:1 allotment ratio stipulated in the Spin-off Agreement.

Execution of the allotment

Since all of Bayer AG's shares are held in collective custody accounts at financial institutions, Bayer AG stockholders need not take any action with respect to the allotment of the LANXESS shares other than to deal with possible fractional rights (see ''— *Fractional rights*''). The allotment of the LANXESS shares is anticipated to occur on 28 January 2005 through Clearstream Banking AG, Frankfurt am Main, in the ratio of 10:1 by way of a credit to the relevant securities account. The allotted LANXESS shares will be credited to the securities account at Clearstream Banking AG, Frankfurt am Main of the respective bank for the account of the relevant stockholders. It is anticipated that the shares will be represented by one or more permanent global certificates which will be deposited with Clearstream Banking AG, Frankfurt am Main, as depositary bank.

The holders of American Depositary Receipts (''ADRs'') of Bayer AG (hereinafter also referred to as ''Bayer ADRs'') will be allotted shares in LANXESS AG through the depositary bank. The Company presently does not intend to list its shares on any U.S. stock exchange, to register its shares in the United States or to set up an ADR programme there. For this reason, the holders of Bayer ADRs will, in the context of the Spin-off, be given the option until 27 January 2005 to either accept or sell the LANXESS shares. Should holders of Bayer ADRs not give any instructions as to which option they wish to pursue by this date, the depositary bank will deem such holders to have opted to sell their LANXESS shares.

Once the Spin-off has been registered in the Commercial Register for Bayer AG, details as to the execution of the allotment will be published without delay in the *Frankfurter Allgemeine Zeitung* and, at a later date, in the Federal Gazette (''Allotment Notice''). Furthermore, stockholders of Bayer AG will be informed of the allotment of the LANXESS shares by way of account statements or other suitable notice from their depositary banks. Holders of Bayer ADRs will receive corresponding information from the depositary bank.

Risk Factors

In deciding whether to purchase the Shares, investors should carefully read and consider the following risk factors together with other information contained in this Listing Memorandum. The occurrence of one or more of these risks may have a material adverse effect on the financial condition and results of operations of LANXESS. The Company's share price could fall significantly as a result of any of these risks, and investors could lose part or even all of their investment. The risks described below are not the only risks to which LANXESS is exposed. Additional risks and uncertainties not currently known to the Company, or which the Company currently believes are immaterial, could likewise impair the business activities of LANXESS and have a material adverse effect on its financial condition and results of operations. The order in which the risks are presented below is not intended to indicate the probability of their occurrence. The risk factors have furthermore been prioritised on the basis of assumptions that could later prove to be false.

Risks relating to the Market

Volatility and cyclicality of the global chemicals and polymers markets and economic fluctuations in customer industries important to LANXESS

The business of LANXESS is exposed to the volatile and cyclical nature of the chemicals and polymers markets, especially in the Chemical Intermediates and Engineering Plastics segments. Depending on the individual market, and to some extent the geographic region, the Group's business alternates between longer or shorter periods of high market growth and longer or shorter periods of stagnation or market decline. The transition from market growth to market decline can be very swift.

Additionally, developments in the chemicals and polymers markets track those in the industries in which the Group's customers operate. A weak economic climate in the relevant customer industries typically results in lower sales volumes and declines in prices for the chemical and polymer products supplied by LANXESS. The Engineering Plastics segment is dependent to a large extent on developments in the automobile industry and, more specifically, in the automotive parts industry. Developments in the chemicals and plastics processing industries, the construction industry, the life sciences industry, the electronics and electrical technology industries, and the leather, textiles and paper industries also affect LANXESS. The industries in which the Group's customers operate are, in turn, strongly influenced by global economic developments.

The volatile and cyclical nature of the global chemicals and polymers markets together with weak or declining growth in customer industries could lead to a reduction in prices and sales volumes and thus affect sales growth and capacity utilisation at LANXESS, which could have material adverse effects on its financial condition and results of operations. Such a scenario could arise particularly if the Company's expectations concerning the duration and characteristics of such cycles, on which the business of LANXESS is based, do not materialise.

Intense competition, purchasing power and consolidation among large customers

As a rule, the global chemicals and polymers markets in which LANXESS operates are highly competitive. A main reason for this high level of competition is the fact that most of the products are classified as commodities. In recent years, intense competition in many sectors has led to declining prices and substantial pressure on profit margins. This trend could also continue in future. If it does, LANXESS could also be forced to reduce its prices.

The risks for LANXESS arising out of intense competition and the pressure on profit margins could increase even further in future since new suppliers from emerging markets — especially China and India — are increasingly entering many market sectors. This trend applies mostly to products that are less technology and capital intensive and is reflected in the developments in the Fibers, Fine Chemicals and Styrenic Resins business units. Moreover, existing competitors of LANXESS could intensify efforts to increase their respective market share.

With respect to certain customer industries, the global chemicals and polymers markets are characterised by a highly-consolidated customer base. This concentration particularly applies to the rubber market sector (butyl rubber, polybutadiene rubber and specialty elastomers), which is a significant market sector for LANXESS. The small number of customers (for rubber, they are mainly companies in the tyre manufacturing industry) results in highly-concentrated purchasing power. In future, especially in the market sector exhibiting consolidation trends, a growing number of LANXESS customers could begin exploiting their purchasing power in order to force down prices. Above all, companies in the tyre industry could be increasingly compelled to take such action since they themselves face intense price pressure imposed by the large automobile manufacturers.

Markets in which LANXESS operates and which until now have had a balanced customer structure could change as a result of the current consolidation trend, which would translate into increased purchasing power for the remaining companies.

The above factors could, either individually or in the aggregate, substantially affect selling prices, profit margins and the market positions of LANXESS and have an adverse effect on LANXESS' financial condition and results of operations.

Demand for chemicals and polymers in Asia

According to the Company's assessments, which are based both on its own market observations and on external market studies for the respective market sectors in which LANXESS operates, the global chemicals and polymers markets are currently exhibiting moderate growth. To a large extent, the current growth is fuelled by strong demand in Asia, particularly in China. This demand, in turn, is critically dependent on the general economic growth in this region.

In view of the strong demand for chemicals and polymers in Asia, suppliers have rapidly expanded their production capacity, especially in fibres, fine chemicals and styrenic resins. At present, this production capacity serves primarily the local Asian market.

In future, should the economic growth in Asia, and particularly in China, slow down or should this region slip into a recession, the possibility that Asian suppliers would focus more on serving the European and American markets in order to make use of freed-up production capacity cannot be excluded. This would lead to a substantial price decline in those markets in which LANXESS generates most of its sales. There is a risk that, in this case, LANXESS could face lower profit margins and lose market share.

There is also a risk that Asian suppliers could increase their sales efforts in the European market because of existing overcapacity or other factors. This trend could also accelerate due to competitive advantages related to currency effects (such as result from manufacturing products in the U.S. dollar zone and selling them in the euro zone) and other factors.

The above factors could have a material adverse effect on the financial condition and results of operations of LANXESS.

Risks relating to the Business of LANXESS

Antitrust proceedings

As part of the Spin-off, the activities of Bayer AG's former Rubber business group were transferred to the LANXESS Group. Various products included in this business group are or have been the subject of investigations conducted by antitrust authorities in the United States, Canada and Europe. In the United States, Bayer AG pled guilty to charges of illegal price-fixing with respect to rubber chemicals between 1995 and 2001 and with respect to nitrile rubber from May to the end of December 2002. Bayer AG agreed to fines of U.S.$66 million and U.S.$4.7 million, respectively. The court approved the underlying settlements. LANXESS established provisions totalling €20 million in the Combined Financial Statements to cover its portion of these fines, as determined by the terms of the Spin-off. Of this amount, a provision of €12 million was established for the Technical Rubber Products business unit in the Performance Rubber segment and a provision of €8 million was established for the Performance Chemicals segment, the bulk of which related to the Rubber Chemicals business unit. Investigations into the same matters are still pending in Europe and Canada. The Company is expecting heavy fines to be imposed by the European Commission. The Company believes it is also exposed to a risk of criminal fines in Canada.

There are also other products which are or were allocable to the former Rubber business and in respect of which investigations by antitrust authorities are still pending in several additional cases, some of which concern exclusively Europe and two others that also concern the United States and Canada. In all but one of these additional cases, Bayer AG was the first affected company to file the relevant application with all competent antitrust authorities that have a special cooperation programme (''leniency programme''). The Company expects that a significant fine will be imposed on it with respect to the investigation in which Bayer AG was not the first company to cooperate with the authorities. It is currently impossible to estimate the amount of this fine. With respect to the remaining investigations, the Company considers the prospects good that no fine will be imposed on Bayer AG.

Moreover, a number of lawsuits — both individual and class actions — have been filed in the United States and Canada, in which Bayer AG and two subsidiaries of LANXESS, RheinChemie Rheinau GmbH and RheinChemie Corp., Trenton, New Jersey, have been named as defendants. The plaintiffs are seeking substantial damages (including treble and punitive damages). The possibility that additional civil suits will be filed in the United States and Canada cannot be excluded.

The financial risk associated with all of the proceedings mentioned above (with the exception of criminal proceedings in which penalties have already been imposed), including the financial risk associated with future civil damage actions, is currently not quantifiable. The Company expects that significant expenses will be required during the further course of the criminal proceedings and civil damage actions.

In a master agreement LANXESS AG and Bayer AG have agreed to specific terms and conditions concerning the proceedings described above. With respect to all liabilities arising out of these proceedings (whether in the form of penalties, fines, damages, punitive damages or claims for the disgorgement of excess revenues arising from the antitrust violation) that had at least commenced prior to 1 July 2004 or in respect of which a company had taken steps prior to 1 July 2004 before an antitrust authority with a view to commencing such proceedings, LANXESS AG will bear 30% and Bayer AG 70% of such liabilities, as between themselves. LANXESS AG's liability is limited to a total of €100 million. In addition, any tax disadvantages arising thereby due to limited deductibility for tax purposes, as well as legal defence costs, are to be reimbursed. In accordance with the terms of a master agreement between them, LANXESS AG and Bayer AG are to agree on rules for handling proceedings (for more details concerning the master agreement, see the section entitled ''*Business Transactions and Legal Relationships with Related Parties — Business Transactions and Legal Relationships with the Bayer Group*'').

Regulatory or court decisions or other matters in connection with the antitrust proceedings or civil actions described above could result in additional costs that are not covered (in whole or in part) by provisions. As of 30 September 2004, total provisions amounted to €35 million. The Company considers it possible that the indemnity obligation agreed as between Bayer AG and LANXESS AG and totalling €100 million, plus the tax indemnity described above, will fully materialise. In this case, the indemnity payments would be limited to €50 million per calendar year (for more details, see ''*Further Details and Explanation of the LANXESS Spin-off*''). In the case of adverse regulatory or court decisions, LANXESS could also suffer a loss of reputation which, in turn, could diminish future earnings. In addition, the possibility that new antitrust proceedings or civil actions will be instituted in future cannot be excluded. Therefore, the possibility cannot be excluded that the financial condition and results of operations of LANXESS will suffer material adverse effects as a result of the unfavourable outcome of one or more antitrust proceedings or civil actions.

Obligations arising from environmental protection laws and liability for pre-existing contamination

As a company operating in the chemical industry, LANXESS is subject to extensive, constantly expanding and increasingly stringent regulations on environmental protection and laws governing chemicals and hazardous substances. In accordance with these requirements, LANXESS imposes high technological and safety standards for the construction, operation and maintenance of production plants. Nevertheless, the possibility that operating disruptions — including those due to external influences such as natural disasters or terrorism — may occur cannot be excluded. These could lead to explosions, to the release of poisonous substances or substances otherwise presenting a health hazard, or to accidents causing personal injury or damage to property or the environment. Such events could result in civil litigation or criminal prosecution as well as loss of production capacity. LANXESS is insured against such risks to an extent customary in the industry by means of insurance covering property damage, third-party liability and production disruptions. Insurance coverage may not, however, be sufficient to cover all claims, pecuniary prejudice and losses resulting from such events.

More stringent statutory environmental protection standards have already been enacted, especially relating to the reduction of emissions. These legislative changes make it necessary for LANXESS to invest substantially in modernising its production plants. LANXESS estimates that — as a result of the 2002 Technical Directives for Air (*Technische Anleitung Luft 2002)* and other legal provisions on protecting against air pollution — it will have to spend approximately €80 million on technological modernisation of its plants between 2005 and 2007. Because of emerging changes in the law, LANXESS also anticipates investment requirements of approximately €20 million with respect to wastewater treatment plants in the next few years. Further tightening of the environmental and safety provisions with which LANXESS must comply could lead to considerable costs and liability outside its control. LANXESS does not have the ability to foresee the extent of this risk.

LANXESS operates production sites, some of which — like those in Leverkusen, Dormagen and Krefeld-Uerdingen — have been put to industrial use for decades and on which significant contamination has occurred in the past, especially with regard to soil and groundwater. Costs associated with existing and potential obligations to secure or remediate contaminated sites in accordance with environmental protection regulations could have a material adverse effect on the financial condition and results of operations of LANXESS.

LANXESS is responsible for numerous industrial sites partially consisting of contaminated areas that must be remediated or secured, e.g., in Bushy Park, Charleston, South Carolina and in Sarnia, Ontario, Canada. The liability of LANXESS may also extend to other real property if pollution has spread undetected. The costs associated with such clean-ups are often almost impossible to estimate and could dramatically affect LANXESS' financial condition. This risk exists particularly for the sites that could be subject to the ''Natural Resource Damages'' initiative of the New Jersey Department of Environmental Protection, most notably the sites in Birmingham and Haledon, New Jersey, U.S.A. Under this programme, environmental damage caused by past industrial use is evaluated — on the basis of presently unclear criteria — and compensation exacted, by way of class action lawsuits, from those companies that bear a nexus to the damaged environmental resource.

In connection with the groundwater contamination with chromium VI compounds in Merebank, South Africa, the extent of which became known in October 2004, LANXESS created a €40 million provision. This provision was estimated on the basis of the remediation costs foreseeable at the stage of the investigation completed at that time. Depending on the results of the continuing investigations, the actual remediation costs could exceed this estimate. Moreover, LANXESS may be exposed to third-party claims based on health threats or loss of enjoyment of property. Chromium VI compounds are or were also used at other LANXESS production sites. At these sites, there is a risk of environmental damage and thus of substantial remediation costs for LANXESS.

Associated with many LANXESS production sites are landfills that could require substantial remediation given the material deposited there in the past, an example being the Bürrig-Dhünnaue landfill in the vicinity of the production site in Leverkusen. Although the Company at present does not consider it necessary or advisable to carry out any significant remediation, the possibility cannot be excluded that such measures will be required in future, including such measures as may be mandated by regulatory authorities.

As of 30 September 2004, LANXESS had set aside provisions totalling €85 million for environmental protection obligations. Future costs for the remediation of existing contamination and environmental damage, as well as for environmental protection as a whole, are difficult to predict because there are numerous uncertainties, especially given the constantly changing regulatory environment and the possible concomitant tightening of safety standards.

The factors mentioned above could, either individually or in the aggregate, have an adverse effect on the financial condition and results of operations of LANXESS and could harm its public image and customer relations.

Risks arising from exchange rate fluctuations

LANXESS transacts business in many different currencies and is therefore exposed to a variety of risks associated with fluctuations in the relative values of these currencies, especially the exchange rates between the euro and the U.S. dollar. Other important currencies are the Canadian dollar and the Japanese yen.

Exchange rate risks exist when, for example, the receivables or payables of a LANXESS Group company are denominated in a currency other than the company's local currency.

Additional exchange rate risks occur if the sales of a LANXESS Group company are denominated in currencies other than those in which the associated costs are denominated. This situation leads to the creation of open currency positions in operations. More than half of the total currency risks arising from outstanding and anticipated business transactions of LANXESS are attributable to accounts denominated in U.S. dollars or currencies pegged to the U.S. dollar.

Since LANXESS attempts to minimise the potential effects of the above-mentioned currency risks by using derivative financial instruments, the Company believes that a significant increase or decrease in the exchange rate of the euro relative to other major currencies should not, in the short term, materially affect its future cash flow. Over time, however, to the extent LANXESS is unable to reflect exchange rate movements in, for example, the pricing of its products in local currency, such exchange rate fluctuations could adversely affect its results of operations. At the same time, LANXESS could suffer a competitive disadvantage *vis-à-vis* certain rivals to the extent that such rivals both manufacture and sell their products in the U.S. dollar region and are therefore not affected by exchange rate fluctuations.

LANXESS prepares its consolidated financial statements in euros. However, many of the companies within the LANXESS Group are located outside the euro zone. For this reason, fluctuations in the average exchange rate of the currency concerned from one accounting period to another also impact the sales, income and assets reported in euros in the LANXESS consolidated financial statements. Thus, for example, depreciation of the U.S. dollar against the euro would — assuming a constant sales volume and constant nominal prices in U.S. dollars, for example — result in LANXESS generating lower sales revenues after converting the figures into euros. Unlike the effect of exchange rate fluctuations in the case of transaction risk, the translation risk exposure does not affect LANXESS' local currency cash flows.

Fluctuations in exchange rates, especially in the rate of the euro against the U.S. dollar or other currencies relevant for LANXESS, could have an adverse effect on the financial condition and results of operations of LANXESS.

Fluctuations in the prices for raw materials and energy

LANXESS depends on numerous raw materials for its production and requires large quantities of energy from various sources. Prices for both raw materials and energy are subject to strong cyclical volatility. The most important petrochemical raw materials for LANXESS, which are heavily dependent on crude oil prices, are 1, 3 butadiene, acrylonitrile, benzene, C4 raffinate 1, cyclohexane, isobutylene, styrene and toluene. In addition, the prices of other important raw materials are also subject to strong cyclical volatility and in particular depend on the price of electricity and natural gas. These include chlorine, sodium hydroxide and ammonia. The costs of raw materials and energy constitute a large proportion — in some business units more than 50% — of the total production costs for LANXESS.

LANXESS uses various methods to avoid and control the price risks for raw materials and energy, including, among other things, long-term supply contracts with pricing formulas and active inventory management. In addition, some of the energy requirements are secured by means of forward contracts. A hedging of all price risk for raw materials and energy is impossible, however. In 2004, LANXESS was able to pass on price increases for raw materials and energy for many products by increasing prices. It is not possible, however, to pass on the entire price increases for raw materials and energy in all of LANXESS' business areas. Petrochemical raw materials in particular have been historically exposed to large price fluctuations. The energy price risk to which LANXESS is exposed mostly relates to natural gas in North America and fuel oil in Europe.

Should prices for raw materials and energy continue to rise and LANXESS be unsuccessful in passing on these higher costs to its customers, this could have an adverse effect on the financial condition and results of operations of LANXESS. This effect could be exacerbated by further cost increases outside of the influence of LANXESS, triggered by future legislative changes such as those relating to the ecology tax (*Ökosteuer*) in Germany. In this respect, particular uncertainty exists about the continued applicability beyond 2006 of the special regulatory treatment accorded the manufacturing industry. Potentially more restrictive rules could affect all LANXESS manufacturing companies in Germany, including companies in which it holds an equity interest.

Observations also show that, when prices for raw materials and energy fall, the selling prices of chemical products, which LANXESS also supplies, often decline disproportionately in relation to the raw materials and energy prices, due to the intense competition. If LANXESS is unsuccessful in adapting to the changes in basic economic conditions through appropriate measures (e.g., by reducing production costs), this could have an adverse effect on the financial condition and results of operations of LANXESS.

Potential impairment of the health of persons due to harmful product characteristics

LANXESS' product portfolio contains or contained, among other things, substances which are classifiable or are classified as carcinogenic (cancer-causing), mutagenic, reproductively toxic, generally toxic or otherwise hazardous to health. The possibility cannot be excluded that the health of persons who come into contact with LANXESS products may be impaired, especially as a result of incorrect use of such products or because of product characteristics that are as yet unknown, and that such health impairments may even be life-threatening.

In addition, some substances used by LANXESS during construction and in the production process are the subject of litigation. This is the case, for example, with asbestos (see ''*Information Concerning the Business of LANXESS — Litigation/Regulatory Proceedings*'').

The factors mentioned above may, either individually or in the aggregate, have an adverse affect on the financial condition and results of operations of LANXESS.

Changes in national or EU rules

The regulatory environment for the business activities of LANXESS is continuously changing at the international and, above all, the supra-national and national levels, in light of technological progress and the public's increased safety needs and awareness with respect to quality and the environment. The tightening of the regulations with which LANXESS must comply could subject LANXESS to even more rigorous controls than at present with regard to its handling of substances or hazardous materials, as well as the production, use, recycling or disposal thereof. Such tightening could require significant capital expenditures and therefore have adverse effects on the production costs and the product portfolio of LANXESS or expose LANXESS to considerable liability risks.

Of great significance for the business activities of LANXESS will be the implementation of the proposed EC regulation on the Registration, Evaluation, Authorisation and Restriction of

Chemicals (''REACh''), the draft of which was submitted by the European Commission on 29 October 2003. It will probably come into force at the end of 2006 or the beginning of 2007. On the basis of the current draft of the regulation and on preliminary estimates, the costs that LANXESS would incur for the complete registration of all the substances covered by the regulation during the eleven years allocated for such registration would total €200 million. LANXESS could also face additional future costs resulting from the implementation of the ''Environment and Health Strategy'' (the SCALE Initiative) proposed by the European Commission in 2003. The aim of SCALE is to develop an EU-wide system for interlinking information about the condition of the environment, the ecosystem and human health and thereby to improve, among other things, the evaluation of so-called ''cocktail effects'', combined strain and cumulative effects on human health. It is not currently possible to predict whether and, if so, when the SCALE Initiative will lead to mandatory EU regulations.

Purchase of sufficient quantities of certain raw materials essential to operations

Certain raw materials and starting products on which LANXESS depends for its manufacturing operations are not always available in sufficient quantities on the respective markets. This currently especially applies to the raw materials 1, 3-butadiene, ammonia and bromine. In addition, LANXESS production plants in some locations are networked with those of third parties and, as part of these arrangements, raw materials, especially those which cannot be transported over long distances, are purchased from such parties. Thus, for example, LANXESS purchases carbon monoxide at the Dormagen site for use in the Basic Chemicals and Fine Chemicals business units.

Given the implementation of the proposed EC regulation on the Registration, Evaluation, Authorisation and Restriction of Chemicals (''REACh''), the possibility cannot be excluded that it may no longer be economically feasible for suppliers to produce certain raw materials and that therefore the supply of these raw materials will be adversely affected.

The inability of LANXESS to purchase sufficient quantities of the necessary raw materials could have adverse effects on its business activities.

Shortages or disruptions of supplies to customers due to unplanned shutdowns of production plants

Production plants of the LANXESS Group can come to a standstill as a result of technical failures, strikes, natural disasters, regulatory actions and other factors. Shortages in the supply of LANXESS products to customers can be mitigated in part by expanding production elsewhere, and gaps caused by short-term interruptions can be bridged using existing inventory. If, however, the manufacture of products is shut down for a prolonged period and products cannot be manufactured (in part or entirely) at other plants (referred to as single source plants), such a shutdown can result in a loss of sales revenues and damages claims and impairment of customer relations. If the resulting losses are not covered by business disruption insurance, the loss of production could have a material effect on the results of operations of LANXESS.

Quantitative adjustment for co-products

A frequent characteristic of chemical production is that one production stage may simultaneously yield two or more substances (co-production). Ideally, all such substances can be sold in the market, but often one or more co-products will generate disposal costs. The possibility cannot be excluded that, over time, the demand for one co-product will decline but adjustments to the quantity produced will not be feasible because of the effect on the other co-product(s) that would otherwise result. This situation could particularly arise with respect to some of the aromatics in the product portfolio of the Basic Chemicals business unit. A decrease in marketability of the so-called ''by-products'' can negatively affect earnings further.

Substitution of LANXESS products with new or improved materials or technologies

In future, alternative materials and technologies could be developed, or existing materials and technologies improved, which could be used in place of the products and technologies supplied by LANXESS. Thus, for example, a material could be developed that is at once airtight and flexible. Such a material could be used, like butyl rubber, for the manufacture of hoses and tyres. Furthermore, certain agrochemicals and specialty elastomers could be replaced by new products.

If new types of materials or technologies are offered at lower prices, have other favourable characteristics or are advantageous for other, particularly regulatory, reasons, there is a risk that customers could replace products offered by LANXESS with new types of materials or technologies. If, in this case, LANXESS is not in a position likewise to offer new types of materials or technologies, this could lead to substantial declines in sales, which could adversely affect the financial condition and results of operations of LANXESS.

Restriction of the financial flexibility of LANXESS due to obligations entered into under a syndicated credit facility

In order to refinance inter-company liabilities toward companies of the Bayer Group and to cover its general liquidity needs, LANXESS AG entered into a syndicated credit facility for €1.5 billion (the ''Credit Facility''). The Credit Facility includes a €0.5 billion tranche structured as a revolving credit line with a term of 364 days, which may be extended one or more times for additional 364-day periods subject to the approval of the banks. In addition, the Credit Facility includes two revolving tranches totalling €1.0 billion with terms ending in December 2009. The Credit Facility contains restrictions with respect to the possibility of borrowings by companies in which LANXESS has an ownership interest as well as restrictions on the right to provide collateral and to sell assets. These restrictions, which are customary in the market, may result in an impairment of LANXESS' entrepreneurial flexibility. In addition, under the terms of the Credit Facility, the banks have the right to call in the outstanding loan if the ratio of net debt (excluding the Convertible Bond) to adjusted EBITDA exceeds a certain level. The parties further agreed under the terms of the Credit Facility that if the Company's current credit ratings decline, it will have to pay a significantly higher spread to the banks. The provisions of the credit facility could have an adverse effect on the financial condition and results of operations of LANXESS.

Risks in connection with intellectual property

LANXESS has a large number of patents at its disposal that are very important for its business. Even though patents are by operation of law presumed to be valid, the granting of a patent does not necessarily mean that the patent is ultimately valid or that any patent claims are enforceable. Moreover, there is absolutely no guarantee that each patent that LANXESS has applied for or has planned for its new technologies will be granted. In addition, the possibility that third parties will infringe patents held by LANXESS cannot be excluded. Inadequate protection or the actual infringement of intellectual property rights may limit LANXESS' ability to derive economic benefit from the technological advances achieved or lead to a reduction in future income if other manufacturers are, as a result, permitted to market products developed by the LANXESS Group or its predecessors.

Furthermore, the possibility that LANXESS will infringe the patents of third parties cannot be excluded since its competitors file applications to register numerous inventions as patents and receive patent protection, just as LANXESS does. In the event of such infringement, LANXESS could specifically be prevented from using certain technologies or from manufacturing or marketing products and could be compelled to adapt its manufacturing processes, acquire a licence or pay damages. Furthermore, competitors could prohibit LANXESS from producing or distributing such goods in countries in which the competitors have higher-ranking patent protection.

Non-patentable business secrets and confidential know-how — especially in areas with technically sophisticated products — are also important factors contributing to the success of the LANXESS business. There is no guarantee that LANXESS can prevent the disclosure of business secrets or that third parties will not develop or obtain access to the same or similar know-how independently of LANXESS.

LANXESS may be forced to rely on the use of the technologies of third parties through the acquisition of licences for its business activities. The possibility cannot be excluded that, in future, LANXESS will not obtain the necessary licences for its business activities or that existing licences — especially reciprocal licences — will be invalid.

Each of these factors could have an adverse effect on LANXESS' competitive position and therefore its financial condition and results of operations.

Dependence on individual suppliers for certain raw materials or products

For some purchased raw materials or products, LANXESS relies on only a limited number of suppliers. In exceptional cases, LANXESS is even dependent on a single supplier. This is the case, for example, with respect to carbon monoxide at the Dormagen site, which is required for use in the Basic Chemicals and Fine Chemicals business units. Supply disruptions or shortages at these suppliers could have adverse effects on the business activities of LANXESS and on its financial condition and results of operations.

Risks in connection with long-term contracts for the supply of goods and services

LANXESS has entered into a number of long-term agreements both with its raw material suppliers and service partners and with its customers, particularly with companies belonging to the Bayer Group. As a rule, these contracts have terms ranging from three to six years (see also ''*Business Transactions and Legal Relationships with Related Parties — Business Transactions and Legal Relationships with the Bayer Group''*). Many of these contracts contain so-called ''sunk costs provisions'' (*Remanenzkostenregelungen*) or so-called ''take-or-pay'' provisions, pursuant to which LANXESS may be under a duty to make compensation payments in the event of a termination of the agreement or if the quantities of products purchased are less than the minimum agreed amount. Moreover, some agreements — such as a supply agreement with a LANXESS supplier and energy supply agreements — provide for minimum purchase requirements (in the former case, even obligations on co-owners to assume the contractual liabilities) over four-year and 15-year periods, respectively.

Most of the contracts contain provisions that allow certain terms such as price and quantity to be adjusted to adapt to changes in general conditions. However, the possibility cannot be excluded that certain long-term contracts will prove to be detrimental for LANXESS in future because of changes in general conditions. Thus, changes in the prices for the goods and services it purchases or the products it sells could adversely affect LANXESS.

Moreover, LANXESS could be specifically compelled to make compensatory payments or to purchase goods or services beyond its actual requirements in accordance with the ''sunk costs'' and ''take-or-pay'' provisions.

Each of these factors could have an adverse effect on the financial condition and results of operations of LANXESS.

Possible deterioration of business relations with distribution partners

In a number of countries in which LANXESS is not represented by a foreign affiliate, local distributions are also conducted through companies of the Bayer Group (so-called ''agency companies''). This arrangement currently exists, *inter alia*, for the countries or regions of Northern Europe (Sweden, Finland, Denmark, Norway and the Baltic states), Central and Eastern Europe (Poland, Czech Republic, Slovakia and Hungary), and Russia and the other CIS states, as well as for Korea and Taiwan in Asia. The Company anticipates that sales conducted through the agency companies will amount to approximately €0.7 billion in fiscal year 2005. LANXESS also distributes its products via numerous other external distribution partners, even in countries where it has its own foreign affiliates.

If agency companies or other distribution partners no longer perform to the desired extent or standard of quality or at competitive rates, LANXESS would be forced to rely on other suppliers. At the same time, the possibility cannot be excluded that one or more agency companies or other distribution partners will decide in future to discontinue distributing LANXESS products. Any changeover to other distributors as well any one-time payments or possible additional costs could have an adverse effect on the business activities and results of operations of LANXESS. Considerable additional costs could arise in fiscal year 2005, particularly in the event that agency companies terminate their operations.

Risks relating to the Spin-off and Strategic Realignment of LANXESS

Tax consequences in connection with the Spin-off and the preparatory measures implemented for this purpose

The German tax authority responsible for Bayer AG has issued an advance ruling in which it confirmed that the factual elements serving as prerequisites to a spin-off pursuant to section 15 of the German Transformation Tax Act (*Umwandlungssteuergesetz*) have been met. The statement of the facts on which this advance ruling was based also contained a description of the establishment of a LANXESS Corporate Center within Bayer AG. This LANXESS Corporate Center, which is relevant for demonstrating in connection with the Spin-off that LANXESS is an operationally separate business division (*Teilbetrieb*), is being transferred to LANXESS AG. The Company intends to continue this Corporate Center with respect to its functions and at least on the same scale (in terms of its personnel) existing on the date the Spin-off takes effect, thereby fulfilling the contractual duty to ensure the continuance of the LANXESS Corporate Center at least until 31 December 2005. The advance ruling is binding only if and to the extent that the supporting facts were correctly described. Otherwise, the Spin-off could be treated as a taxable dividend distribution to the participating stockholders, from which Bayer would be required to withhold the statutory withholding tax. The parties believe that, regarding the LANXESS Corporate Center, there is no discrepancy from the facts as described in the application.

On the basis of the above-mentioned advance ruling, corporate income tax and trade tax loss carry forwards incurred by Bayer AG may also pass to LANXESS AG on a *pro rata* basis by way of the Spin-off. It is currently not certain whether and to what extent these loss carry forwards can be utilised by LANXESS AG. The transfer of the pro-rated tax loss carry forwards pre-supposes that the businesses or business divisions to which such apportionable past losses are attributable will continue to operate for five years following the Spin-off date, as defined for tax purposes, on a scale considered comparable in view of the overall economic circumstances. This rule applies to the businesses or business divisions transferred to LANXESS as well as those remaining with the Bayer Group. No agreement was made to the effect that the Bayer companies refrain from undertaking restructuring measures during this period.

Irrespective thereof, LANXESS AG will not be able to utilise the loss carry forwards if more than 50% of LANXESS AG's shares are transferred (for example, by virtue of the listing of the LANXESS Shares on the stock exchange) and LANXESS AG receives predominantly new assets. The possibility of such injections of new capital cannot currently be excluded, especially in view of the current opinion of the German tax authorities that even the increase in cash resulting from borrowing funds or issuing debt instruments, such as the issued Convertible Bond, could constitute a receipt of new business assets. Should it emerge that the tax loss carry forwards of LANXESS AG cannot be utilised, valuation adjustments would have to be made to the deferred tax assets recorded in the consolidated balance sheet. This would lower LANXESS AG's consolidated net income and reduce the Group's stockholders' equity.

With respect to the amount of the loss carry forwards to be transferred to LANXESS AG, there is a general risk that government tax audits could result in corrections for tax assessment periods ending prior to the effective transfer date for tax purposes. Similarly, pursuant to the allocation ratio confirmed by the tax authorities, the amount of the loss carry forwards to be transferred will be determined by the ratio of the market capitalisation of Bayer AG (the average of the last ten exchange trading days) before the initial stock exchange listing of LANXESS AG to the market capitalisation of LANXESS AG beginning on the initial stock exchange listing of LANXESS (the average of the first ten trading days). Therefore, price movements during this period, in particular a weakening in the LANXESS share price immediately following the initial stock exchange listing, could possibly have an adverse effect on LANXESS with respect to the amount of the transferred loss carry forwards.

In connection with the preparatory spin-offs from Bayer Chemicals AG and Bayer MaterialScience AG to LANXESS GmbH, the latter has, from a tax point of view, acquired assets transferred to it as part of a capital contribution at the fair market value. The allocation of the aggregate value of the capital contribution among the individual assets was conducted by the participating Bayer companies and by LANXESS GmbH by mutual agreement and on the basis of the existing valuation reports. Under this procedure, the necessary write-downs of book values were allocated primarily to non-current economic assets. Nevertheless, the tax authorities are bound neither by the figures computed in the valuation reports nor by the above-mentioned allocation. Therefore, the possibility cannot be excluded that the tax authorities will calculate a different aggregate value and/or a different apportionment of the aggregate capital contribution among the individual assets acquired by LANXESS GmbH. If this situation occurs, the possibility that future income tax charges will be imposed on LANXESS GmbH cannot be excluded, particularly if some of its current assets are sold. Bayer AG and LANXESS GmbH entered into an agreement under which the present value of such future additional income tax charges, as may be conclusively determined in the context of a governmental tax audit and that result from a different apportionment of the aggregate value, will be shared equally between both these companies, insofar as these tax charges relate to current assets. In computing this cost-sharing, the parties agreed to factor in any favourable tax effects with respect to non-current assets, although the timing of the recognition of the favourable tax effect is stipulated depending on type and irrespective of LANXESS GmbH’s actual future income situation.

Pursuant to the Spin-off Agreement and the master agreement concluded in connection therewith between Bayer AG and LANXESS AG, Bayer AG or the relevant transferring enterprises affiliated with it bears any income taxes based on actions taken on or before the effective date of the Spin-off (1 July 2004) in order to establish the LANXESS subgroup. In addition, the contractual provisions concluded in the context of the transfer of portions of the LANXESS subgoup generally provide that the respective transferring Bayer company must bear income taxes assessed for those periods that end on or prior to the effective date of the transfer (as a rule 1 July 2004) to the extent the prior figures reported on the balance sheet are exceeded and the present value of any tax relief effects from offsetting changes in income at LANXESS cannot be set off against such tax liability. When calculating present value, rules based on type will be applied with respect to the timing of the recognition of the reversal effect, irrespective of LANXESS GmbH’s actual income situation.

An exception to this principle applies in certain circumstances with respect to tax liabilities arising from transfer-pricing adjustments involving foreign affiliates which were not transferred as part of the spin-offs from Bayer Chemicals AG or Bayer Material Science AG. Transfer-pricing adjustments normally arise when factual assessments by tax authorities differ from existing assessments made by the audited company. In addition, sanctions that may be imposed beginning in 2004 for failing to meet the documentation requirements prescribed under section 90 (3) of the German Fiscal Code (*Abgabenordnung*) may apply. Although there is currently no indication of this, the possibility that LANXESS could thereby be exposed to material financial liability cannot be excluded.

Irrespective of these contractual provisions, the possibility cannot be excluded that the transferee LANXESS companies will also be held liable *vis-à-vis* third parties for such taxes on account of their joint and several liability in connection with the Spin-off. However, the agreements entered into in the course of establishing the LANXESS subgroup and/or corporate practices routinely provide that the transferee LANXESS company is entitled to be indemnified against such liability by the respective transferor Bayer company.

Transfer taxes arising as a result of the measures taken to establish the LANXESS structure, such as land transfer taxes, must be borne by LANXESS. The same applies to any land transfer tax applicable upon the purchase of domestic real property by LANXESS GmbH. The land purchase agreement concluded on 30 December 2004 will become effective upon the expiry of the first calendar day following the Spin-off. At such time, the use and enjoyment of and the risks and encumbrances relating to the land will also be transferred. Consequently, in the opinion of the

Board of Management of LANXESS AG, LANXESS GmbH is not the economic owner of these properties at the time of the Spin-off as a result of the condition precedent. Thus, the Spin-off as such does not trigger any land transfer tax liability in addition to that arising from the separate purchase agreement.

Limited informative value and comparability of the Combined Financial Statements and possible changes in future financial reporting

The Combined Financial Statements of LANXESS reproduced elsewhere in this Listing Memorandum were prepared with the goal of reflecting the Group structure, as defined for the Spin-off, in the historical financial data. In preparing the Combined Financial Statements, assumptions and estimates had to be made that affect the amounts and presentation of assets and liabilities, income and expenses and contingent liabilities. Actual figures could differ from the estimates. In particular, the reported deferred tax assets are expected to be different, and corresponding changes in stockholders' equity are anticipated, in future consolidated financial statements of LANXESS following the Spin-off, since then only those loss carry forwards that passed by law to LANXESS are to be recorded and further differences between the amounts stated for tax purposes and the amounts shown in the consolidated financial statements will become effective.

Consequently, the Combined Financial Statements do not necessarily reflect the financial condition and results of operations that would have resulted had the LANXESS Group already existed as an independent group as of 1 January 2002 and the underlying transactions between the LANXESS and Bayer companies thus been entered into between independent companies.

For the reasons set forth herein, the absence of historical unity and independence of the LANXESS Group limits the informative value of the Combined Financial Statements. Therefore, the Combined Financial Statements do not enable reliable forecasting of the future development of the businesses combined in the LANXESS Group.

For a further discussion of the preparation of the Combined Financial Statements, see the section entitled ''*Management's Discussion and Analysis of Financial Condition and Results of Operations*'' and the Notes to the Combined Financial Statements, reprinted elsewhere in this Listing Memorandum.

The issues described in the following paragraphs could furthermore limit the comparability of the Combined Financial Statements to future financial reporting:

In calculating fiscal year 2004 EBITDA for the business units affected by the impairments made as of 31 December 2003, asset depreciation and amortisation amounts included in the cost of production of inventories in the balance sheet as of 31 December 2003 were added to EBIT for the second quarter — contrary to the computation method generally applied by Bayer and LANXESS — in order to obtain a presentation of EBITDA that permits comparisons to be made over time.

In addition, it may become necessary to make adjustments in future reporting as a result of new internal accounting rules — if, for example, income and expenses are allocated differently among functional units and reporting segments (particularly if Corporate Center costs are stated separately), subsidiaries' interest expense is restated or depreciation and amortisation are reported differently in fiscal year 2004 than in the Combined Financial Statements.

At the end of 2004, LANXESS and the Bayer Group agreed to extend the payment due dates on the delivery of goods and services from the Bayer Group to LANXESS. The amount deferred totalled approximately €130 million, the payment of which will be made on a rolling basis until the third quarter of fiscal year 2006.

Liability consequences and obligations to provide security in connection with the Spin-off and the associated preparatory measures

The Spin-off and the combining of the chemicals and polymers businesses in LANXESS GmbH and its direct and indirect subsidiaries involve liability risks for the LANXESS Group (see also ''*Further Details and Explanation of the LANXESS Spin-off*'').

Pursuant to section 133 (1) and (3) of the German Transformation Act, LANXESS AG is jointly and severally liable for the performance of the obligations remaining with Bayer AG that had already been established prior to the date the Spin-off took effect, if such obligations become due within five years following the date on which the registration of the Spin-off in the Commercial Register for Bayer AG is announced and such obligations give rise to claims against LANXESS AG that are asserted in the manner prescribed by law. Bayer AG and LANXESS AG agreed in the Spin-off Agreement that Bayer AG would indemnify LANXESS AG with respect to any claims enforced against LANXESS AG on the basis of such obligations of BAYER AG. Nevertheless, if creditors enforce such claims in future and Bayer AG is not in a position to comply with its indemnity obligations, this could have a material adverse effect on the financial condition and results of operations of LANXESS.

Furthermore, pursuant to sections 22, 125 and 133 of the German Transformation Act, creditors of LANXESS AG may, within six months from the date the registration of the Spin-off in the Commercial Register for Bayer AG is announced, demand that the Company furnish them with collateral to secure their claims. This applies if such creditors are unable to demand satisfaction of their claims at the respective time, that they provide written notice of the grounds and extent of their claims and that they provide credible evidence that the Spin-off jeopardises the satisfaction of their claims. Should LANXESS AG be obliged to provide collateral to some or all of its creditors, this could have an adverse effect on the LANXESS Group's financial condition and results of operations.

The arrangements mentioned above with respect to liability also apply to the spin-offs from Bayer Chemicals AG and/or Bayer MaterialScience AG to LANXESS GmbH which were carried out in the course of combining the relevant chemicals and polymers activities in LANXESS GmbH. Here, too, LANXESS GmbH is subject to joint and several liability under section 133 (1) and (3) of the German Transformation Act for the performance of the obligations remaining with Bayer Chemicals AG and/or Bayer MaterialScience AG that had already been established prior to the date the spin-off took effect, if such obligations become due within five years following the date on which the registration of the relevant spin-off in the Commercial Register for Bayer Chemicals AG or Bayer MaterialScience AG, as the case may be, is announced and such obligations give rise to claims against LANXESS GmbH that are asserted in the manner prescribed by law. These obligations include those arising from the joint liability of Bayer Chemicals AG and Bayer MaterialScience AG for Bayer AG's former liabilities in connection with the carve-out of the business activities from Bayer AG to these companies in 2002. As in the case of the Spin-off from Bayer AG to LANXESS AG, Bayer Chemicals AG and Bayer MaterialScience AG, on the one hand, and LANXESS GmbH, on the other, agreed that Bayer Chemicals AG or Bayer MaterialScience AG will, respectively, indemnify LANXESS GmbH in respect of claims asserted against it based on liabilities of Bayer Chemicals AG or Bayer MaterialScience AG. Nevertheless, if Bayer Chemicals AG or Bayer MaterialScience AG, as the case may be, are unable in future to comply with their indemnity obligations, this could have a material adverse effect on the financial condition and results of operations of LANXESS.

Furthermore, pursuant to sections 22, 125 and 133 of the German Transformation Act, creditors of LANXESS GmbH may, within six months from the date the registration of the spin-offs in the Commercial Register for Bayer Chemicals AG or Bayer MaterialScience AG, as the case may be, is announced, demand that the LANXESS GmbH furnish them with collateral to secure their claims. This applies if such creditors are unable to demand satisfaction of their claims at the respective time, that they provide written notice of the grounds and extent of their claims and that they provide credible evidence that the spin-off jeopardises the satisfaction of their claims. Should LANXESS GmbH be obliged to provide collateral to some or all of its creditors, this could have a material adverse effect on the LANXESS Group's financial condition and results of operations.

Development of administrative, financial and other functions as well as other measures in connection with the Spin-off

Until the Spin-off enters into effect, the Bayer Group will continue to provide administrative, financial, legal, information technology and other services for the business operations combined into LANXESS GmbH and its direct and indirect subsidiaries. The newly-established LANXESS

Corporate Center currently performs the following functions, among others: board office, corporate development, industrial & environmental affairs, treasury, tax, corporate controlling, internal auditing, accounting, communications, law & intellectual property, investor relations and human resources. Employees of LANXESS GmbH support the LANXESS Corporate Center in the performance of its tasks.

There is a risk that the above-mentioned functions will not attain the requisite level of independence in a timely manner and that, for example, during a transitional period, LANXESS will not have adequately-functioning departments such as accounting, controlling, risk management, cash management, its own patent, trademark and domain administration, or equity participation administration.

In connection with the Spin-off, a number of data processing systems and IT networks of LANXESS have been reconfigured or completely redesigned, particularly systems used by the LANXESS accounting department (including SAP systems). The Company plans to take additional measures to adapt the data processing systems after the Spin-off. The possibility cannot be excluded that the systems in question will not fulfil their functions or that they will fail to do so in the anticipated manner during the transitional period or that additional costs will arise. Moreover, in connection with the Spin-off and the ensuing independence of LANXESS, additional costs could arise as a result of changeover and/or adjustment measures, for example with respect to calibrated measuring instruments or other systems.

All the above-mentioned factors could, either individually or in the aggregate, have an adverse effect on the financial condition and results of operations of LANXESS.

Implementation of planned restructuring and cost-reduction measures

The Company plans to restructure the LANXESS Group and reorganise its business activities. To this end, the Company will examine all business units and identify those which will belong to the strategic core business of LANXESS in the medium and long term. The Company will continue to carefully examine the earnings potential of those business units that are not classified as strategic core business, with a view to potential partnering or possibly taking portfolio measures once the specific restructuring and cost-reduction measures have been implemented. In addition, LANXESS plans in the short term to implement performance programmes for improving competitiveness as well as Group-wide programmes for optimising processes and reducing costs. In regional terms, LANXESS aims for selective growth, particularly in China, possibly together with suitable partners (see also ''*Information Concerning the Business of LANXESS — Corporate Strategy*''). The measures undertaken by LANXESS in order to implement its strategic realignment could significantly impact the Group's results as early as fiscal year 2005.

There can be no assurance that LANXESS will succeed in achieving the extensive alignment of the Group and the associated restructuring in a timely manner. The possibility cannot be excluded that, for instance, due to the existing general legal framework, certain operations may need to be continued or that LANXESS will be unable to implement portfolio measures because the divestiture of certain business operations fails or because no suitable partner is found. As a result of the Agreement to Safeguard Sites and Employment III (*Vereinbarung zur Standort- und Beschäftigungssicherung III*), to which LANXESS AG and LANXESS GmbH must adhere, and a breakdown in negotiations on the modifications to or conclusion of other collective bargaining agreements, the possibility cannot be excluded that potential necessary restructuring measures may be delayed or prevented. In addition, actions relating to labour struggles in Germany or abroad cannot be excluded. Likewise, the implementation of the restructuring measures may be delayed or prevented because of existing production network structures, the complexity of LANXESS' IT system or the inability to convey real property from Bayer AG to LANXESS GmbH as planned. Furthermore, the possibility that the expenses incurred during the implementation of the restructuring and cost-reduction measures will be higher than budgeted cannot be excluded. This risk applies to, among other things, possible revaluations of LANXESS business operations in connection with portfolio measures, which could necessitate impairments. In addition, the Group may lose current synergies with other business operations if individual business activities are sold.

There is also a risk that LANXESS' growth strategy cannot be implemented in the Asian market as planned because, for example, no suitable partners can be found there or because existing or future partnerships turn out to be unsuccessful.

Should the Company not succeed in achieving the appropriate measures for implementing its strategy or should the measures taken not be successful, this could have a material adverse effect on the financial condition and results of operations of LANXESS.

Pending measures for the establishment of the LANXESS Group and actions in connection with the Spin-off

A number of measures have been implemented for purposes of combining almost all of the chemicals and parts of the polymers activities of the Bayer Group in LANXESS GmbH and its subsidiaries. In addition to the spin-offs from Bayer Chemicals AG and Bayer MaterialScience AG to LANXESS GmbH, the LANXESS Group's foreign chemicals and polymers businesses were transferred to LANXESS GmbH and its subsidiaries in the individual countries using different legal methods (see ''*Further Details and Explanation of the LANXESS Spin-off — First Step — Combination of Major Parts of the Chemicals and Parts of the Polymers Activities*'').

At present, the transfer of certain business activities — in particular in Brazil, India, South Africa — has not yet been effected. This also applies to the Thane production site in India and the Rustenberg mine in South Africa. The business operated at the Rustenberg mine cannot be transferred to LANXESS until the latter has complied with the legal requirements for obtaining the required licences and thus for operating the mine. Accordingly, the transfer of the land, the machinery and the intangible assets will be subject to the condition precedent that such legal requirements are met. On the other hand, the business's accounts receivable and consumables (such as spare parts) were transferred with effect from 1 August 2004. LANXESS already took over the chromium distribution business with effect from 1 July 2004. Pending the final transfer of all assets, LANXESS Mining (Pty) Ltd. will operate the mine on behalf of Bayer (Pty) Ltd. The existing Bayer licence for the Rustenberg mine expires in 2007. The failure of LANXESS to obtain its own licence by that time could have a material adverse effect on the business activities of LANXESS in the area of leather chemicals.

The possibility also cannot be excluded that the transfer to LANXESS of interests in individual joint ventures will require the consent of the respective joint venture partners and that such consent may be withheld or delayed or that the transfer will trigger rights of first refusal.

The failure to transfer certain business activities and/or equity interests to LANXESS, or delays in such transfer, could have an adverse effect on LANXESS business activities.

LANXESS GmbH continues to hold a 40% interest in Bayer Industry Services GmbH & Co. OHG. Pursuant to the land and building use agreement dated 30 December 2004, Bayer Industry Services GmbH & Co. OHG is obliged to demolish and remove — at Bayer AG's request — the buildings, plants and other installations located on certain parcels of land that had been used by the business activities combined in LANXESS GmbH. This obligation owed by Bayer Industry Services GmbH & Co. OHG could, in future, have a material adverse effect on the results of operations of the company in which LANXESS GmbH holds a 40% ownership interest.

In addition, the conveyance of the real property and operating equipment on the basis of the land purchase agreement dated 30 December 2004 between LANXESS GmbH and Bayer AG has not yet been completed. The possibility cannot be excluded that the conveyance cannot transpire as planned because, for example, regulatory permits have not been granted. In addition, adjustments may be made to existing governmental permits and/or new governmental permits may be required in connection with subdividing the relevant land, which in turn could lead to additional capital expenditures and/or more costs. Furthermore, the possibility that these properties may be subject to future revaluations cannot be excluded.

Obligation to make a public offer to purchase the shares of a listed subsidiary in India

In connection with the Spin-off, shares of LANXESS India Private Ltd., New Delhi, India, which, in turn, holds shares in Bayer ABS Limited, Baroda, India, are being transferred by Bayer AG to

LANXESS GmbH. As a consequence of this transaction, LANXESS GmbH will indirectly hold 50.97% of the shares of Bayer ABS Limited. Bayer ABS Limited is listed on the Bombay Stock Exchange in India. Under the applicable Indian regulations, an obligation may exist, in connection with the Spin-off, to make a public offer to purchase the remaining shares of Bayer ABS Ltd. The costs for purchasing these shares would be determined by the share price as calculated under the relevant regulations and the number of stockholders who accepted the purchase offer.

There would be no assurance that the purchase price that may have to be paid by LANXESS in connection with the public offer would reflect the value of the shares in Bayer ABS Limited that are to be acquired.

Risks arising from the Admission to the Stock Exchange

Effects on the stock market price of LANXESS Shares resulting from the stockholders' behaviour immediately following admission to the stock exchange

Immediately after the Spin-off enters into effect, all shares of LANXESS AG will be held by Bayer stockholders. From the investors' point of view, however, the chemicals and polymers business activities combined in the LANXESS Group have different risk profiles and therefore generally appeal to different groups of investors than do the business activities remaining with the Bayer Group. In addition, certain institutional investors may be forced by their investment guidelines to sell their holdings in the Company, irrespective of their assessment of the prospects for LANXESS shares. Therefore, the possibility cannot be excluded that some of Bayer's stockholders, who will become simultaneous LANXESS stockholders when the Spin-off takes effect, will decide immediately or shortly after the shares are listed to sell their LANXESS Shares in accordance with their risk preferences, investment strategies or investment guidelines in effect at the time.

In connection with the Spin-off, the holders of Bayer ADRs have been given an option to choose by 27 January 2005 whether they wish to receive the LANXESS Shares or arrange for them to be sold. If no instructions with respect to the exercise of the option are issued by the holders of Bayer ADRs by this date, the depositary bank will deem such holders to have elected to sell their LANXESS Shares. Such LANXESS Shares, together with those with respect to which explicit instructions for sale have been received, will be sold on behalf of the depositary bank as promptly as practicable following the delivery of the LANXESS Shares consistent with prevailing market conditions. The Company assumes that this sale — which may, if necessary, be effected in several tranches — will occur, subject to market conditions, within four trading days following the delivery of the LANXESS Shares. Fractional rights will be aggregated and the whole shares resulting therefrom will be sold. The proceeds from this sale will be remitted to the relevant holders of Bayer ADRs. On 15 December 2004, Bayer ADRs constituted approximately 4.6% of Bayer AG's capital stock. The possibility that a large percentage of the LANXESS Shares allotted to holders of Bayer ADRs will be sold in connection with the exercise of the option cannot be excluded.

If a significant number of stockholders or holders of Bayer ADRs sell or arrange for the sale of their LANXESS Shares within a short period of time or if the impression arises that such sales are likely, then the market price of LANXESS Shares could decline.

On the basis of the stockholder resolution dated 15 September 2004, LANXESS AG issued a convertible bearer bond to Bayer AG in the nominal amount of €200 million with a term expiring on 15 September 2007 (see also ''*Business Transactions and Legal Relationships with Related Parties — Business Transactions and Legal Relationships with the Bayer Group*''). Pursuant to the terms and conditions of the convertible bond, the bondholder may convert the convertible bonds into shares in LANXESS AG (conversion right) between 20 July 2005 and 20 July 2007. In addition, the bondholder is obliged to convert the convertible bonds into shares in LANXESS AG on 15 September 2007 (conversion duty). Should Bayer AG hold the convertible bond, either in whole or in part, at the time the conversion right is exercised or the conversion duty arises, it will obtain an ownership interest in LANXESS AG. The extent of the ownership interest will significantly depend on the percentage of the convertible bond Bayer AG still holds at that time, the initial market price of the LANXESS shares (in simplified terms, the average share price during the first ten trading days) and the market price of LANXESS shares on the date the conversion right is exercised or the conversion duty arises, as the case may be (in simplified terms, the average share price during the first 20 trading days prior to the exercise of the conversion right or the date on which the conversion duty arises, as the case may be).

In the Joint Spin-off Report prepared in connection with the Spin-off, Bayer AG stated that, in the event of a conversion, it does not intend to retain these LANXESS Shares for the long term. If Bayer AG sells a significant portion of its LANXESS Shares thus acquired in a single transaction or within a short period of time, or if the impression arises that such a sale is likely, then this could have an adverse effect on the development of the share price of the LANXESS Shares. Moreover, it could be difficult for LANXESS AG in such a situation to issue new shares at what it considers to be a favourable time and at a reasonable price.

Development of a liquid market

No public trading existed in shares in LANXESS AG prior to the stock exchange listing. There is no guarantee that, following the initial listing of LANXESS shares, a liquid market for trading in these shares will develop and become established.

Volatility of the LANXESS share price

Following the commencement of trading, the price of shares in LANXESS AG may be exposed to significant fluctuations, in particular as a result of fluctuations in the actual or projected results of operations, changes in the earnings forecast or the failure to meet the earnings expectations of securities analysts, changes in general economic conditions and other factors. In addition, general share price volatility — particularly with respect to shares in companies in the chemicals industry — could lead to pressure on the price of shares in LANXESS AG, without such pressure necessarily being based on the business or the earnings prospects of LANXESS AG.

Selected Consolidated Financial Data

The selected consolidated financial data set forth below are merely a summary of the Combined Financial Statements for the years 2002 and 2003 as well as for the first nine months of 2003 and 2004. These data should be read in conjunction with the section entitled ''*Management's Discussion and Analysis of Financial Condition and Results of Operations*'' and the LANXESS Group's Combined Financial Statements and the Notes thereto included in the financial section of this Listing Memorandum.

The following selected financial data for the years 2002 and 2003 as well as for the first nine months of 2003 and 2004 have been derived from the Combined Financial Statements. The assets and liabilities to be transferred to the LANXESS Group were recognised and valued in the Combined Financial Statements in accordance with the standards issued by the International Accounting Standards Board (''IASB''), London, in effect as of the closing date of the financial statements. There are several material differences between the International Financial Reporting Standards (''IFRS'') and U.S. Generally Accepted Accounting Principles (''U.S. GAAP'').

The Combined Financial Statements generally present LANXESS as if the Group had already existed in the past and had the structure defined for the Spin-off. Underlying the selected financial data is an assumption that the role of LANXESS AG as the Group parent company and the legal structure below this Company, in effect after the Spin-off of the LANXESS Group takes effect, had already been in place as of 1 January 2002. IFRS do not contain any rules for allocating assets and liabilities in the Combined Financial Statements. The allocation of business activities to the LANXESS Group was authoritatively based on the relevant provisions of the agreements executed for the formation of LANXESS. The legal entities to be transferred (so-called ''Share Deals'') were accordingly reported in the Combined Financial Statements on the basis of their legal structure. Business activities (so-called ''Asset Deals'') were generally reported on the basis of the reporting structures of the Bayer Group authoritative for financial controlling purposes having regard to the contractual arrangements between LANXESS and the Bayer Group. In preparing the Combined Financial Statements, additional assumptions and estimates had to be made, which have an effect on the amounts and presentation of assets and liabilities, income and expenses and contingent liabilities. Actual figures could differ from the estimates. The section ''*Basis for Financial Statement Reporting*'' in the Notes to the Combined Financial Statements appearing in the financial section contains a more detailed description of those allocation procedures and their limitations that are material in this context.

In the 2002 Combined Financial Statements contained in the Joint Spin-off Report, a portion of property, plant and equipment already existing as of 1 January 2002 was erroneously reported as additions, thus leading to an error amounting to €94 million in the presentation of 2002 capital expenditures and amounting to €40 million in the presentation of 2002 depreciation and write-downs of property, plant and equipment. This technical error was corrected in the following financial data and the 2002 Combined Financial Statements contained in the financial section of this Listing Memorandum and did not have an effect on either the 2002 balance sheet and income statement, or on the financial data and financial reports for subsequent periods. The correction of this error led most importantly to a decrease of €40 million in net cash provided by operating activities, a decrease of €94 million in net cash used in investing activities and a decrease of €54 million in net cash provided by (used in) financial activities. Segment data were changed accordingly. The Group financial statements (the Combined Financial Statements according to IFRS) of the LANXESS Group as of 31 December 2003 were audited and issued with an unqualified audit opinion by PwC Deutsche Revision Aktiengesellschaft, Wirtschaftsprüfungsgesellschaft, Essen.

Consolidated Income Statement Data

All figures in € millions	Fiscal year ending 31 December - audited - 2002	2003	1 January to 30 September - unaudited - 2003	2004
Net sales	6,763	6,315	4,828	5,047
Cost of goods sold	(5,285)	(5,211)	(3,919)	(3,937)
Gross profit	1,478	1,104	909	1,110
Selling expenses	(985)	(935)	(683)	(638)
Research and development expenses	(149)	(168)	(118)	(95)
General and administrative expenses	(202)	(257)	(162)	(196)
Other operating expenses, less other operating income	(261)	(1,041)	(23)	(105)
Operating result	(119)	(1,297)	(77)	76
Non-operating result	(89)	(111)	(92)	(58)
Income (loss) before income taxes	(208)	(1,408)	(169)	18
Income taxes	90	412	60	(21)
Income (loss) after taxes	(118)	(996)	(109)	(3)
Minority stockholders' interest	(1)	(1)	(4)	(5)
Net income (loss)	(119)	(997)	(113)	(8)

Consolidated Balance Sheet Data

All figures in € millions	As of 31 December - audited - 2002	2003	As of 30 September - unaudited - 2003	2004
Non-current assets	3,021	1,690	2,724	1,675
Current assets (including prepaid expense items and deferred taxes)	2,598	2,841	2,793	3,008
of which liquid assets	10	13	14	80
Stockholders' equity	2,465	1,358	2,294	1,366
Liabilities (including deferred income items and deferred taxes)	2,427	2,317	2,404	2,359
of which long-term financial obligations	446	209	173	336
Provisions	688	813	778	924
of which provisions for pensions and other post-employment benefits	324	408	361	412

Consolidated Cash Flow Data

All figures in € millions	Fiscal year ending 31 December - audited - 2002	2003	1 January to 30 September - unaudited - 2003	2004
Cash inflow/(outflow) from operating activities	369	346	205	40
Cash inflow/(outflow) from investing activities	(347)	(300)	(148)	85
Cash inflow/(outflow) from financing activities	(25)	(46)	(56)	(59)
Change in cash and cash equivalents due to business activities	(3)	0	1	66

Other Financial Data

All figures in € millions	Fiscal year ending 31 December - audited - 2002	2003	1 January to 30 September - unaudited - 2003	2004
Operating result (EBIT)	(119)	(1,297)	(77)	76
of which exceptional items*	(244)	(1,178)	(42)	(81)
EBITDA*	507	180	300	325
of which exceptional items*	(80)	(131)	(25)	(60)
Capital expenditures	393	312	193	158

* EBITDA is defined as operating result (EBIT) plus depreciation and amortisation. EBITDA and exceptional items are not financial data defined under IFRS and should not be considered in isolation as a substitute for net income, operating result or other measures of financial performance under IFRS. Potential investors should be aware that EBITDA and exceptional items are not consistently applied or standardised, that there may be material differences in the way in which companies calculate them and that they, considered in isolation, do not establish a basis for comparison with similarly-named performance measures of other companies.

Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of financial condition and results of operations should be read together with the Combined Financial Statements of the LANXESS Group and the related Notes, which are reprinted elsewhere in this Listing Memorandum.

The forward-looking statements in this section are not guarantees of future performance of the LANXESS Group. These statements entail both risks and uncertainties. Several factors could cause the actual financial data of the LANXESS Group to differ materially from those anticipated by these statements. Many of those factors are macroeconomic in nature or are otherwise beyond the control of LANXESS AG's Board of Management. See ''*General Information — Forward-looking Statements*''.

The determination of the LANXESS Group's financial data presented in this section is based on certain assumptions with respect to the accounting and valuation methods described herein and in the Notes to the Combined Financial Statements. For a more detailed description of these assumptions, see the section entitled ''— *Overview — Discussion of critical accounting and valuation policies and methods*''.

The LANXESS Group is a global chemicals company. Its portfolio includes basic, specialty and fine chemicals as well as polymers. The LANXESS portfolio consists primarily of products that have reached a relatively high level of market maturity and are therefore exposed to rather low barriers to market entry and growth rates. Generally lower margins require the creation of lean and simple structures and a commitment to optimising equipment and processes.

Overview

Bases for financial statement reporting

In order to reflect the structure of the LANXESS Group (as defined for the Spin-off) in the historical financial data for the LANXESS Group, two steps were taken in preparing the financial data for the LANXESS Group for the period from 1 January 2002 until 30 September 2004. The first step was to define certain companies and business areas of the Bayer Group as LANXESS-relevant business. The second step was to combine such companies and business areas.

The chemicals and polymers activities combined in LANXESS were first reported under ''Discontinuing Operations'' in accordance with IAS 35 in the 2003 Bayer consolidated financial statements. The LANXESS Group was first reported as an independent segment in the Bayer Group's quarterly report for the first quarter 2004. The Combined Financial Statements, which are included in this section and which are derived from the Bayer Group's consolidated reporting, differ from the Discontinuing Operations data in terms of their stated objectives. The objective of Discontinuing Operations reporting is to present the discontinuing business as an integral part of the Bayer Group (*i.e.*, after consolidating all intra-Group transactions), while the Combined Financial Statements are intended to present the business on an independent group basis. Thus, information concerning the future LANXESS Group's historical financial condition and results of operations is intended to be conveyed based on the fictitious assumption that the structure of the future LANXESS Group had already existed in the past.

In principle, the demarcation of the business to be transferred is based on the consolidated reporting structures and, therefore, the reporting units underlying those structures. For this reason, diverging allocations of individual products below this level are not taken into account. However, these deviations are the exception and, based on current knowledge, would not, in the aggregate, result in any materially different statements for the LANXESS Group.

In preparing the Combined Financial Statements, assumptions and estimates must be made which have an effect on the amounts and presentation of assets and liabilities, income and expenses and contingent liabilities. Actual figures could differ from the estimates. The Combined Financial Statements presented in this section therefore do not necessarily reflect the financial condition and results of operations that would have resulted had the LANXESS Group already existed as an independent group as of 1 January 2002 and the underlying transactions between the LANXESS and Bayer companies thus been entered into between independent companies.

Specifically, assumptions were made as to net debt and interest expense, which are dependent on the capital structure of the future LANXESS Group. The section entitled ''— *Liquidity and Capital Resources — Financing and Liquidity*'' contains a description of the assumptions used to calculate the interest expense. For the reasons set forth herein, the absence of historical unity and independence of the LANXESS Group limits the informative value of the Combined Financial Statements. Therefore, the Combined Financial Statements do not enable reliable forecasting of the future development of the businesses combined in the LANXESS Group.

Supply and services relationships between the Bayer Group and the LANXESS Group

The material supply and services relationships between the Bayer Group and LANXESS Group are described in the section entitled ''*Business Transactions and Legal Relationships with Related Parties — Business Transactions and Legal Relationships with the Bayer Group*''.

Discussion of critical accounting and valuation policies and methods

Critical accounting and valuation policies and methods are those that are both most important to the portrayal of the LANXESS Group's financial condition and results of operations and that require the application of difficult, subjective and complex judgments, often as a result of the need to make estimates about the effects of matters that are inherently uncertain and may change in subsequent periods. The Company's Board of Management is not aware of any reasonably possible events or circumstances, other than those disclosed in this Listing Memorandum, that would result in the reporting of different figures and that would have a material adverse effect on the financial condition and results of operations of the LANXESS Group.

The significant accounting and valuation policies and methods of the LANXESS Group are outlined in the Notes to the Combined Financial Statements. While not all of these significant accounting policies require difficult, subjective or complex judgments, the Board of Management of the Company believes that the following accounting policies could be considered critical.

Accounting for intangible assets and property, plant and equipment

Intangible assets (including goodwill) and property, plant and equipment are amortised over their estimated useful lives. The estimated useful lives are based on estimates of the period during which the assets will generate revenue.

Intangible assets and property, plant and equipment are tested for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may no longer be recoverable. Impairment testing under IAS 36 (Impairment of Assets) requires the Board of Management of the Company to compare the carrying value of the assets to the future discounted estimated cash flows from the related assets. Determining the future discounted estimated cash flows involves significant estimations, particularly with regard to future sales prices and sales volumes, costs and risk-adjusted discount rates. The discounting process is also based on assumptions and estimations relating to business-specific costs of capital, which, in turn, are based on country risks, credit risks and additional risks resulting from the volatility of the respective line of business as well as the relevant capital structure of the LANXESS company in question.

As described in more detail in the section entitled ''— *Results of Operations — Factors Influencing Net Sales, Results of Operations and Cash Flows of LANXESS — Most important factors in fiscal year 2003 and the first nine months of 2004*'', in November 2003 the Bayer Group considered it necessary to review the carrying amount of its global assets as part of an impairment test conducted in accordance with IAS 36.

Although the Company's Board of Management believes that its estimates of the relevant expected useful lives, its assumptions concerning the macroeconomic environment and developments in the industries in which LANXESS operates and its estimations of the future discounted cash flows are appropriate, changes in assumptions or circumstances could require the LANXESS Group to change this analysis. This could lead to additional impairment charges or write-backs in future should the trends identified by the Board of Management of the Company reverse (or the assumptions or estimates of LANXESS AG's Board of Management prove incorrect). This would impact the future results of the LANXESS Group.

Until the end of 2004, LANXESS amortised goodwill in accordance with its scheduled useful life. Beginning on 1 January 2005, scheduled amortisation will no longer be conducted, but instead an annual impairment review will be performed. Beginning on 31 March 2004, under IFRS 3, any goodwill recorded prior to that date will require an annual impairment review. In contrast, for business combinations with closing dates on or after 31 March 2004, IFRS 3 must already be applied, even if the acquisition occurs prior to 1 January 2005. In general, the process of evaluating goodwill involves making adjustments and estimates relating to the projection and discounting of future cash flows. These evaluations are linked closely to the assumptions made by the Board of Management of LANXESS AG regarding the future development of the assets concerned and any changes in the discount rate applied by the LANXESS Group. An increase in the discount rate increases the likelihood of impairment charges.

Accounting for pensions and other obligations

The companies of the LANXESS Group offer pension and other retirement plans in various forms to employees who meet the relevant plan's eligibility requirements. These plans cover the majority of LANXESS employees. LANXESS uses several statistical and other models that attempt to anticipate future events in calculating the expenses and liabilities related to the plans. Factors influencing the calculation include, for example, assumptions about the discount rate, expected return on plan assets and rate of the participants' future compensation increases. Actuarial consultants also use statistical information, such as withdrawal and mortality rates, to estimate these factors. The actuarial assumptions used may differ materially from actual results due to changing market and economic conditions, higher or lower withdrawal rates, or longer or shorter life spans of participants. Such differences could have a significant impact on the amount of the pension income or expenses recorded in future years for the LANXESS Group.

Accounting for environmental provisions

As described in Note (27) to the Combined Financial Statements for fiscal year 2003, LANXESS' business is subject to a variety of laws and regulations in the jurisdictions in which it does business or maintains properties. Where such legislation relates to environmental protection, the LANXESS Group may be compelled to remove or mitigate the effects of the disposal or release of chemical substances at various sites. Provisions for expenses that may be incurred in complying with such laws and regulations are set aside, if environmental investigations have been ordered or safety and remediation measures are probable, the cost can be sufficiently and reliably estimated, and no future benefits are expected from such measures. Significant factors in estimating the costs include previous experiences in similar cases, expert opinions regarding environmental programmes, current costs and new developments affecting costs, the interpretation of current environmental laws and regulations by LANXESS management, the number and financial condition of third parties that may become obliged to participate in any remediation costs at the various sites on the basis of joint liability, and the safety and remediation measures likely to be deployed. Changes in these factors could impact future reported results. The material provisions of the master agreement concerning the apportionment of contingent liabilities as between LANXESS AG and Bayer AG with regard to environmental and other matters are described in the section entitled ''*Business Transactions and Legal Relationships with Related Parties — Business Transactions and Legal Relationships with the Bayer Group — Master Agreement between LANXESS AG and Bayer AG*''. Environmental provisions for the relevant reporting periods are presented in Note (27) to the Combined Financial Statements for fiscal year 2003 (see also ''*Information Concerning the Business of LANXESS — Environment*'').

Income tax accounting

The LANXESS Group is required to make estimates for purposes of determining provisions for income taxes and deferred tax assets.

In addition, estimates must be made to determine whether valuation allowances are required against deferred tax assets in respect of the availability of tax loss carry forwards. Such valuation allowances are recognised when it is no longer sufficiently certain that the advantages from tax loss carry forwards will be realised. Uncertainties exist with respect to the interpretation of complex tax regulations and the amount and timing of future taxable income. Any differences between actual results and the assumptions made by LANXESS or any future changes to such assumptions could result in an adjustment of the future tax expense of the LANXESS Group. Currently existing tax-related risks are described in the section entitled ''*Risk Factors — Risks relating to the Spin-off and Strategic Realignment of LANXESS — Tax consequences in connection with the Spin-off and the preparatory measures implemented for this purpose*''.

Results of Operations

Factors Influencing Net Sales, Results of Operations and Cash Flows of LANXESS

General factors

The most important factors influencing net sales, results of operations and cash flows of LANXESS are:

- currency exchange rate development of the euro, particularly relative to the U.S. dollar, and
- costs of raw materials and energy in connection with the manufacture of LANXESS products.

The following sections describe these key factors.

Exchange rate fluctuations

Since a portion of the assets, liabilities, sales and earnings of LANXESS are denominated in currencies other than the euro, such items are exposed to exchange rate fluctuations in the values of these currencies relative to the euro. The Group is therefore subject to both transaction risk (*i.e.*, sales are generated in one currency but costs relating to those revenues are incurred in a different currency) and translation risk (*i.e.*, the risk connected with the necessary currency translation of the annual financial statements of non-euro zone subsidiaries when preparing the consolidated financial statements).

As a general rule, an increase in the value of the euro relative to the U.S. dollar and other currencies as a result of transaction risks has two inter-related consequences:

- reduced or negative margins (in euros), if the costs were incurred in euros and the relevant sales were generated in currencies weaker than the euro, and
- reduced competitiveness since the products manufactured in Europe were produced at constant cost (in euros).

Over time, transaction risks could therefore adversely affect the cash flows and results of operations of the LANXESS Group to the extent it is unable to reflect changes in exchange rates in the pricing of the products in local currency. The effects of the transaction risks are not quantified in the Combined Financial Statements.

Currency translation risks do not affect local currency cash flows or results of operations but do affect the consolidated annual financial statements. In general, an increase in the euro value relative to the U.S. dollar and other currencies will result in a lower euro value of the sales generated in currencies that have depreciated relative to the euro. If the non-euro denominated expenses do not match the non-euro denominated sales, this currency difference may have an adverse effect on the operating result of the LANXESS Group.

Additional information on transaction and currency translation risks are contained in the section ''*— Management of Market Price Risks at LANXESS*''.

Costs of raw materials and energy

The prices of raw materials for LANXESS products probably have the most significant effect on Group costs. In order to reduce its dependency on outside sources of supply, LANXESS manufactures raw materials internally, to the extent commercially feasible. Petrochemical products, which are not manufactured by LANXESS itself, are a key source material for a variety of LANXESS products. For production at LANXESS, the most important petrochemical raw materials by far include 1, 3-butadiene and styrene. Other important petrochemical raw materials are acrylonitrile, benzene, C4 raffinate 1, cyclohexane, isobutylene and toluene. Other significant raw materials include the basic chemicals ammonia, aniline, chlorine and sodium hydroxide. Crude oil prices, which increased dramatically throughout 2004, especially during the third quarter, are a particularly volatile variable for the above-mentioned petrochemical products. Scarcity in raw materials due to increasing demand, capacity bottlenecks among suppliers of raw materials and energy, and governmental and non-governmental regulations are significant factors that have historically affected the volatility of raw material prices and could affect them again in future. By entering into agreements with price escalation clauses to adjust its sales prices based on increases in energy and raw materials prices and by executing corresponding hedging transactions, LANXESS seeks to offset energy price increases. Nevertheless, since price adjustment agreements have been concluded with only a limited number of customers and since volatilities can only partially be eliminated through active financial management, fluctuations in raw material prices could have an adverse effect on the LANXESS Group’s results of operations. Moreover, contractually enforceable price adjustments can sometimes only be passed on to customers partially or with delay. The possibility cannot be excluded that existing contracts may not permit increases in raw material prices to be taken into account. While the Polybutadiene Rubber business unit is largely able to pass on increases in raw materials prices to its customers since sales agreements executed by that business unit are generally based on pre-set price formulas, such agreements do not exist for most other business units. Among these business units, the key factors determining the extent to which price adjustments can be made on the basis of changes in the cost of raw materials are the respective market position of the LANXESS business, market demand and capacity utilisation. This effect could be aggravated by additional cost increases outside of LANXESS’ control in the form of future legislative changes relating to the environmental tax in Germany. In particular, it is uncertain whether the special regulations governing the manufacturing industry will continue to apply after 2006. Additional obligations may therefore arise for all German LANXESS manufacturing companies, including companies in which they hold shares.

Most important factors in fiscal year 2003 and the first nine months of 2004

The most significant factors influencing LANXESS’ results in fiscal year 2003 were the impairment charges.

In November 2003, the Bayer Group considered it necessary to review the carrying amount of its global assets as part of an impairment test conducted pursuant to IAS 36. The impairment test was performed, in particular, in connection with unfavourable economic developments in various business lines. These developments were caused primarily by a number of anticipated adverse external factors such as sustained unfavourable price trends, especially higher raw material costs, that could only be passed on to customers to a limited extent. An additional underlying cause was lower sales volume growth as a result of tougher competition caused partially by global overcapacities. Moreover, lower expectations regarding macroeconomic growth and sustained unfavourable currency exchange rates played a role. For more details concerning this impairment test, see the section entitled ‘‘*Global Impairment Testing Procedures and Impact*’’ in the Notes to the Combined Financial Statements contained in the financial section of this Listing Memorandum. For the LANXESS Group, this impairment test yielded impairment charges of €988 million in fiscal year 2003, compared to impairment charges of €84 million in fiscal year 2002. The impairment charges in 2003 were recorded in the line item ‘‘Other operating expenses’’. The write-downs related primarily to the Styrenic Resins and Fine Chemicals business units and also the Technical Rubber Products business unit. In the first nine months of 2004, net impairment charges amounted to €21 million.

In 2003, the net sales and operating result of the LANXESS Group were also significantly affected by changes in exchange rates, particularly between the euro and U.S. dollar. The euro strongly appreciated relative to the U.S. dollar and other currencies in 2003. This trend continued until the end of February 2004. Thereafter, the euro exchange rate stabilised at a level that remained, until the end of the first nine months of 2004, higher than the average exchange rate for the prior-year period.

In the first half of 2003, crude oil prices were about 10% higher than the previous year's average. In the second half of the year, prices declined to the levels of early 2002, which were somewhat higher than the 2002 average. 2004 saw rapid increases in crude oil prices, with occasional small price declines, into October.

LANXESS Group

The following table shows the net sales and results of the LANXESS Group for the periods specified.

	Fiscal year 2002 - audited -	Fiscal year 2003 - audited -	Change from prior year	1 January to 30 September 2003 - unaudited-	1 January to 30 September 2004 - unaudited -	Change from prior-year period
	(in € millions)	(in € millions)	(%)	(in € millions)	(in € millions)	(%)
Net sales	6,763	6,315	(6.6)	4,828	5,047	4.5
Cost of goods sold	(5,285)	(5,211)	1.4	(3,919)	(3,937)	(0.5)
Gross profit	1,478	1,104	(25.3)	909	1,110	22.1
as a percentage of net sales (%)	21.9	17.5	—	18.8	22.0	—
Selling expenses	(985)	(935)	5.1	(683)	(638)	6.6
Research and development expenses	(149)	(168)	(12.8)	(118)	(95)	19.5
General and administrative expenses	(202)	(257)	(27.2)	(162)	(196)	(21.0)
Other operating expenses, less other operating income	(261)	(1,041)	*	(23)	(105)	*
Operating result	(119)	(1,297)	*	(77)	76	—
as a percentage of net sales (%)	—	—	—	—	1.5	—
of which exceptional items**	(244)	(1,178)	*	(42)	(81)	(92.9)
Non-operating result	(89)	(111)	(24.7)	(92)	(58)	37.0
Income (loss) before income taxes	(208)	(1,408)	*	(169)	18	—
Net income (loss)	(119)	(997)	*	(113)	(8)	92.9

* Change of more than 100%.

** Exceptional items are not defined under IFRS.

The following table shows a geographical breakdown of net sales based on the regions in which the LANXESS Group sold its products.

	Fiscal year 2002 - audited -	Fiscal year 2003 - audited -		Change from prior year	1 January to 30 September 2003 - unaudited -	1 January to 30 September 2004 - unaudited -		Change from prior-year period
	(in € millions)	(in € millions)	(% total)	(%)	(in € millions)	(in € millions)	(% total)	(%)
Europe	3,606	3,565	56.5	(1.1)	2,720	2,804	55.5	3.1
North America	1,567	1,346	21.3	(14.1)	1,053	1,058	21.0	0.5
Asia/Pacific Rim	1,019	887	14.0	(13.0)	672	750	14.9	11.6
Latin America/Africa/ Middle East	571	517	8.2	(9.5)	383	435	8.6	13.6

Based on the LANXESS Group's intended future segmentation of sales regions, sales in fiscal year 2003 were generated as follows: 25% in America, 34% in Europe, Middle East and Africa (excluding Germany), and 14% in Asia (including Pacific Rim countries). Based on this new geographic segmentation, 27% of sales were generated in Germany in fiscal year 2003.

Fiscal year 2003 compared with fiscal year 2002

Net sales

Net sales represent the gross inflow of economic benefits received or receivable by the LANXESS Group from the sale of goods and services. Net sales do not include rebates and discounts that LANXESS grants its customers, nor any amounts that it collects on behalf of third parties such as sales taxes, goods and services taxes and value added taxes.

In 2003, the Group's net sales declined by 6.6% from the previous year — from €6,763 million to €6,315 million — primarily as a result of unfavourable exchange rate effects (€353 million) and portfolio effects (€58 million). The portfolio effect resulted from the sale of the Organic Pigments product group in 2003. The Combined Financial Statements generally reflect the target structure of the LANXESS Group. However, transactions completed after 1 January 2002 with respect to individual product groups — primarily the sale of Organic Pigments — are included in the Combined Financial Statements as of the date on which they took economic effect. Organic Pigments was sold to the Sun Chemicals Group in the United States for a purchase price of €46 million, which was offset against asset disposals totalling €41 million and transaction and other costs in the amount of €5 million.

In 2003, net sales generated by the Chemical Intermediates segment as a percentage of LANXESS Group net sales increased from 21.4% to 22.3% and the share generated by the Performance Chemicals segment rose slightly from 30.4% to 30.5%. The Performance Rubber segment's percentage of Group net sales fell slightly from 21.9% to 21.8% in 2003, while that of the Engineering Plastics segment remained at 22.2%.

Gross profit

Gross profit represents net sales after deducting the cost of goods sold. Cost of goods sold includes both the production costs for the goods sold as well as the costs of goods purchased for resale.

The cost of goods sold (cost of services provided) declined by 1.4% from €5,285 million in 2002 to €5,211 million in 2003. Currency effects more than offset cost increases triggered by higher energy and raw material prices. Gross profit declined from €1,478 million to €1,104 million. This represented a decline in the gross profit margin from 21.9% to 17.5%.

Operating result (EBIT)

Operating result represents gross profit after deducting selling expenses, research and development expenses, general and administrative expenses and other operating expenses and income.

In 2003, selling expenses declined by 5.1% or from €985 million to €935 million compared to the previous year. This decline was caused primarily by currency effects.

Research and development expenses rose by 12.8% from €149 million to €168 million. This increase can be attributed to, among other things, one-time charges for the closure of research and development facilities.

The 27.2% increase in general and administrative expenses (from €202 million to €257 million) resulted primarily from a change in reporting necessitated by organisational changes. In the formation of the subgroup, certain functions, for which expenses had previously been allocated among various function costs, were centralised. These expenses are now reported under administrative expenses, thereby reducing the amounts of the other function costs — especially cost of goods sold and selling expenses. In addition, currency effects of €12 million, write-downs on software made in the course of restructuring, and personnel expenses associated with restructuring had negative impacts.

Other operating expenses and income rose to €1,041 million. Other operating expenses totalled €1,098 million, whereas other operating income accounted for €57 million. Other operating expenses included primarily impairment charges totalling €988 million, litigation costs totalling €15 million and restructuring charges of €12 million. In fiscal year 2002, other operating expenses amounted to €337 million (including restructuring charges of €144 million, impairment charges of €84 million and write-downs of software amounting to €8 million), and other operating income totalled €76 million. Notes (13) and (14) to the Combined Financial Statements for fiscal year 2003 discuss the cost of materials and personnel expenses.

Operating result deteriorated from a €119 million loss to a €1,297 million loss. This was caused in particular by net exceptional items of €934 million. In fiscal year 2003, exceptional items totalled €1,178 million (of which €131 million affected EBITDA), while exceptional items in fiscal year 2002 totalled €244 million (of which €80 million affected EBITDA). The €1,178 million in expenses incurred in fiscal year 2003 were attributable to impairment charges (€988 million), asset write-downs (€59 million) (of which €57 million related to software), expenses associated with the early retirement programme implemented at the Group level (€67 million), site closure and other restructuring expenses (primarily staff adjustment programmes) (€48 million), and litigation costs (€15 million). Except for the 2003 exceptional items described in the preceding paragraph and amounting to €1,015 million, the above-mentioned expenses were allocated among the various function costs. An amount totalling €13 million relating to write-downs of software was not allocable to any reporting segment. In fiscal year 2002, impairment charges of €84 million, restructuring expenses of €72 million primarily relating to the closing of various sites and production facilities, asset write-downs in connection with this restructuring amounting to €72 million, write-downs of software totalling €8 million (all collectively reported in the line item ''other operating expenses''), and miscellaneous reorganisation measures totalling €8 million (allocated among the remaining function costs) were incurred. In 2002, an amount equalling €6 million (of which €1 million was attributable to software write-downs) was not allocable to any of the reporting segments.

Non-operating result

The non-operating result declined from a €89 million loss in fiscal year 2002 to a €111 million loss in fiscal year 2003. This was predominantly attributable to losses from investments in affiliated companies totalling €15 million (compared to a break-even result in 2002) and a €10 million increase in interest expenses on pensions. This could only be partially offset by an increase in interest income of €17 million.

Income (loss) before income taxes

Losses before income taxes worsened from €208 million in 2002 to €1,408 million in 2003.

Income taxes

Taxes paid or owed on income and other revenues in the individual jurisdictions, as well as any deferred taxes, are reported under income taxes. In 2003, an income tax credit of €412 million was reported, compared to an income tax credit of €90 million in 2002. The effective tax rate of the LANXESS Group was 29.3% compared to 43.3% in the previous year. Future actual tax results of LANXESS are dependent on the legal structure and tax strategy of the LANXESS Group as an independent organisation. For additional details on income taxes, see Note (9) to the Combined Financial Statements for fiscal year 2003.

Net income (loss)

In 2003, the LANXESS Group reported a net loss of €997 million after minority stockholders' interest of €1 million. In the previous year, the Group reported a net loss of €119 million after minority stockholders' interest of €1 million.

First nine months of 2004 compared with the first nine months of 2003

Net sales

The LANXESS Group's net sales in the first nine months of 2004 increased by 4.5% over the prior-year period, from €4,828 million to €5,047 million. A €351 million increase in sales due to higher prices and volumes was offset by negative currency effects amounting to €132 million and arising primarily in the U.S. dollar regions.

Sales of the Engineering Plastics segment as a percentage of LANXESS Group sales increased in the first nine months of 2004 over the prior-year period from 22.0% to 25.4%. In contrast, the

Performance Rubber segment's share of Group sales in the first nine months of 2004 declined from 21.5% to 20.7% compared to the prior-year period, while the share of the Chemical Intermediates segment fell from 22.4% to 21.8% and that of the Performance Chemical segment declined from 31.1% to 28.9%.

Gross profit

Gross profit improved by 22.1% over the prior-year period, increasing from €909 million to €1,110 million. The gross profit margin thereby increased by 3.2% to 22.0%.

The costs of goods sold (and of services provided) rose only slightly (0.5%) compared to the first nine months of 2003, from €3,919 million to €3,937 million. The lower write-downs (by €100 million) in connection with the impairment performed at the end of 2003 as well as the lighter burden of currency effects on cost of goods sold (by €108 million) contributed to offsetting most of the energy and raw material costs, which had risen in some cases.

Operating result (EBIT)

Selling expenses declined by 6.6% or from €683 million to €638 million in the first nine months of 2004 compared to the prior-year period. This decline resulted primarily from currency effects (€13 million), cost reductions resulting from organisation-related reallocations of costs among the line items (see notes to the general administrative expenses in the section entitled ''— *Fiscal Year 2003 compared with fiscal year 2002*''), a €3 million net drop in commission expenses, licence expenses and other rebates and discounts and a €2 million reduction in advertising and information expenses.

Compared to the first nine months of 2003, research and development expenses declined by 19.5% from €118 million to €95 million. The reduction in research activities initiated at the end of 2003 — primarily at the Leverkusen site — as well as the relocation of employees to other functional areas were among the factors in this development.

The 21.0% increase in general and administrative expenses (from €162 million to €196 million) was primarily attributable to cost increases resulting from organisation-related reallocations of costs among the line items as well as the relocation of employees to other functional areas. Currency effects had a partially offsetting effect.

Other operating expenses (reduced by other operating income) increased by €82 million from €23 million to €105 million in the first nine months of 2004 compared to the prior-year period. The main cause of this cost increase was the creation of environmental provisions (€40 million) in the third quarter as well as the establishment of a litigation reserve (€20 million). Operating result was moreover reduced by a goodwill impairment in the RheinChemie business unit of €20 million and net impairment charges of €13 million (after write-backs totalling €5 million) in the Fine Chemicals business unit. In contrast, net write-backs in the Styrenic Resins business unit amounted to €12 million (after impairment charges of €12 million). In the first nine months of 2003, the line item ''other operating expenses'' included €12 million in restructuring costs relating to the Antwerp site.

Operating result improved significantly by €153 million from a €77 million loss in the first nine months of 2003 to a €76 million profit in the first nine months of 2004, primarily as a result of increased sales, a proportionately smaller increase in the cost of goods sold and the reduction in the remaining function costs. Charges relating to environmental protection, impairment and restructuring, as well as costs incurred in connection with litigation, had a €39 million total negative impact on earnings. Exceptional items in the first nine months of 2004 totalled €81 million (of which €60 million affected EBITDA) and, as described above, were reported in the line item ''other operating expenses''. Exceptional items in the prior-year period amounted to €42 million, of which €25 million affected EBITDA and of which restructuring costs totalling €12 million were reported in ''other operating expenses''. Exceptional items for the prior-year period also included asset write-downs of €17 million (which, in turn, included write-downs of software of €13 million, which could not be allocated to any individual segment) and expenses relating to site closures and other restructuring measures, primarily related to the Marl site, of €13 million. These items were assigned to the various function costs.

Non-operating result

The non-operating loss improved by 37.0% from €92 million to €58 million primarily as a result of an increase in net income from investments in affiliated companies, lower interest expenses (regarding the determination of interest expenses please refer to the description in the section entitled ''— *Liquidity and Capital Resources — Financing and Liquidity*'') and greatly improved currency results.

Income (Loss) before income taxes

Income before income taxes improved from a loss of €169 million in the first nine months of 2003 to a €18 million profit in the first nine months of 2004.

Income taxes

Income tax expenses for the first nine months of 2004 were €21 million (compared to an income tax credit of €60 million in the prior-year period). The increase in income tax expenses comprised €57 million in taxes paid or owed and €24 million in deferred taxes. The effective tax rate for the LANXESS Group was 116.6% compared to 35.5% in the prior-year period. The increase can be attributed primarily to the non-deductibility of goodwill impairment charges.

Net income (loss)

For the first nine months of 2004, the LANXESS Group reported a net loss of €8 million, after taking into account €5 million in minority stockholders' interest. The Group reported a net loss of €113 million for the prior-year period, including a €4 million minority stockholders' interest.

Segment Data

Performance Rubber

	Fiscal year 2002 - audited -	Fiscal year 2003 - audited -	Change from prior year	1 January to 30 September 2003 - unaudited -	1 January to 30 September 2004 - unaudited -	Change from prior-year period
	(in € millions)	(in € millions)	(%)	(in € millions)	(in € millions)	(%)
Net sales	1,484	1,375	(7.3)	1,038	1,046	0.8
Operating result	(2)	(246)	*	(51)	42	—
of which exceptional items**	(80)	(191)	*	(15)	(12)	20.0

* Change of more than 100%.

** Exceptional items are not defined under IFRS.

Fiscal year 2003 compared with fiscal year 2002

Net sales in the Performance Rubber segment fell by 7.3% from €1,484 million in 2002 to €1,375 million in 2003. This development can be attributed primarily to a decline in sales of speciality rubber products in the Technical Rubber Products business unit and of synthetic rubbers for the tyre industry in the Butyl Rubber business unit.

Operating result of the Performance Rubber segment declined from a €2 million loss to a €246 million loss. The key contributing factors were impairment charges totalling €133 million and €26 million in asset write-downs relating primarily to software. Other factors that depressed the segment's operating result were litigation costs of €9 million, restructuring expenses of €16 million relating primarily to the production site at Marl and expenses of €7 million relating to the early retirement programme. In fiscal year 2002, operating result was affected by restructuring expenses totalling €37 million related, above all, to the production site in Sarnia (Canada), associated asset write-downs of €42 million and write-downs of software of €1 million. No impairment charges were incurred in that year.

First nine months of 2004 compared with the first nine months of 2003

Sales in the Performance Rubber segment in the first nine months of 2004 were €1,046 million or 0.8% higher than sales in the prior-year period (€1,038 million). Increases in prices and volumes compensated for the adverse exchange rate effects. The Technical Rubber Products business unit increased sales by lifting volume sales of its core products. This development compensated for the volume-related sales decline in the Polybutadiene Rubber business unit.

Operating result of the Performance Rubber segment rose dramatically by €93 million, from a €51 million loss in the first nine months of 2003 to a €42 million profit in the first nine months of 2004. The increase is primarily due to the impairments made at the end of the previous fiscal year and the resulting cost reductions. The establishment of provisions in connection with the investigations conducted by antitrust authorities in the Technical Rubber Products business unit negatively affected operating result by a total of €12 million. In the prior-year period, charges relating to site closures and restructuring, primarily with regard to the Marl production site, were €11 million, and associated write-downs totalled €4 million.

Engineering Plastics

	Fiscal year 2002 - audited -	Fiscal year 2003 - audited -	Change from prior year	1 January to 30 September 2003 - unaudited -	1 January to 30 September 2004 - unaudited -	Change from prior-year period
	(in € millions)	(in € millions)	(%)	(in € millions)	(in € millions)	(%)
Net sales	1,504	1,401	(6.8)	1,060	1,281	20.8
Operating result	(146)	(488)	*	(57)	16	—
of which exceptional items**	(84)	(408)	*	(10)	12	—

* Change of more than 100%.

** Exceptional items are not defined under IFRS.

Fiscal year 2003 compared with fiscal year 2002

Net sales generated by the Engineering Plastics segment declined by 6.8%, from €1,504 million in 2002 to €1,401 million in 2003. This decline can be attributed primarily to lower sales in the Styrenic Resins and Fibers business units, which resulted from a decrease in prices triggered by global overcapacities. The Semi-Crystalline Products business unit reported only slightly lower sales.

Operating result of the Engineering Plastics segment fell from a €146 million loss to a €488 million loss. The main cause for this development were the impairment charges totalling €355 million in the Styrenics and Fibers business units, as well as write-downs of software totalling €16 million. The segment also incurred charges of €12 million relating to the closing of the Goch production site, other restructuring charges of €18 million, which related primarily to the Antwerp site, and expenses of €7 million in connection with the early retirement programme. Of the restructuring expenses, €18 million were incurred by the Fibers business unit. The Fibers business unit faced overcapacity and strong competitive pressure, particularly in Asia. Impairment charges totalling €84 million had already impacted this business unit's operating result in 2002.

First nine months of 2004 compared with first nine months of 2003

In the first nine months of 2004, the Engineering Plastics segment generated sales of €1,281 million, which represents a 20.8% increase over the prior-year period. The increase in sales in the Styrenic Resins business unit and in the Semi-Crystalline Products business unit (which was triggered by both higher prices and volumes sold) more than compensated for the slight decrease in sales in the Fibers business unit caused by global overcapacities and the resulting pressure on prices.

Despite significant increases in the cost of raw materials, operating result in the Engineering Plastics segment rose from a €57 million loss in the first nine months of 2003 by €73 million to a

€16 million profit in the first nine months of 2004. The primary causes of this favourable development, apart from the significant increase in sales, were the €24 million in write-backs of assets in the Styrenic Resins business unit (which were partially offset by additional impairment charges totalling €12 million) and the reduced costs resulting from the impairments and restructuring carried out in fiscal year 2003. During the prior-year period, restructuring charges totalling €10 million — incurred primarily at the Antwerp site — impacted operating result.

As described in the section entitled ''— *Overview — Bases for financial statement reporting*'', allocations below the reporting unit level were not taken into account in preparing the Combined Financial Statements. Based on current knowledge, on an aggregated basis, no materially different statements would result for the LANXESS Group had they been taken into account. Allocations of products diverging from the treatment of those products in the Combined Financial Statements concern the Engineering Plastics segment in particular. Although the most significant individual effect of these diverging allocations would be to substantially reduce operating result of this segment, the aggregate of these divergences does not lead to any materially different statements in respect of operating result because the gross effects largely offset one another.

Chemical Intermediates

	Fiscal year 2002 - audited -	Fiscal year 2003 - audited -	Change from prior year	1 January to 30 September 2003 - unaudited -	1 January to 30 September 2004 - unaudited -	Change from prior-year period
	(in € millions)	(in € millions)	(%)	(in € millions)	(in € millions)	(%)
Net sales	1,447	1,411	(2.5)	1,080	1,102	2.0
Operating result	5	(344)	—	33	46	39.4
of which exceptional items**	(32)	(366)	*	0	(13)	—

* Change of more than 100%.

** Exceptional items are not defined under IFRS.

Fiscal year 2003 compared with fiscal year 2002

The Chemical Intermediates segment generated net sales of €1,411 million in 2003. This represented a decrease of 2.5% or €36 million from the previous year.

Increases in net sales in the Basic Chemicals business unit could not offset declines in the Inorganic Pigments and Fine Chemicals business units. The decline at Inorganic Pigments was primarily attributable to currency effects, while the Fine Chemicals business unit faced stronger competition from Asian suppliers and the continued weakness of the photo chemicals market. As a whole, the segment suffered from economic stagnation in Europe and a weak economy in North America.

The impairment tests resulted in €332 million in impairment charges in the Chemical Intermediates segment, primarily in the Fine Chemicals business unit. In addition, the segment incurred €34 million in expenses related to the Group-wide early retirement programme. After reporting an operating profit of €5 million in 2002, the segment sustained a €344 million loss in 2003, mostly as a result of these impairment charges and expenses. Operating result in 2002 was especially affected by restructuring charges of €23 million in the Inorganic Pigments business unit and asset write-downs of €9 million, primarily in connection with the above-mentioned restructuring. In fiscal year 2002, the Chemical Intermediates segment did not report any impairment charges.

First nine months of 2004 compared with the first nine months of 2003

Sales generated by the Chemical Intermediates segment during the first nine months of 2004 totalled €1,102 million, an increase of 2.0% over sales of €1,080 million in the prior-year period. The Basic Chemicals business unit profited from increasing demand in core product areas. Sales performance of the Inorganic Pigments business unit was affected by weaker demand in the construction industry in Europe and for toner oxides in Japan. The Fine Chemicals business unit reported sales losses in a difficult market environment as a result of a continuing decline in demand in its areas of operations, especially for photo chemicals.

The segment's operating result rose to €46 million in the first nine months of 2004 from €33 million in the prior-year period. The impairments taken at the end of fiscal year 2003 enabled the segment to report lower costs. Operating result was also reduced by impairment charges totalling €18 million (reduced by write-backs of €5 million) in the Fine Chemicals business unit.

Performance Chemicals

	Fiscal year 2002 - audited -	Fiscal year 2003 - audited -	Change from prior year	1 January to 30 September 2003 - unaudited -	1 January to 30 September 2004 - unaudited -	Change from prior-year period
	(in € millions)	(in € millions)	(%)	(in € millions)	(in € millions)	(%)
Net sales	2,055	1,925	(6.3)	1,501	1,459	(2.8)
Operating result	67	(176)	—	51	(8)	—
of which exceptional items**	(42)	(200)	*	(4)	(68)	*

* Change of more than 100%.

** Exceptional items are not defined under IFRS.

Fiscal year 2003 compared with fiscal year 2002

Net sales in the Performance Chemicals segment declined by 6.3% from €2,055 million in 2002 to €1,925 million in 2003. Net sales in the Functional Chemicals and Material Protection Products business units increased. However, these improved sales figures could not offset declining sales in the other business units, in particular Textile Processing Chemicals. The reason for the decline in sales was the unfavourable economic environment in Europe and a North American economy weakened by high oil prices, especially in the first half of 2003.

Operating result fell from a €67 million profit in 2002 to a €176 million loss in 2003, primarily due to impairment charges totalling €168 million. These charges related to the Paper, Rubber Chemicals and Textile Processing Chemicals business units. In addition, this segment incurred write-downs of software of €4 million, expenses of €18 million in connection with the early retirement programme, litigation expenses of €6 million in the Rubber Chemicals business unit and other restructuring charges of €4 million, primarily incurred at the Antwerp site. In 2002, the segment reported restructuring charges of €15 million as well as asset write-downs of €27 million, which related primarily to the Functional Chemicals business unit.

First nine months of 2004 compared with the first nine months of 2003

In the first nine months of 2004, net sales in the Performance Chemicals segment declined by 2.8% from €1,501 million in the first nine months of 2003 to €1,459 million. The decline was attributable primarily to adverse currency effects. Increases in sales in the Ion Exchange Resins, Leather, Material Protection Products and RheinChemie business units could not offset the decline in sales in the other business units.

The segment's operating result dropped from a €51 million profit to a €8 million loss, due to the establishment of environmental provisions of €40 million in the Leather business unit, impairment charges of €20 million in the RheinChemie business unit and the establishment of €8 million in provisions relating to an investigation by antitrust authorities in the Rubber Chemicals business unit. Operating result for the prior-year period was influenced by restructuring charges of €4 million incurred by the Rubber Chemicals business unit at the Antwerp site.

Liquidity and Capital Resources

Financial Condition

Fiscal year 2003 compared with fiscal year 2002

The cash flow statement shows the inflow and outflow of cash from operating, investing and financing activities. Despite the income tax relief resulting from the pre-tax loss, the gross operating cash flow declined by 47.3% or €200 million to €223 million in 2003. This decrease largely mirrored the decline in operating business. Net operating cash flow in 2003 totalled €346 million and was therefore 6.2% or €23 million lower than in 2002. The cash included in working capital improved by €177 million over the previous year.

Cash used in investing activities was €300 million in 2003 and therefore 13.5% or €47 million below the amount for 2002. This development can be attributed primarily to the fact that expenditures for property, plant and equipment were reduced by €81 million from €393 million to €312 million as a result of strict capital discipline. Sales of property, plant and equipment yielded a cash inflow of €65 million (2002: €62 million). Investments, mainly in the form of loan grants to Bayer companies based on the internal Bayer Group financing model still in place at the time, resulted in a cash outflow of €58 million (2002: €21 million).

Cash used in financing activities was €46 million. This amount consists of interest expense (€69 million) less net borrowings (€23 million).

First nine months of 2004 compared with the first nine months of 2003

The gross operating cash flow was €252 million and therefore lower than in the prior-year period (€316 million). It included a €57 million increase in tax payments due to the improved operating result. Given the greater amount of cash included in working capital, net operating cash flow declined by €165 million to €40 million. Cash included in working capital increased as a result of higher sales, higher raw material prices as well as anticipated maintenance-related production stoppages and the related increase in inventories.

Following a cash outflow from investing activities totalling €148 million in the first nine months of 2003, the Group reported a cash inflow from investing activities of €85 million in the first nine months of 2004, primarily as a result of income received from the repayment of a short-term loan granted to the Bayer Group. The expenditures for property, plant and equipment fell by 18.1% to €158 million. This item was partially offset by income received from the sale of property, plant & equipment and other assets totalling €29 million.

Cash outflow from financing activities in the first nine months of 2004 totalled €59 million, consisting of a net loan repayment of €11 million and interest expenses of €48 million. The net loan repayment amount includes the cash inflow from the €200 million convertible bond issued to Bayer AG in September 2004.

The following table shows the cash flow statement for the LANXESS Group for fiscal years 2002 and 2003 as well as for the first nine months of 2003 and 2004:

	Fiscal year 2002 - audited -	Fiscal year 2003 - audited -	Change from prior year	1 January to 30 September 2003 - unaudited -	1 January to 30 September 2004 - unaudited -	Change from prior-year period
	(in € millions)	(in € millions)	(%)	(in € millions)	(in € millions)	(%)
Gross operating cash flow	423	223	(47.3)	316	252	(20.3)
Changes in working capital and other net current assets	(54)	123	—	(111)	(212)	91.0
Net cash provided by (used in) operating activities (net cash flow)	369	346	(6.2)	205	40	(80.5)
Net cash provided by (used in) investing activities	(347)	(300)	(13.5)	(148)	85	—
Net cash provided by (used in) financing activities	(25)	(46)	84.0	(56)	(59)	5.4
Change in cash and cash equivalents from business activities	(3)	0	—	1	66	*
Cash and cash equivalents at the beginning of the period	13	10	(23.1)	10	13	30.0
Change in cash and cash equivalents from changes in the scope of consolidation and exchange rate movements	0	3	—	3	1	(66.6)
Cash and cash equivalents at the end of the period	10	13	30.0	14	80	*
Marketable securities and other instruments	0	0	—	0	0	—
Liquid assets as per balance sheet	10	13	30.0	14	80	*

* Change of more than 100%.

Financing and Liquidity

Presentation in the Combined Financial Statements

In the Bayer Group, liquidity and financial debt are not assigned to business units, but instead are managed centrally at the company or Group level.

Based on the net indebtedness envisaged for the LANXESS Group at the time of the Spin-off and factoring in the expected free cash flow for 2004, a financing structure was computed retroactively for the years 2003 and 2002.

The targeted net indebtedness was presented on the assumption that LANXESS GmbH succeeded in making additional outside borrowings.

Interest expenses for 2002 and 2003 are based on market interest rates for industrial bonds at the lower end of the investment grade range. These interest rates were computed by averaging the rates charged on a short-term instrument and on a five-year instrument. A risk premium was added to account for non-euro denominated financing. For the first nine months of 2004, the interest expense in the first six months was computed in accordance with the approach described above. In the third quarter, the interest expenses recorded by the individual Group companies in their account preparation were included in the interim financial statements.

Financing at the time of the Spin-off

In connection with the combination of major parts of the chemicals and parts of the polymers activities of the Bayer Group in LANXESS GmbH and its direct and indirect subsidiaries (hereafter, ''LANXESS Subgroup'') and to the extent possible and economically practicable, the financial debt was consolidated into LANXESS AG or LANXESS GmbH. On 10 December 2004, LANXESS AG, LANXESS GmbH and LANXESS Corporation (Pittsburgh, PA, U.S.A.) agreed a €1.5 billion credit facility with an international bank syndicate led by the Bank of America, Citigroup Global Markets Ltd., Commerzbank Aktiengesellschaft and Deutsche Bank AG. Planned uses for this credit line include the repayment to Bayer Group companies — after the effective date of the Spin-off — of financial debt owed toward such companies that were assigned to the LANXESS Subgroup when it was set up. The credit facility includes a €0.5 billion tranche structured as a revolving credit line with a term of 364 days, which may be extended one or more times for additional 364-day periods subject to the approval of the banks. The credit facility also includes two revolving tranches totalling €1 billion with terms ending in December 2009.

In addition, an asset-backed commercial paper programme (funded up to €200 million) was created. Financial leases relating to the LANXESS Group that exist at the time of the Spin-off will be transferred, either directly or indirectly to the LANXESS Group companies in the form of sub-leases. In countries with heavily regulated capital markets, such as China, the LANXESS Group will also finance itself through local bank loans.

Another component of the LANXESS Group's financing base will be the convertible bearer bond issued by LANXESS AG to Bayer AG on 15 September 2004 with a face value of €200 million and maturing on 15 September 2007. The bond may be converted between 20 July 2005 and 20 July 2007, with mandatory conversion at the end of the term. The convertible bond contains an interest deferment right and the claims of its holder(s) will be subordinated to the claims of all other creditors of LANXESS AG which are senior and not subordinated.

The LANXESS Group plans to take advantage of the currently favourable market conditions to issue medium-term corporate bonds in 2005 in an aggregate amount customary in the market. This measure would further improve the debt maturity schedule, considering that the syndicated credit line could be partially repaid.

It is anticipated that net indebtedness in the form of financial debt owed to the Bayer Group (including the convertible bond), bank debt and financial leasing, less any liquid funds and excluding pension provisions for the LANXESS Group, will amount to €1.1 billion as of 31 December 2004. In October 2004, Standard & Poor's assigned LANXESS AG a BBB– (investment grade) rating with a stable outlook. Standard & Poor's awards a BBB rating if the relevant obligor has an adequate capacity to meet its financial commitment on its obligations, but adverse economic conditions or changing circumstances are more likely to lead to a weakened capacity of the obligor to meet its financial commitment on its obligations. The minus sign represents the position within this category.

Capital expenditures

LANXESS generally finances its capital expenditures from operating cash flow and, if such funds are insufficient, from other available cash sources and from the sale of short-term investments, including cash equivalents and marketable securities. The Group finances its further capital expenditures with borrowings. Capital expenditures totalled approximately €0.4 billion in 2002 and €0.3 billion in 2003.

In 2003, the focus was on the Engineering Plastics segment. Approximately two thirds of the expenses incurred in 2002 and 2003 involved expenditures to preserve existing facilities, whereas approximately one third related to expansion and rationalisation programmes. The budget for capital expenditures in 2004 totalled approximately €0.3 billion. Approximately 60% of the capital expenditures made in 2004 involved investments to preserve existing facilities, while the remainder was spent on expansion and rationalisation measures. In 2004, from a regional perspective, approximately 73% of the capital expenditures were made in Europe, approximately 15% in North America and the remainder in the other regions in which LANXESS operates.

Major capital expenditures in 2002, 2003 and 2004 included:

Year	Segment	Description
2002	Performance Rubber	Modernisation/rationalisation of the butyl rubber facilities; Zwijndrecht, Belgium and Sarnia, Canada (expenditures in 2002: approx. €12 million).
	Engineering Plastics	Expansion of capacities for ABS plastics; Tarragona, Spain and Map Ta Phut, Thailand (expenditures in 2002: approx. €13 million).
	Chemical Intermediates	Efficiency improvement in the integrated aromatics production network; Leverkusen, Germany (expenditures in 2002: approx. €15 million).
2003	Performance Rubber	Modification of the butyl rubber production facilities; Zwijndrecht, Belgium and Sarnia, Canada (expenditures in 2003: approx. €3 million).
	Engineering Plastics	Expansion of capacities for ABS plastics; Tarragona, Spain and Map Ta Phut, Thailand (expenditures in 2003: approx. €10 million).
	Engineering Plastics	Polybutylene terephthalate (PBT) production facility operated jointly with DuPont in Hamm-Uentrop (share of expenditures in 2002-2003: approx. €25 million).
	Chemical Intermediates	Efficiency improvement in the integrated aromatics production network; Leverkusen, Germany (expenditures in 2003: approx. €10 million).
2004	Chemical Intermediates	Modernisation and expansion of production facilities for precursors of specialty isocyanates; Leverkusen, Germany (approved expenditures for 2004: €14 million).
	Chemical Intermediates	Conversion of facilities for the production of agrochemical intermediates; Leverkusen, Germany (approved expenditures for 2004: €6 million). The project is a response to the growth in the market for the new generation of fungicides from Bayer CropScience.
	Performance Chemicals	Capacity expansion for biocide products; Dormagen, Germany (approved expenditures for 2004: €5 million). This project should serve to expand the business in the significantly growing industry for the cold sterilisation of specialty beverages.

For 2005, the LANXESS Group is likewise budgeting approximately €0.3 billion for capital expenditures. Approximately 60% of the expenditures budgeted for 2005 involve capital expenditures to preserve existing facilities, while the remaining funds are budgeted for expansion and rationalisation programmes. The Company expects that the regional allocation of capital expenditures in 2005 will closely match those of the previous year. The following strategic capital improvement projects are currently underway or planned:

Year	Segment	Description
2005	Performance Rubber	Expansion of capacities for butyl rubber production (by approximately 25% to 250,000 tonnes per year); Sarnia, Canada and Zwijndrecht, Belgium (budgeted expenditure for 2005: €24 million. Additional expenditures of €16 million are anticipated for 2006 for these expansion projects).
	Engineering Plastics	Compounding facility for Durethan® and Pocan®, 1st phase, Wuxi, China: approximately €6 million.
	Chemical Intermediates	Modernisation and expansion of production facilities for precursors of specialty isocyanates; Leverkusen, Germany (approved expenditures for 2005: €16 million).
	Chemical Intermediates	Conversion of facilities for the production of agrochemical intermediates; Leverkusen, Germany (approved expenditures for 2005: €5 million).
	Performance Chemicals	Expansion of capacity for biocide products; Dormagen, Germany (approved expenditures for 2005: €5 million).

It is planned to finance these capital expenditures from current cash flow.

Off-balance sheet arrangements

The non-consolidated LANXESS companies are not deemed special-purpose vehicles and do not constitute other off-balance sheet arrangements.

Seasonality

During the course of any typical fiscal year, the LANXESS business is not subject to any significant seasonality. Nevertheless, certain markets and regions in which LANXESS sells its products may be subject to certain seasonal volatilities. These include the construction industry with its slow winter months, which can affect the Inorganic Pigments business unit, as well as segments that manufacture starting products used in agrochemicals. This could affect the Fine

Chemicals and Basic Chemicals business units. In addition, parts of Southern Europe report slower summer months. Viewed in their entirety, the business units generate relatively constant sales throughout the year. However, the Group tends to generate higher business volumes in the first two quarters of any given fiscal year than in the two remaining fiscal year quarters.

Research and Development Expenses

The following table sets forth the total research and development expenses incurred by the LANXESS Group for the years ending 31 December 2002 and 31 December 2003 as well as for the first nine months of 2003 and 2004.

	Fiscal year 2002 - audited -	Fiscal year 2003 - audited -	Change from prior year	1 January to 30 September 2003 - unaudited -	1 January to 30 September 2004 - unaudited -	Change from prior-year period
			(%)			(%)
Research and development expenses:						
Amount (in € millions)	149	168	12.8	118	95	(19.5)
As a percentage of sales	2.2	2.7	—	2.4	1.9	—

The largest share of research and development expenses of the LANXESS Group was incurred by the Fine Chemicals, Semi-Crystalline Products and Technical Rubber Products business units. In 2003, these business units accounted for 37.5% of the Group's total expenditure on research and development (2002: 27.5%). In the first nine months of 2004, the share equalled 40.0% (prior-year period: 35.6%).

The higher research and development costs in 2003 are related to, among other things, the relocation of central research activities and the allocation of the corresponding resources to the individual business units in the same period. The relevant expenses in the first nine months of 2004 were reduced by 19.5% compared to the prior-year period, which was due to, among other things, the restructuring of the research and development activities begun in 2003.

Management of Market Price Risks at LANXESS

The global nature of the LANXESS Group's business exposes its operations, financial results and cash flow to a range of market price risks. Certain risks to which LANXESS is exposed are described in more detail in the section entitled ''*Risk Factors*''. The following section explains the measures taken by LANXESS that are designed to identify, observe and reduce the disadvantages arising from volatilities in market prices and other market-related indices. Such market price risks include:

- Currency risk: LANXESS is exposed to exchange rate fluctuations between the euro and other major currencies. The most significant currency fluctuation risk is between the euro and the U.S. dollar.
- Interest rate risk: LANXESS is exposed to changes in interest rates. LANXESS' primary interest rate exposure is to fluctuations in short-term and long-term European and U.S. interest rates.
- Credit risk: LANXESS is subject to credit risks with respect to counterparties in its transactions.
- Raw materials and energy price risks: LANXESS is subject to possible increases in raw material prices and energy prices.

In the past, LANXESS placed only limited reliance on hedging transactions to mitigate its exposure to market price risks and only entered into such transactions in the context of its pooling arrangements with the Bayer Group. Where Share Deal companies reported derivative financial instruments, these instruments were transferred. With respect to Asset Deal companies, the relevant financial instruments remained with the Bayer Group. In future, the LANXESS Group's Board of Management will be responsible for replacing the financial instruments that remain with the Bayer Group and for providing for ongoing hedging for all business allocable to the LANXESS Group.

The risks mentioned above could adversely affect the results of operations and the financial condition of the LANXESS Group. The description below focuses on the individual market price risks and on the LANXESS Group's risk management.

Currency Risk

Since the LANXESS Group transacts business in many different currencies, it is exposed to a variety of risks associated with fluctuations in the relative values of these currencies. The currency with regard to which the Group is exposed to the greatest exchange rate risk is the U.S. dollar. In general, any appreciation in the value of the euro relative to other currencies has an adverse effect on the reported sales and results of LANXESS. Depreciation in the value of the euro, by contrast, has a positive effect.

Transaction risk

Currency risks (*i.e.*, the potential depreciation in the value of a financial instrument as a result of changes in the exchange rate) arise especially when receivables or payables are denominated in a currency other than the Company's local currency. Positions denominated in U.S. dollars, Canadian dollars or Japanese yen are especially relevant to LANXESS. The risks arising from the operating activities are systematically recorded and analysed. Decisions about the scope of hedging of such risks are taken regularly. Such hedging may also cover anticipated transactions. A material portion of the contractual and foreseeable currency risks is hedged by using derivative instruments. Changes in the fair value of these instruments are recognised in the income statement or, in the case of cash flow hedges, under ''other changes in stockholders' equity''. Since LANXESS enters into derivative transactions for a significant portion of its currency risks, the Company believes that a significant increase or decrease in the exchange rate of the euro relative to other major currencies would not, in the short term, materially affect its future cash flow. Over time, however, if LANXESS is unable to reflect exchange rate movements in, for example, the pricing of its products in local currency, such exchange rate fluctuations could adversely affect its cash flows.

Currency risks from financial transactions, including interest, are generally hedged at 100%. With respect to operating cash flows, LANXESS seeks to minimise currency risks by constantly adjusting its portfolio of derivative instruments. Cross-currency interest rate swaps and forward exchange contracts are the main hedging instruments used. In order to hedge operating cash flow, LANXESS also enters into option transactions. In order to minimize currency risk, investments in long-term securities and other loans are made primarily in the currency zone of the Group company making the investment.

Translation risk

Many of the companies within the LANXESS Group are located outside the euro zone. Since the euro is the Group's financial reporting currency, the annual financial statements of these subsidiaries were translated into euros for inclusion in the Combined Financial Statements. Period-to-period changes in the average exchange rate for a particular country's currency can significantly affect the translation into euros of both sales and income denominated in that currency. Unlike the transaction risk, the translation risk exposure does not affect the Group's local currency cash flows.

Outside the euro zone, LANXESS holds significant assets, liabilities and operations denominated in local currencies, most notably the U.S. dollar, the Canadian dollar and the Japanese yen. Although the long-term currency risk inherent in these investments is regularly assessed and evaluated, LANXESS generally enters into foreign exchange transactions covering this type of risk only when it is considering withdrawal from a specific venture and repatriation of the funds that the withdrawal would generate. Nevertheless, the Group recognises in equity the effects of currency fluctuations on the translation of net asset amounts into euros.

Interest rate risk

Interest rate risk, *i.e.*, the possibility that the total return of a financial instrument will change due to movements in market interest rates, primarily affects financial assets and liabilities. To the extent the LANXESS Group does not completely abstain from hedging against interest rate fluctuations due to favourable fixed interest rates, it primarily uses derivative financial instruments to hedge interest rate risk, including interest and interest currency swaps. The targeted net indebtedness of the future LANXESS Group is presented in terms of predominantly centralised external borrowings.

Interest expense computed for these purposes is based on the market interest rates for industrial bonds at the lower end of the investment grade range. These interest rates were computed by averaging the rates charged on a short-term instrument and on a five-year instrument. A risk premium was added to account for non-euro denominated financing. Based on this assumption, the Combined Financial Statements do not include any interest-rate derivative instruments.

Other loans primarily consist of loans to employees, most of which have been issued at market-oriented, fixed interest rates. Due to their fixed interest rates, these loans are generally subject to interest rate risk, which, because it is assumed for overriding reasons, is not hedged. More than three quarters of the employee loans have terms of over five years.

Credit risk

Credit risk is the risk that counterparties cannot meet their obligations to the LANXESS Group in transactions involving financial instruments. Since LANXESS does not conclude master netting arrangements with its transaction partners, the total of the amounts recognised in assets represents its maximum exposure to credit risk.

Raw materials and energy price risks

LANXESS operates in markets in which economic cycles often affect raw material and product prices. Fluctuations in prices and availability of raw materials and commodities affect its business units.

Consequently, LANXESS is exposed to market price risks with regards to commodities used in its operating activities. For production at LANXESS, the most important petrochemical raw materials by far include 1, 3-butadiene and styrene. Other important petrochemical raw materials are acrylonitrile, benzene, C4 raffinate 1, cyclohexane, isobutylene and toluene. Other significant raw materials include the basic chemicals ammonia, aniline, chlorine and sodium hydroxide. Prices for petrochemical raw materials are exposed to strong cyclical volatility which arises, among other things, from crude oil prices.

In order to ensure its supply of raw materials, LANXESS has entered into long-term supply contracts, buys additional quantities on the spot markets and concludes swap agreements to manage its supply and demand as needed. By means of pricing formulas incorporated in its contracts, LANXESS can pass on to its customers a not insignificant portion of the price fluctuations caused by such market price risks. The LANXESS Group typically uses the following measures to avoid and manage pricing risks in purchasing raw materials:

- coverage of recurring requirements in part through long-term contracts to reduce the price volatility of purchases on spot markets;
- incorporating pricing formulas (linked to economic indices) instead of fixed prices into its contracts; and
- active inventory management, flexibility in the choice of supply sources and, wherever possible, alternative production plants to limit the risks of non-availability of raw materials.

Petrochemical raw materials have historically been particularly exposed to strong price volatility. Changes in value of approximately one third of these raw material purchases (total purchasing volumes of petrochemical raw materials in 2004: approximately €1.2 billion) are passed on to customers pursuant to contractual arrangements. In 2004, many raw material price increases were passed on to customers even in the absence of such agreements. In connection with the Spin-off, LANXESS is in the process of developing a comprehensive strategy for minimising these risks through financial transactions, including the use of derivative financial instruments.

In view of the increasing volatility of prices in the energy markets and the ensuing consequences for LANXESS' production costs, these factors have been incorporated into the Group's financial risk management. The physical supply contracts for the purchase of gas and steam for the major European sites are based on fuel oil and gasoline indices and, for sites in the United States and Canada, on various U.S. indices for natural gas. The energy price risk to which the LANXESS Group is exposed mainly relates to natural gas in North America and fuel oil in Europe.

The strategy for managing these risks with financial instruments is to achieve a cost average effect within a stipulated risk spectrum by building up strategic hedging positions over time. It is designed to significantly reduce volatility in results and to improve forecasting accuracy for budgeting purposes.

Derivative financial instruments

Only derivative instruments used by existing legal entities that conducted solely LANXESS-related business (Share Deals) were included in the Combined Financial Statements. In this context, fair values totalling €4 million were recognised on the balance sheet in 2003.

The instruments used to hedge the risks mentioned above consist primarily of swaps and options traded on OTC markets with counterparties with high levels of creditworthiness. For accounting purposes, all hedging contracts are treated as instruments held for sale and their fair value changes are recognised in the income statement.

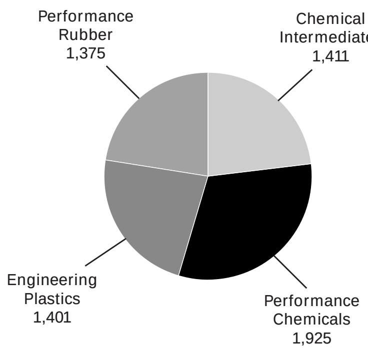
Information Concerning the Business of LANXESS

Overview

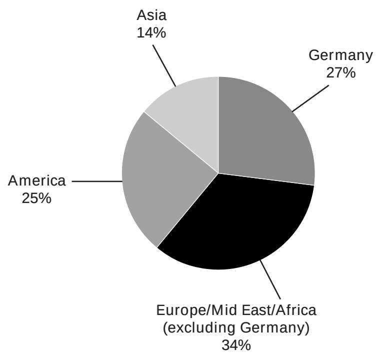
LANXESS is one of Europe's major providers of polymers and chemicals with a comprehensive product portfolio in the fields of polymers and basic, specialty and fine chemicals. With more than 50 operating companies, LANXESS generated sales of approximately €6.3 billion in fiscal year 2003 (sales figures based on the Combined Financial Statements). As of 30 September 2004, the Group employed approximately 19,600 employees worldwide, of which approximately 10,100 were based in Germany. The global business activities of LANXESS are structured into 17 operating business units combined into the four segments Performance Rubber, Engineering Plastics, Chemical Intermediates and Performance Chemicals.

The following two diagrams show the LANXESS Group's net sales in fiscal year 2003, broken down by segment and by the geographical regions in which LANXESS operates.

Net Sales in Fiscal Year 2003 in € millions broken down by segment



Net Sales in Fiscal Year 2003 broken down by geographical region as a percentage of total sales



Competitive Strengths

The Company believes that LANXESS distinguishes itself from the competition through the following competitive strengths:

Strong market position: With sales of €6.3 billion in 2003, LANXESS is expected to be the sixth-largest publicly-listed chemicals company in Europe. The Company estimates that, based on sales revenue or volume, in some two thirds of its business units, LANXESS holds one of the leading positions in the respective markets worldwide.

Global presence: Represented by its foreign affiliates, LANXESS has a presence in all major global chemicals and polymers markets and has production sites in 50 locations in 18 countries, in particular in Germany, Belgium, the United States, Canada and the People's Republic of China, most of which have the necessary critical mass and leading processes and technologies at their disposal. In the Asian market, which is currently experiencing particularly dynamic growth, LANXESS already has ten distribution and application technology centres as well as eight production sites at its disposal. In all, nearly 50% of LANXESS employees are employed internationally and approximately three quarters of LANXESS' sales are generated outside of Germany.

Diversified product portfolio: LANXESS has an extensive product portfolio ranging from solid rubbers, plastics and synthetic fibres to high quality basic and fine chemicals as well as chemicals for the leather, textile and paper industries. LANXESS' customers include well-known manufacturers particularly in the polymer processing and chemicals industry, the fields of electronics and electrical engineering, the automobile and tyre industry, the construction industry, life sciences companies, and the leather, textile and paper industries.

High level of customer orientation: Due to the close cooperation it enjoys with its customers and the comprehensive know-how of its employees in the area of application technology, LANXESS is able to offer its customers tailor-made products and thus meet their particular needs. The Group's research and development activities are also focused on the specific requirements of its business activities and customers.

Performance-oriented corporate structure: The independence resulting from the Spin-off will provide LANXESS with more flexibility and greater transparency, and enable it to strategically restructure its product portfolio. The clear organisational structure consisting of business units that have independent business responsibilities on a worldwide basis, as well as the planned introduction of performance-oriented compensation schemes, will create the foundations LANXESS needs for this purpose.

Business Areas

The range of products offered by LANXESS comprises a comprehensive portfolio in the fields of polymers as well as basic, specialty and fine chemicals.

Performance Rubber

The LANXESS Group's operations in the area of rubber manufacturing are consolidated within the Performance Rubber segment. LANXESS is one of the world's largest manufacturers of butyl rubber and polybutadiene rubber which are used, in particular, in the manufacture of automobile and truck tyres. LANXESS also produces a variety of synthetic rubbers for a broad range of applications, e.g., for use in tyre compounds or plastics modification, as well as a series of specialty elastomers which exhibit a high level of resistance to heat and abrasion and to aggressive environmental influences. The Performance Rubber segment generated sales of €1,375 million in fiscal year 2003. A categorisation of the business units of this segment based on sales in 2003 can be illustrated as follows:

- Sales < €200 million
  - None of the business units of this segment fall into this sales category
- Sales between €200 million and €500 million
  - Butyl Rubber
  - Polybutadiene Rubber
  - Technical Rubber Products
- Sales > €500 million
  - None of the business units of this segment fall into this sales category

Engineering Plastics

With its Engineering Plastics segment, LANXESS is one of the world's major providers of polymers. The Group's range of polymer products includes high-quality PBT (polybutylene terephtalate) and PA (polyamide) plastics, as well as ABS (acrylonitrile-butadiene-styrene), ASA (acrylonitrile-styrene-acrylic esters), SAN (styrene-acrylonitrile) and PA-ABS (polyamide-acrylonitrile-butadiene-styrene) plastics. Potential applications for these plastics are to be found, in particular, in the household goods, automobile, electronics and electrical engineering and medical technology industries. Through its Fibers business, LANXESS offers high-quality brand-name fibres for virtually all branches of the textile industry as well as polyamide-based monofilaments for technical applications. In fiscal year 2003, the segment generated sales of €1,401 million. A categorisation of the business units of this segment based on 2003 sales can be illustrated as follows:

- Sales < €200 million
  - Fibers
- Sales between €200 million and €500 million
  - None of the business units of this segment fall into this sales category

- Sales > €500 million
  - Semi-Crystalline Products
  - Styrenic Resins

Chemical Intermediates

LANXESS' operations in the area of basic and fine chemicals and inorganic pigments are combined within its Chemical Intermediates segment. Intrinsic to the production of high-quality industrial chemicals is a complex network of chlorination, nitration, hydrogenation, phosgenation and isomer separation plants (the aromatics network), which enables the segment to offer a broad range of products at low production costs. In the area of fine chemicals, LANXESS' production is focused primarily on custom manufacturing of, in particular, active ingredients and intermediates for the pharmaceuticals and crop protection industries, starting products for the electrical and electronics industry, as well as photo chemicals. LANXESS is thus able to offer tailor-made products and development services. The inorganic pigments manufactured by LANXESS, particularly iron oxide pigments, are used primarily in the colouring of concrete building components and coatings. In fiscal year 2003, the Chemical Intermediates segment generated sales of €1,411 million. A categorisation of the business units of this segment based on 2003 sales can be illustrated as follows:

- Sales < €200 million
  - None of the business units of this segment fall into this sales category
- Sales between €200 million and €500 million
  - Fine Chemicals
  - Inorganic Pigments
- Sales > €500 million
  - Basic Chemicals

Performance Chemicals

The applications-based business activities of the Group in the area of specialty chemicals are combined within the Performance Chemicals segment. Specialty chemicals are used in a variety of different areas. For example, LANXESS produces and markets biocides and material protection agents for the areas of, for example, wood protection, disinfection and corrosion protection. The Group offers a broad range of plastics additives (e.g., plasticisers, blowing agents), rubber chemicals (e.g., antioxidants), organic and inorganic colouring agents as well as other specialty chemicals (e.g., flame retardants) for the polymers processing and rubber and lubricants industries. In addition, LANXESS' multitude of chemical products makes it one of the major providers of system solutions for the leather industry; it offers textile and textile processing chemicals, in particular in the area of textile pre-treatment and dyeing auxiliaries and also possesses a comprehensive range of products for the paper industry. One special area of business is the production of ion exchange resins, adsorbers and functional polymers for the treatment of aqueous solutions. In fiscal year 2003, the segment reported sales of €1,925 million. A categorisation of the business units of this segment based on 2003 sales can be illustrated as follows:

- Sales < €200 million
  - Ion Exchange Resins
  - Material Protection Products
  - Textile Processing Chemicals

- Sales between €200 million and €500 million
  - Functional Chemicals
  - Leather
  - Paper
  - RheinChemie
  - Rubber Chemicals
- Sales > €500 million
  - None of the business units of this segment fall into this sales category

Corporate Strategy

The Company plans to use its new corporate independence intensively to increase the profitability of the LANXESS Group. The earnings potential of all business activities will thus be reviewed, and concerted cost-reduction, efficiency-enhancement and restructuring measures will be implemented.

The four cornerstones of the Company's strategy are:

- Short-term measures for improving operational productivity
- Systematic restructuring of businesses with inadequate profitability
- Active portfolio management
- Selective organic growth in profitable business activities

For fiscal year 2006, assuming sales at the level of those in fiscal year 2004, the Company aims to achieve an EBITDA margin before exceptional items of 9 to 10%. At the same time, the Company intends to limit capital expenditures by LANXESS to approximately 4% of Group sales *per annum* by 2006, by means of disciplined cash management and systematic allocation of resources.

In the long term, the Company will also consider possible acquisitions and, where appropriate, will strengthen LANXESS by making selective acquisitions. LANXESS intends to bridge the profitability gap between it and comparable competitors with the help of an optimised portfolio. At the present time, there are no plans for any significant growth through acquisitions.

To enable better management of its strategic goals and, in particular, to better manage the optimisation of its portfolio, LANXESS furthermore intends to adapt its organisational and corporate legal structure, including by carving out individual groups into separate independent entities and, where appropriate, modifying LANXESS' national organisations.

The Board of Management will also review whether profitability may be further increased by the carving-out or outsourcing of services, existing distribution structures or other parts of the value chain.

Short-term measures for improving operational productivity

In order to achieve lasting improvements in productivity, the Company plans to continue its efforts to reduce costs, optimise processes, improve the product and customer mix and develop a new price-quantity strategy. These measures are intended to increase the earnings potential of all business units along the entire value chain (e.g., in relation to production, plant maintenance, logistics and other services, marketing, distribution and applications technology).

As regards business units with commoditised product groups (*i.e.*, product groups with products in more mature markets), there are plans to implement cost-oriented performance programmes; those units with a greater application technology orientation will focus on higher benefits to customers.

In order to increase profitability in individual cases, the Company is also prepared to consciously forego sales in certain areas where profit margins are low.

Systematic restructuring of inadequately profitable businesses

The Company continues to plan a systematic restructuring of the business activities of the LANXESS Group in order to achieve a sustained increase in the Group's earning potential over the long term.

Restructuring measures are particularly planned for those businesses and product lines which are unlikely to attain a satisfactory level of profitability through implementation of the planned short-term measures alone.

Restructuring measures to bring about an improvement in operating results of approximately €25 million in fiscal year 2005 were already adopted and implemented in 2004. These restructuring measures specifically include the shutdown of the polybutadiene rubber plant in Marl, the shutdown of the yarn finishing factory in Goch, and the closure of the rubber distribution site in Akron, Ohio, U.S.A. Product lines from the active ingredient production will be discontinued in the first half of fiscal year 2005. These products are manufactured in the plants of the Fine Chemicals business unit. The Company anticipates that the resulting shutdowns will generate total costs of approximately €15 to €20 million.

In addition, the relocation of a facility for the production of hydrazine hydrate from Baytown, Texas, U.S.A. to China has begun. Moreover, a restructuring programme has already been established in the Styrenic Resins business unit for the reorganisation of its activities in Europe and North America.

Other possible restructuring measures are the consolidation, relocation or closure of facilities. Moreover, there are plans for a further cutback of personnel costs, for example, by reducing the number of employees and a review of the schemes for payment of wages, social benefits and working hours. The Company's Board of Management has already adopted resolutions regarding specific personnel-related issues. Initial talks and negotiations with employee representatives in connection with the planned measures have commenced.

Active portfolio management

The Company will carry out an extensive review of its business and product portfolio, taking into account strategic and profitability considerations. The aim is to achieve a marked increase in the Company's average profitability by concentrating on those businesses that demonstrate sustained profitability. Cooperative ventures or divestitures will primarily be sought in those cases where the Company is unable with its own resources to attain, within a given timeframe, the strategic or financial position it desires.

In this context, the above-mentioned restructuring programmes will be developed in the short and medium term with the aim of successfully improving those businesses that are not performing satisfactorily, such as Fibers, Fine Chemicals and Styrenic Resins, or preparing them for partnering. This should also increase flexibility for portfolio adjustments.

The Company will review all measures for portfolio adjustments that present themselves. The Company will act on suitable opportunities that may arise for making divestitures and entering into strategic partnerships, even in the short-run and even in profitable business areas where appropriate.

Selective organic growth in profitable business activities

In the short to medium term, the Company plans to use its own resources to develop its business activities through selective internal growth, the emphasis of which will be on profitable businesses with attractive growth potential. For example, a capital expenditure programme has been developed for the Butyl Rubber business unit to enable the expansion of production capacities by a projected 25% over the coming two to three years. To this end, there are plans to invest approximately €40 million in expanding existing production sites in Belgium and Canada and in redressing shortages.

Moreover, the Company plans to strengthen its presence in Asia, particularly in China, where its initial goal is systematic growth, through measures involving minimal capital expenditures, in particular technology and production joint ventures. An example is the joint venture company that was formed in September 2004 by LANXESS and the Chinese company Weifang Yaxing Chemical Company Ltd. for the production of hydrazine hydrate. The Company plans to continue to closely observe developments in the Asian market and, together with suitable partners, to systematically strengthen the market positions of the LANXESS Group.

Market Environment and Competition

The structure of the international chemicals and polymers markets in which LANXESS sells its products is characterised by a few major companies operating at a global level, each of which does business in a range of different individual markets. These globally operating companies commonly compete with a number of small and medium-sized providers, which primarily do business in their respective local markets. Their customers likewise consist of a number of both smaller and larger companies with very different purchasing volumes. The rubber market has its own particular structure, which is characterised by a small number of customers, mostly from the tyre industry.

As a rule, the worldwide chemicals and polymers markets in which LANXESS operates are characterised by intense competition and significant pressure on margins due to the fact that most of the products are highly commoditised. Assuming a generally high level of product quality, sales prices and the quality of order processing (including delivery logistics), in particular, play an important role with respect to competition. In markets for specialty products, application technology consulting services confer an additional important competitive advantage.

The structures of the chemicals and polymers markets, which had been stable for a long time, have in recent years become more dynamic. A decline in growth can be observed in the United States and Europe. Increasing demand in Asia has prompted new chemicals and polymers suppliers to enter local markets, particularly in those areas that are less technology- or capital-intensive. These new suppliers, particularly those from China and India, are also extending their business beyond their domestic markets into Europe and America. The trend for consolidation in the chemicals industry continues due to the price competition dominating large parts of the market, particularly with respect to commoditised product groups, and the resulting pressure on margins.

Developments in the international chemicals and polymers markets are of a pronounced cyclical nature. Depending on the individual market, longer or shorter periods of higher market growth are interspersed with longer or shorter periods of stagnation or decline in the market. The transition from market growth to market decline can be very swift. To some extent, developments in markets for products vary from region to region. As a rule, developments in the global chemicals and polymers markets track those in the respective customer industries.

The international chemicals and polymers markets are currently experiencing a general upward trend which the Company expects to peak in 2006 (see also World Petrochemical Conference of CMAI, November 2004) or 2007. The LANXESS portfolio includes operations in the basic chemicals and fine and specialty chemicals sectors. The latter two typically exhibit less pronounced economic cycles. The Company believes that the basic chemicals business is currently benefiting to a greater extent from recovery potential as regards price and volume developments.

The sales development of the Engineering Plastics and Chemical Intermediates segments to a large extent tracks the cycles of the global polymers and chemicals markets. The Engineering Plastics segment is also heavily dependent upon developments in the automobile industry and, in particular, in the automotive parts industry. In contrast, the Performance Chemicals segment, with its highly-diversified product portfolio and a high number of niche markets, is less dependent on general economic developments. The business development of the Performance

Rubber segment, for which the tyre industry is the most important customer, is also less cyclical since its products can be used both for tyres as OEM equipment as well as for the spare tyres market sector.

With respect to its customer industries, LANXESS is furthermore dependent on the developments in the chemicals and plastics processing industry, the construction industry, the life sciences industry, the electronics and electrical engineering industry, as well as the leather and paper industries.

A selective, industry-wide definition of the chemicals and polymers markets and their individual markets and segments above the level of individual products is not available due to the large number of different products, their varied fields of application and the divergent market structures. For purposes of this Listing Memorandum, the Company in the following section breaks down its sales markets into segments corresponding to the product offerings of its respective business units. The information provided concerning the respective competitive positions of the business units is also based on such segmentation. Unless stated otherwise, the following description of the market environment and the competitive positions reflect the assessments of the Company (see also ''*General Information — Notice Regarding Sources of Market Information and Technical Terms*'').

In the context of its worldwide business activities, LANXESS competes with a range of major global companies and, depending on the business unit in question, with a number of smaller to medium-sized companies primarily operating at the local level. The Company estimates that in some two thirds of the LANXESS business units, LANXESS holds one of the leading positions in the respective markets worldwide.

Performance Rubber

Butyl Rubber

The global halogen-free and halogenised butyl rubbers business is conducted by a few major companies that focus on a few major global customers. The growth of the market is largely driven by growth in the automobile tyre market, which in turn is determined by the rapidly-increasing number and use of automobiles in Asia, particularly in China. Market growth outside of Asia is expected to be moderate. The number of suppliers is currently increasing as a result of Russian and new Chinese suppliers. In important areas, LANXESS supplies a significant portion of global demand for butyl rubber and halobutyl rubber and, as such, ranks as one of the leading suppliers worldwide (IISRP, Worldwide Rubber Statistics, 2003). The business unit's main competitor is Exxon Mobil Corporation, New Jersey and Irving, Texas (hereinafter referred to as ''Exxon''). Other important competitors are Japan Synthetic Rubber Co., Ltd., Tokyo, Japan (hereinafter referred to as ''JSR''), Sinopec Beijing Yan Hua Petrochemical Co. Ltd., Beijing, People's Republic of China (hereinafter referred to as ''Yan Hua''), and a number of Russian companies.

Polybutadiene Rubber

The Polybutadiene Rubber business unit operates in the field of polybutadiene and solution styrene butadiene rubbers. In-house production by the large tyre producers accounts for approximately two thirds of North America's and approximately one third of Europe's requirements for these types of rubber. In addition, other so-called ''merchant producers'' of polybutadiene also supply the tyre industry. Growth in the global polybutadiene rubbers trade goes hand in hand with economic growth, particularly in Asia (SRI, Chemical Economics Handbook, ''Polybutadiene Elastomers'', May 2003). A growing number of customers are building new production sites there and also at the same time in other low-wage regions such as Latin American and Eastern Europe. The big tyre producers with their own production of polybutadiene are increasingly withdrawing from the merchant market and relying on their own production for supplies to the extent this is technically possible. The Polybutadiene Rubber business unit is one of the world's leading manufacturers of polybutadiene rubbers and, alone among the so-called merchant producers, operates production plants on two continents (North America and Europe). Its main competitors are Firestone Polymers LLC, Akron, Ohio, The

Goodyear Tire & Rubber Company, Akron, Ohio, The Dow Chemical Company, Delaware, and Midland, Michigan (hereinafter referred to as ''Dow Chemical''), Polimeri Europa S.p.A., Milan, Italy, (hereinafter referred to as ''Polimeri Europa''), JSR Corporation, Tokyo, Japan, UBE Industries, Ltd., Tokyo, Japan (hereinafter referred to as ''UBE''), Korea Kumho Petrochemical Co., Ltd., Seoul, South Korea, Nippon Zeon Co., Ltd., Tokyo, Japan (hereinafter referred to as ''Nippon Zeon''), Yan Hua and Michelin, Clermont-Ferrand, France.

Technical Rubber Products

The Technical Rubber Products business unit serves the market sectors for specialty elastomers based on chloroprene rubber (CR), nitrile rubber (NBR), hydrogenated nitrile rubber (HNBR), ethylene-propylene-diene rubber (EPDM), emulsion-styrene-butadiene rubber (E-SBR), and ethylene-vinyl acetate rubber (EVM). While the segments with more mature products report moderate growth, the specialty product segments demonstrate higher growth rates. From a regional perspective, the highest growth rates are observable in Asia. Consistent with the trend among customer industries, relocation by a number of customers of production sites to these regions is underway. The customer base of this business is highly fragmented. The Company anticipates that, in the case of EPDM and NBR, the pressure on prices caused by supply shortages will subside. The Technical Rubbers Products business unit is one of the world's leading companies in the field of specialty elastomers. Its main competitors are Nippon Zeon, Polimeri Europa, DuPont Dow Elastomers, Wilmington, Delaware (a joint venture between E.I. Du Pont de Nemours, Wilmington, Delaware (hereinafter referred to as ''DuPont'') and Dow Chemical, Royal DSM N.V., Heerlen, Netherlands (hereinafter referred to as ''DSM''), JSR and Exxon.

Engineering Plastics

Styrenic Resins

The Styrenic Resins business unit produces and markets the thermoplastic ABS (acrylonitrile-butadiene-styrene), SAN (styrene-acrylonitrile copolymer) and ABS+PA- and ABS+AES-(acrylonitrile-ethylene-propylene-styrene) blends. The ABS segment accounts for most of the worldwide volume; more than half of which is generated in Asia. The Company anticipates that volume growth in the ABS business will be slightly above that of the global economy, essentially due to the positive developments in Asia (particularly in China). Business in Europe and North America is experiencing moderate growth. Overcapacity as well as currency-dependent imports from Asian suppliers are affecting margins, especially as regards standard ABS types. LANXESS has one of the leading positions in the ABS business, particularly in Europe, North and South America and India. The business unit possesses particular technological competence with respect to dyed products and specialties. Its main competitors are Chi Mei Corporation, Tainan County, Taiwan, BASF Aktiengesellschaft, Ludwigshafen, Germany (hereinafter referred to as ''BASF''), LG Chem, Ltd., Seoul, South Korea, Dow Chemical and GE Advanced Materials (a division of General Electric Company, New York, New York and Fairfield, Connecticut.

Semi-Crystalline Products

The Semi-Crystalline Products business unit supplies the demand for polyamide- and polyester-based engineering plastics. It also markets the starting products for these (caprolactam and adipic acid) and glass fibres. The Company anticipates growth in the business to be above that of the general economy due to, in particular, growth in Asia — above all China — and Europe. The business is characterised by a heavily-fragmented customer base. Companies in the various industries of its customers are also increasingly setting up production in Asia. Opportunities for growth for the plastics marketed by the business unit also arise from the substitution of other materials (e.g., hybrid technology by which plastics are processed together with metals). The Semi-Crystalline Products business unit holds a significant position in Europe. In addition, it also operates in niche markets in North and South America and Asia. Its main competitors are BASF, DuPont, Rhodia, Paris, France (hereinafter referred to as ''Rhodia''), UBE and DSM. Together with DuPont, Semi-Crystalline Products has a joint venture for the manufacture of polybutylene terephthalates (PBT) in Hamm-Uentrop.

Fibers

The markets for synthetic elastane fibre (spandex) and polyamide and polyester monofilaments are highly competitive. The elastane fibres segment supplies the greater part of worldwide demand (over 90%, based on sales); the polyamide and polyester monofilaments segments constitute a specialty business. Asian suppliers, in particular, are continually expanding their spandex capacities and individual suppliers are increasingly distributing their products in North and South America and Europe. Growth rates here are significantly above those of the general economy. Asia is by far the largest market and exhibits the highest growth rates. The business unit holds one of the leading positions in Europe and North and South America. In the area of textile fibres, the business unit's main competitors are Invista, Wichita, Kansas, Radici Fil SpA, Casnigo, Italy and Fillattice, Capriate S. Gervasio, Italy, as well as a variety of companies in Asia, such as Hyosung Corporation, Seoul, South Korea, Asahi Kasei Fibers Corporation, Osaka, Japan, Yantai Spandex Stock Co. Ltd., Yantai, the People's Republic of China, Tongkook Corporation, Chung-gu, South Korea, and Taekwang Industries Company Limited, Seoul, South Korea. In the area of monofilament fibres, LANXESS competes with, among others, Teijin Monofilament Limited, Osaka, Japan, Filkemp Industria e Filamentos SA, Mem Martins, Portugal, Hahl Filaments GmbH & Co. KG, Munderkingen, Germany, Monofil-Technik GmbH, Hennef, Germany, Rhodia Technical Fibers, Malmaison, France, Shakespeare Monofilaments and Specialty Polymers, Columbia, South Carolina, SIAT Societa Italiana Applicazione Termoplastici s.r.l., Caronno, Italy and MA.RE. S.p.A., Pilzone d'Iseo, Italy.

Chemical Intermediates

Basic Chemicals

The Basic Chemicals business unit supplies demand for aromatic basic chemicals (chlorobenzenes, nitrotoluenes, chlorotoluenes, cresols and monoisocyanates), benzyl products, polyols, amines and inorganic acids. The basic chemicals business environment is characterised by the limited number of competitors, except in India and the People's Republic of China.

Competition in the area of basic chemicals is increasing as a result of Asian suppliers. At the same time, many customers are relocating their production facilities to Asia. Further consolidation is anticipated in all areas. The Company assumes that existing overcapacities, e.g., in the area of nitrotoluenes, will persist in the next few years. At the same time, the Company anticipates growth in the basic chemicals business to be slightly below that of the general economy. The Basic Chemicals business unit holds one of the leading positions worldwide in most of the product segments.

Due to its broad range of products, the business unit competes with a variety of different companies, depending on the segment in question. The business unit's most important competitors are BASF, Dow Chemical, Jiangsu Yangnong Chemical Group Company Limited, Yangzhou, People's Republic of China, Kureha Chemical Industry Co. Ltd., Tokyo, Japan, Merisol U.S.A. LLC, Houston, Texas, Tessenderlo SA-MV, Brussels, Belgium, Perstorp AB, Perstorp Kristianstad, Sweden, Celanese Ltd., Dallas, Texas, Lonza Group Ltd., Basel, Switzerland (hereinafter referred to as ''Lonza''), and DSM.

Fine Chemicals

The Fine Chemicals business unit offers custom manufacturing services, particularly in the field of agrochemicals as well as in the areas of pharmaceutical chemicals and specialties. Fine chemicals are distributed on the global market without any further regional segmentation. As a result of increased in-sourcing by the big pharmaceutical companies and the establishment by competitors of numerous new facilities, there are currently overcapacities with respect to custom manufacturing for pharmaceuticals. At the same time, Asian suppliers are increasingly establishing themselves as suppliers of starting products. There is significant pressure on prices. Consolidation in the market is continuing as a result of increasing competition. Developments in the fine chemicals business have been very volatile in recent years. A focal point of the Fine Chemicals business unit's operations is in the area of complex chemical syntheses. In the area of custom manufacturing (e.g., as regards agrochemicals), the business unit is one of the leading companies worldwide. Its main competitors are DSM, Lonza, Degussa AG, Dusseldorf, Germany and Rhodia.

Inorganic Pigments

The Inorganic Pigments business unit operates in the synthetic iron oxide pigments and chromium oxide pigments market sectors. Synthetic iron oxides comprise approximately one third of the world's volume of inorganic colour pigments (chromium oxide pigments comprise less than 5%). Natural iron oxides and carbon blacks account for the remaining volume. In keeping with the current trend towards cleanroom applications, LANXESS also distributes granulated and compacted iron oxides. Business is growing at a steady rate slightly below that of the general economy. The Company estimates that approximately 40% of iron oxide pigments are currently being manufactured in China and marketed to some extent at very low prices. The segment is characterised by a number of Chinese manufacturers and dealers who can readily supply the construction industry with lower-quality products. Despite overcapacities at Chinese manufacturers, there were still supply shortages in 2004 due to problems with the supply of raw materials (scrap) and energy. Anticipated consolidation of competitors is intensifying competitive pressure. A sizeable share of the market is in the hands of just a few companies. The Company anticipates that, in future, the demand for iron oxide pigments will be met by European and Chinese companies. Some competitors are beginning to relocate their production capacities to China. The Inorganic Pigments business unit was able to reclaim a share of the market in 2004 and, with its broad product range, is currently one of the leading companies in the fields of iron oxide and chromium oxide pigments.

The business unit's main competitors in the iron oxide pigments segment are Elementis plc, Staines, Great Britain (''Elementis''), Rockwood Specialities Group, Inc., Delaware and Princeton, New Jersey, and a variety of Chinese producers, e.g., Hunan Three-Rings Corp. Ltd., Shaoyang, People's Republic of China, and Deqing Huayuan Pigment Co. Ltd. of Shenghua Group, Zhejiang, People's Republic of China. In the chromium oxide pigments segment, the main competitors are Elementis, Nikon Denka, Japan, and suppliers from Russia, Kazakhstan and the People's Republic of China.

Performance Chemicals

Material Protection Products

The Material Protection Products business unit operates in the area of biocidal active ingredients and formulations as well as material protection products for industrial preservatives, disinfectants and personal care, for wood protection and anti-fouling, as well as in the area of cold sterilisation for specialty beverages. In the area of biocides and material protection products, moderate growth in line with that of the general economy is anticipated. The largest market for biocides and material protection products is in North America, followed by Europe and Asia. The number of suppliers in this area is currently growing as a result of the influx of new Asian producers. The increasing statutory regulation of biocides and material protection products, particularly in Europe, also poses a barrier to entry into the market, which could lead to a strengthening of the position of the major market players. The business unit holds one of the leading positions among the European suppliers. Its sales in the last three years have increased substantially as a result of internal and external growth.

The primary competitors of the business unit are Arch Chemicals, Inc., Norwalk, Connecticut, Dow Chemical, Lonza, Rohm and Haas Company, Philadelphia, Pennsylvania (hereinafter referred to as ''Rohm & Haas''), and Thor GmbH, Speyer, Germany.

Functional Chemicals

The Functional Chemicals business unit operates primarily in niche markets for plastics additives, water and specialty chemicals, colorants and flame retardants. The individual segments exhibit very heterogeneous structures and growth in line with that of the general economy. With respect to water and specialty chemicals, the trend towards consolidation continues. With respect to flame retardants, there is a broader trend away from brominated flame retardants towards more environmentally-friendly halogen-free phosphorus-based flame retardants, which are one of the focal points of the Functional Chemicals business unit. Larger manufacturers are particularly profiting from this trend because of the high technological and structural requirements involved in the development of new flame retardants. The Functional Chemicals business unit holds one of the leading market positions in the sub-markets for auxiliaries for water conditioning and phosphorus-based flame retardants. Its primary competitors are BASF, Crompton Corporation, Delaware and Middlebury, Connecticut (hereinafter referred to as ''Crompton''), Great Lakes Chemical Corporation, Delaware and Indianapolis, Indiana, Ciba Specialty Chemicals Holding Inc., Basel, Switzerland (hereinafter referred to as ''Ciba Specialty Chemicals''), Clariant International Ltd., Muttenz, Switzerland (hereinafter referred to as ''Clariant''), Sun Chemical Group B.V., Weesp, Netherlands, Akzo Nobel N.V., Arnheim, the Netherlands, Ferro Corp., Cleveland, Ohio, FMC Corp., Philadelphia, Pennsylvania, and Lonza.

Leather

LANXESS' Leather business unit operates in the leather chemicals business, particularly in the market sectors for inorganic and synthetic tanning agents, preservatives and fat liquoring agents, dyes and tanning and finishing auxiliaries. The largest markets for leather chemicals are in Asia, particularly in China. The Company anticipates that the automobile industry, in particular, will provide the impetus for positive growth. The Leather business unit has given LANXESS one of the leading positions in the global market for leather chemicals. Its main competitors are BASF, Clariant, TFL Holding GmbH, Weil am Rhein, Germany, and Stahl Holland B.V., Waalwijk, the Netherlands.

Textile Processing Chemicals

The textile and textile processing chemicals business (chemicals for pre-treatment, dyeing, textile printing and finishing) is heavily fragmented. No one supplier holds a prominent position. There are only a few major suppliers operating worldwide and they offer a portfolio of products covering most aspects of textile processing. The development of the textile and textile processing chemicals market sector is to a large extent determined by and the global textile industry. This industry is growing along with the world's population, however, and increased productivity and substantial pressure on prices are reducing total revenues. The textiles business is very regional in nature because product requirements and trends vary greatly from region to region. Markets that have traditionally been important for textiles, such as Western Europe, Japan and the United States, are saturated and are shrinking. The Textile Processing Chemicals business unit, with its focus on textile pre-treatment, dyeing auxiliaries, finishing and textile printing, is one of the few major suppliers operating internationally. Its portfolio comprises products that essentially exhibit growth rates below that of the general economy. Compared with other companies worldwide, the business unit's production complies with strict environmental standards. With respect to ink jet printing of carpets, the Company believes it holds one of the leading positions in the market. The business unit's main competitors are BASF, Clariant, Ciba Specialty Chemicals, CHT R. Beitlich GmbH, Tübingen, Germany and Cognis Deutschland GmbH & Co. KG, Dusseldorf, Germany.

Paper

The Paper business unit operates in the field of chemical additives for the paper industry (particularly fluorescent whitening agents (FWAs), processing and functional chemicals as well as dyes). The Company anticipates growth of the business with additives for the paper industry to be in line with that of the general economy. The business is characterised by significant pressure on prices due, in particular, to heavy competition, also with respect to technical add-on services, as well as the emergence of new suppliers, particularly in Asia. Current overcapacities will contribute to further consolidation of the market. In the FWA and liquid dye fields, the business unit holds major positions. The business unit's main competitors are BASF, Nalco Holdings LLC, Delaware and Naperville, Illinois, Kemira Oyj, Helsinki, Finland, Ciba Specialty Chemicals, Clariant, Hercules Incorporated, Wilmington, Delaware, and EKA Chemicals AB, Bohus, Sweden.

RheinChemie

The business in the area of formulations and specialty chemicals for improving material characteristics is characterised by a customer base made up of mostly small to medium-sized companies from the rubber, plastics, polyurethane and lubricant industries. As regards suppliers in the important polymer-based chemicals segment, only smaller companies operate on a worldwide basis. The technical demands of customers, particularly those in Asia, Central and Eastern Europe and Brazil, are increasing. At the same time, a growing number of customers are reducing their capacities for application technology for cost reasons. In the Company's estimation, this will result in further potential for growth for suppliers who manufacture products primarily according to customer specifications.

As a supplier of formulations and specialty chemicals for improving material characteristics, the RheinChemie business unit is focused on small and medium-sized companies. In certain areas, for example in its role as partner to the lubricant industry, RheinChemie also sees itself as a leading supplier of other customers. RheinChemie is particularly strong in the business for polymer dispersion agents for the rubber industry and hydrolysis protection agents for plastics and polyurethanes. Its main competitors are Lubrizol Corporation, Wickliffe, Ohio, Raschig GmbH, Ludwigshafen, Germany, Schill+Seilacher Aktiengesellschaft, Böblingen, Germany, Air Products and Chemicals, Inc., Delaware and Allentown, Pennsylvania, and MLPC International, Rion de Landes, France (subsidiary of Atofina, Paris, France).

Rubber Chemicals

The supply of rubber chemicals worldwide is concentrated in a small number of suppliers. The largest producers are Flexsys N.V., St-Sevens-Woluwe, Belgium (hereinafter referred to as ''Flexsys''), LANXESS and Crompton.

The rubber chemicals business is heavily dependent on the rubber processing industry. In particular, the pressure on prices exerted by the automobile industry on its suppliers is also noticeable with respect to rubber chemicals. As a result of the recent significant increase in raw material prices, margin pressure has increased even more markedly. The Company anticipates that new opportunities will arise as a result of innovation and new fields of application. The Rubber Chemicals business unit is one of the world's leading companies in the rubber chemicals field.

Ion Exchange Resins

The Ion Exchange Resins business unit operates in the areas of ion exchange resins, adsorbers and functional polymers for the treatment of water and other liquids. As these products largely represent capital assets, the business is characterised by clear development cycles. At the same time, it exhibits a very heterogeneous customer base. It is already possible today to substitute reverse osmosis technology for ion exchange resins in the construction of water treatment plants. The Company assumes that this will not significantly affect the business unit's sales in the short to medium term. The business unit's main competitors are Dow Chemical, Purolite International Limited, Pontyclun, Great Britain, Mitsubishi Chemical Corporation, Tokyo, Japan, as well as Rohm & Haas.

Product Portfolio

The product portfolio of the LANXESS Group primarily comprises established and thus more mature products from the polymers and basic, specialty and fine chemicals fields. However, LANXESS also manufactures and markets less mature products with high innovative potential, such as for high temperature-resistant applications in engine construction (structural components, oil modules and oil pans, etc.).

The significant polymers activities of the LANXESS Group are combined in the Performance Rubber and Engineering Plastics segments. The polymers and polymer additives of the Performance Chemicals segment's Functional Chemicals, RheinChemie, Rubber Chemicals and Ion Exchange Resins business units supplement the Group's overall competence with respect to polymers. In addition, the Performance Chemicals segment's business units produce and distribute, in particular, finishing agents and additives for the leather, textile and paper industries, as well as material protection products. The Chemical Intermediates segment encompasses activities in the fields of basic and fine chemicals, which are used as intermediates in a number of fields of application, and inorganic pigments, which are used to colour, for example, concrete components and coatings.

Performance Rubber

Butyl Rubber

The Butyl Rubber business unit produces high-quality rubber products for the tyre and rubber industries. Butyl rubber is impermeable to air. The Butyl Rubber business unit builds on this characteristic, producing and marketing butyl rubber, bromobutyl rubber and chlorobutyl rubber. Bromobutyl and chlorobutyl rubbers are used in tubeless tyres for cars, trucks and aircraft. Special applications include pharmaceutical packaging and protective apparel. Butyl rubbers are found, for example, in bicycle inner tubes, truck inner tubes and balls. An interesting niche application continues to be the chewing gum market.

Polybutadiene Rubber

The Polybutadiene Rubber business unit supplies the general-purpose rubber grades PBR (polybutadiene rubber) and S-SBR (solution-styrene-butadiene-rubber). The various synthetic rubbers are sold under the brand name Buna™ CB/Buna™ VSL (not registered in the United States) and Taktene®, and are primarily used in tyre components and plastics modification (HIPS/ high impact polystyrene). They are also used in technical rubber goods, electronics and golf balls. In addition to neodymium and cobalt-catalysed grades, the portfolio of products also includes polybutadiene manufactured by lithium catalysis.

Technical Rubber Products

The Technical Rubber Products business unit is one of the major suppliers of specialty elastomers for the worldwide rubber processing industry. The business unit's products are processed primarily into technical rubber goods outside the tyre industry, and are also used as modifiers for plastics and adhesive raw materials. In this regard, abrasion and heat resistance play an especially important role, as does resistance to aggressive environmental influences.

The business unit's key products are polychloroprene solid rubber and Latex (CR / Baypren®), ethylene-propylene-diene-rubber (EPDM / Buna™ (not registered in the United States) EP), nitrile rubber (NBR / Krynac®, Baymod® N, Perbunan®), hydrogenated nitrile rubber (HNBR / Therban®), emulsion-ethylene-vinyl acetate rubber (EVM/Levapren®, Levamelt®, Baymod® L) and styrene-butadiene-rubbers (E-SBR/Krylene®, Krynol™). The business unit's broad range of products is tailored to, among other things, applications in the automobile, construction, electronics and construction engineering industries, as well as industrial plants, oil exploration, aviation, household goods and footwear.

Engineering Plastics

Styrenic Resins

The Styrenic Resins business unit is a supplier of ABS, SAN and ABS+PA plastics operating at the global level. The most important products of this business unit include the ABS brands Novodur®, Lustran® ABS and Absolac™ with applications focusing on the areas of household goods, automobiles, electronics and medical engineering. The SAN-grades Lustran® SAN and Absolan™ are, for example, used in battery casings, lighters and cosmetic packaging. Activities in the area of ABS+PA-blends are consolidated under the name Triax® and are opening up new fields of application particularly in automotive engineering and for the electrical and electronics industries. ASA and AES polymers are marketed in the United States under the brand Centrex®, specifically in the area of weatherproof outdoor applications such as mobile homes and whirlpools.

Semi-Crystalline Products

The high-quality plastics Durethan® (based on polyamide 6 and polyamide 6.6) and Pocan® (basis polybutylene terephthalates) as well as the starting products for these plastics (caprolactam and adipic acid) and glass fibres comprise the Semi-Crystalline Products business unit's future-oriented product portfolio. Durethan® and Pocan® are marketed both in a non-reinforced state and as compounds (in some cases reinforced with glass fibres). The most important applications of these products are in the automobile industry, the electronics and electrical engineering industries and the packaging industry. In hybrid technology, for example, the plastics are processed with metals to produce high-strength components, which maintain their shape even when exposed to heat.

Fibers

The Fibers business unit produces and markets high-quality brand-name fibres for nearly all textile industries, and offers polyamide-based and polyester-based monofilaments for technical applications. The business unit's most important products include the elastane fibre Dorlastan® for the clothing industry, sanitary goods and industrial fabrics, as well as polyamide monofilaments such as Perlon®, Atlas® and Bayco® for use in paper machines, fishing lines and the manufacture of cables and ropes. Technical fibre specialties (monofilaments) are subject to different market trends than are elastane fibres (spandex). For this reason, the Company is currently planning the transfer of the monofilaments business into a separate LANXESS company.

Chemical Intermediates

Basic Chemicals

The Basic Chemicals business unit is a major manufacturer of high-quality industrial chemicals. Noteworthy among its broad range of products are the products of the aromatics network (chlorobenzenes, chlorotoluenes, nitrotoluenes, cresols, toluidines and monoisocyanates). The business unit also produces amines, amino alcohols, benzyl products, hydrofluoric and sulphuric acids, thio products such as thionylchloride and sulfurylchloride, fluoride compounds, oxidation products such as phthalic anhydride and maleicanhydride and polyols such as trimethylolpropane and hexandiol. The basis for the aromatics production is a network of production facilities for chlorination, nitration, hydrogenation, phosgenation and isomer separation which enables the business unit to offer a broad range of products.

Fine Chemicals

The Fine Chemicals business unit offers syntheses for fine chemicals in the area of custom manufacturing. The business unit produces and markets numerous starting products and intermediates for crop protection agents and active ingredients for pharmaceuticals as well as other high-quality fine chemicals (e.g., vitamin precursors, starting products for cosmetics and the electronics industry, and photo chemicals).

Inorganic Pigments

The Inorganic Pigments business unit is a global manufacturer of iron oxide pigments and chromium oxide pigments, and has a broad range of products. The preferred areas of application include the colouring of construction materials (e.g., of concrete and roof tiles), surface coatings, plastics and numerous specialty applications. The business unit's most important products include the iron oxide pigments Bayferrox®, Bayoxide®, Bayscape®, Colortherm® and chromium oxide pigments (e.g. Chromoxid GN).

Performance Chemicals

Material Protection Products

The Material Protection Products business unit offers a broad range of biocidal active ingredients and material protection agents for applications in the areas of industrial preservatives, disinfection, personal care, wood protection and anti-fouling, as well as in the area of cold sterilisation of specialty beverages.

The most important product line is the Preventol® range. The bactericides, fungicides, insecticides and corrosion inhibitors produced by the business unit are used in wood preservation, as industrial, hospital and household disinfectants and in animal hygiene. Other brand name products are Solbrol™ (preservatives for cosmetics), Velcorin® (cold sterilisation for beverages containing fruit juice) as well as Tektamer®, Metasol® and Biochek®.

Functional Chemicals

The Functional Chemicals business unit has an extensive range of plastics additives (including plasticisers, blowing agents and emulsifiers), phosphorus and specialty chemicals (flame retardants, water chemicals, synthesis chemicals), and organic and inorganic colorants, *i.e.*, dyestuffs and pigments (for colouring plastics and surface coatings in ink jet printing, but also for specialty pigmentation, e.g., of crop protection agents). Other important fields of application for the products are in the areas of polymers processing, office communication equipment, optical data storage and water treatment, and flame retardants for plastics and polyurethanes or as synthesis chemicals.

Among the business unit's most important products are Baypure®(water conditioning, washing powder and surface cleansers), hydrazine hydrate (for the synthesis of pharmaceutical preparations and crop protection agents) and Levoxin™ (used for corrosion control in closed steam generation and heating systems), Disflamoll®, Bayfomox®, Levagard™ (flame retardants), phosphorus chloride (preliminary stage, e.g., for organicphosphoric esters/flame retardants), Macrolex®, Bayplast® (organic pigments for plastics), Mesamoll®, Adimoll®, Ultramoll®, Unimoll®, Triacetin (specialty plasticisers for polymers processing), Bayhibit® (stone and corrosion inhibitor for the treatment of water and for industrial cleansers) as well as Levanyl™ and Solfort™ (dyes).

Leather

The Leather business unit is one of the major providers of system solutions for the leather industry. It develops, produces and markets a number of products for leather manufacturing, including inorganic and synthetic tanning agents, preservatives and fat liquoring agents, dyes and tanning and finishing auxiliaries for the shoe, furniture, automobile and clothing industries and also provides on-site application technology support.

The business unit's products include tanning auxiliaries (Baymol®, Cismollan™, Preventol, Baykanol® and Xeroderm®), mineral tanning and re-tanning agents (Baychrom®, Blancorol™, Chromosal®), synthetic/organic tanning and re-tanning agents (Baykanol®, Levotan®, Tanigan®, Retingan®), dyes (Aciderm®, Baygenal®, Levaderm®, Euderm®, Bayderm®, Baycolor™, Eukanol™), PU dispersions (Bayderm®, Aquaderm™, Hydrholac™), finishing auxiliaries (Baysin™, Euderm®, Eusin®, Persiderm™), solvent-based top coats (Isoderm®) and special processes (Baygen™, Levacast™).

Collaborations with Rohm & Haas with its brands Leukotan®, Primal®, Lubritan™ and Acrysol™ (e.g., as polyacrylics for the wet end as well as finishing) and Seta S/A, Taquari, Brazil with its brand Seta™ as a vegetable tanning agent serve to extend the range of products offered by the business unit.

Textile Processing Chemicals

The Textile Processing Chemicals business unit is an important supplier in the field of textiles and textile processing chemicals. The business unit's primary focus is on the area of textile pre-treatment, dyeing auxiliaries, finishing and textile printing. In addition to standard products, the business unit offers, particularly in Europe and North America, a number of specialty products for sophisticated applications, such as flame-retardant textiles or in carpet printing. The business unit offers brand-name products that include Diadavin®, Tanaterge®, Baylase®, Baysolex®, Erkantol®, Levapon®, Plexene™ and Tannex® in the area of pre-treatment, and Astragal®, Avolan®, Levegal®, Levogen®, Lubit®, Tanasperse™, Tanapal®, Tanadel™ and Tanede™ in the area of dyeing auxiliaries. Brand-name products used in finishing and textile printing are, among others, Baygard®, Baypret®, Persoftal®, Eulan™, Synthappret®, Acraconz™/Acraconc™, Acramin®, Acrafix®, Tanaprint®, Nofome™ and Cellolube™.

Paper

The Paper business unit develops, produces and markets a comprehensive range of products for the paper industry. Products include primarily liquid dyes for colouring paper, cardboard (packaging material) and specialty papers (Levacell®/Pontamine®, Astra™/Verona™ Basic), organic pigments (Halopont™, Ponolith®), a broad range of fluorescent whitening agents (Blankophor®), process chemicals such as retention aids, fixation agents (Retaminol®, Levogen®), functional chemicals such as sizes and wet strength agents (Baysize®, Baystrength™, Nadavin™, Parez®) and products for the manufacture of micro capsules for carbonless copying paper (Baymicron®).

RheinChemie

The RheinChemie business unit is a cross-industry manufacturer of custom-made formulations and specialty chemicals for the rubber, lubricant, polyurethane and plastics industries, as well as pigment pastes and coatings.

Important products of the business unit include additives for the rubber industry (Rhenogran®, Rhenoslab®, Aktiplast®, Aflux®, Rhenosin®, Rhenopren®, Urepan™, Rhenoblend®, Rhenodiv®, Rhenofit®, Rhenocure®, Antilux®), additives for the lubricant industry (Additin™), additives for the polyurethane and plastics industry (RC-PUR®, Stabaxol®) as well as colour pastes, coatings and pigment preparations (Isopur™/Bayflex™, Isothan™, Moltopren™).

Rubber Chemicals

The Rubber Chemicals business unit is a global manufacturer and supplier of rubber chemicals. Rubber chemicals enable and facilitate the mixing and processing of elastomers, blends or their rubber compounds, and help to achieve certain characteristics of the elastomers or finished rubber or latex products, e.g., through vulcanisation, and protect an end product against undesirable alteration of its physical properties or degradation, e.g., oxidation, under its conditions of use.

The business unit's most important products include antioxidants (Vulkanox®, Vulkazon®), accelerators (Vulkacit®, NaMBT) and specialty chemicals (Vulkalent®, Zinkoxyd Aktiv™, Cohedur®, Vulcuren®, Emulvin®W, Vulkasil®, Renacit®, Vulkanol™, Coagulant WS, Colloidal Sulphur acid 95, Zinc Oxide Transparent). The products are used particularly in the tyre industry and by manufacturers of technical rubber goods.

Ion Exchange Resins

The Ion Exchange Resins business unit is one of the world's major providers of ion exchange resins, adsorbers and functional polymers which are used, in particular, for the treatment of water and purification of glucose and starch solutions, as chemical catalysts and for the treatment of chemical process streams. The products are sold worldwide under the brand names Lewatit® and Ionac®.

Raw Materials, Suppliers and Service Partners

By far the most important petrochemical materials for the LANXESS Group's production activities are 1, 3-butadiene and styrene. Other important petrochemical raw materials include acrylonitrile, benzene, C4-raffinate 1, isobutylene and toluene. In addition, the basic chemicals ammonia, aniline, chlorine and sodium hydroxide are of major importance. The raw materials are obtained from a large number of different companies, to some extent in the context of long-term agreements. Chlorine and sodium hydroxide are supplied by Bayer Group companies to the sites in the Lower Rhine region (Leverkusen, Dormagen and Uerdingen) (see also ''*Business Transactions and Legal Relationships with Related Parties — Business Transactions and Legal Relationships with the Bayer Group*''). For fiscal year 2004, the company estimates that the ten most important raw materials accounted for a total purchasing volume of approximately €1.2 billion. This represents approximately 50% of the LANXESS Group's total raw material expenses.

The prices of petrochemical raw materials are exposed to strong cyclical volatility that is dependent on, among other things, crude oil prices. This also applies to the prices of inorganic chemicals which, in the case of chlorine and sodium hydroxide, are dependent on, among other things, electricity prices and, for example in the case of ammonia and formaldehyde, on natural gas prices (see also ''*Risk Factors — Risks relating to the Business of LANXESS*'').

LANXESS procures its most important raw materials through its own centrally-managed global procurement organisation in close coordination with the business units.

In 2004, the principal suppliers of petrochemical raw materials were BP p.l.c., London, Great Britain, Shell (a joint venture between Royal Dutch Petroleum Company, The Hague, Netherlands, and The Shell Transport and Trading Company p.l.c., London, Great Britain), BASF, Chevron Phillips Chemical Company LLC, The Woodlands, Texas, Huntsman LLC, Salt Lake City, Utah, Repsol YPF, Madrid, Spain, Exxon, Dow Chemical, Nova Chemicals Corporation, Calgary (Alberta), Canada, and the Bayer Group. At the same time, LANXESS obtains base chemicals from BASF and the Bayer Group. The Company estimates that approximately 14% of the LANXESS Group's raw materials requirements in 2004 were met through the Bayer Group.

In Germany, LANXESS obtains services to a large extent from the service companies of the Bayer Group, namely Bayer Business Services GmbH (''BBS''), Bayer Technology Services GmbH (''BTS'') and Bayer Industry Services GmbH & Co. OHG (''BIS''), in which LANXESS GmbH holds a 40% interest, and their subsidiaries. BIS' infrastructure services, such as energy, waste disposal and logistics services, are largely provided locally in the chemical park sites, while the services of BBS (economic management, administrative and IT services) and BTS (engineering and process technology) are also provided outside Germany. LANXESS is contractually obliged to obtain a range of services from BIS, BBS and BTS. Apart from these obligations, LANXESS is generally free to obtain services from other companies. Moreover, foreign companies of the LANXESS Group also utilise the services of the local Bayer companies, in particular, plant services and IT services.

In addition to the services of the Bayer service companies, LANXESS also obtains services from other Bayer companies. These services include, for example, infrastructure services of the Bayer MaterialScience subgroup at the co-production plants in Antwerp, Belgium, Tarragona, Spain and Map Ta Phut, Thailand. Furthermore, LANXESS utilises to a lesser extent the services of other service partners, for example, the PC support provided by Borsu Computer GmbH, Dusseldorf, Germany, and by Siemens Aktiengesellschaft, Berlin and Munich, Germany, at the Leverkusen site, and the procurement of energy services from TransAlta Corporation, Calgary, Alberta, Canada at the Sarnia site in Ontario, Canada, and Sabine Corporation, Dallas, Texas at the Orange, Texas site in the United States.

Production and Logistics

LANXESS is one of the major manufacturers of chemical and polymer products in Europe. At its production plants, it can manufacture both the smallest quantities of products on the basis of tailored customer syntheses as well as several thousand tonnes of basic, specialty and fine chemicals and polymers.

In organisational terms, the Group's production operations are allocated to individual business units. The most important production sites are located in Leverkusen, Dormagen and Uerdingen in Germany, Antwerp in Belgium, Bushy Park and Addyston in the United States, Sarnia in Canada, and Wuxi in China. LANXESS also has additional production sites in Argentina, Australia, Belgium, Brazil, Canada, China, France, Germany, Great Britain, India, Italy, Japan, Mexico, the Netherlands, South Africa, Spain, Thailand and the United States.

The production sites in Leverkusen, Dormagen, Uerdingen, Brunsbüttel, Bitterfeld, Marl and Bushy Park are operated as so-called ''chemical park'' sites. The site-related services for the LANXESS operations in those locations are provided by the respective chemical park site operators (Leverkusen, Dormagen, Uerdingen and Brunsbüttel: Bayer Industry Services GmbH & Co. OHG; Bitterfeld: a company of the Bayer Group; Marl: Infracor GmbH; Bushy Park: a company of the LANXESS Group).

The Leverkusen site includes production operations for the Performance Chemicals, Chemical Intermediates and Performance Rubber segments. As part of a network of various production operations of the Basic Chemicals business unit at the Leverkusen site (the so-called ''aromatics network''), a broad range of aromatic intermediates is manufactured from aromatic starting products, in particular through chlorination, nitration, hydrogenation and isomer separation (crystallisation and distillation). These include, in particular, chlorobenzenes, chlorotoluenes, cresols, nitrotoluenes and amines.

The Uerdingen site includes, amongst other things, a production network of the Inorganic Pigments business unit for the manufacture of pigments based of iron oxide and chromium oxide bases which are used principally in the construction industry for colouring building materials. Moreover, inorganic pigments for dyeing surface coatings, for colouring plastics and for toner colour pastes, as well as polyols, oxidation products and benzyle products are manufactured for the Basic Chemicals business unit. The high quality plastics Durethan® and Pocan® are produced for the Semi-Crystalline Products business unit.

Dormagen includes, among other operations, a production network of the Styrenic Resins business unit where the ABS plastics Lustran® and Novodur® are manufactured.

The production site in Antwerp, Belgium, is located in the middle of the Antwerp Harbour chemical complex and is characterised by its excellent infrastructure. Several operations of the Semi-Crystalline Products business unit which form a production network are located here. Starting with organic and inorganic raw materials, the intermediates caprolactam and glass fibres are produced for the manufacture of semi-crystalline thermoplastics such as Durethan® and Pocan®. Moreover, production facilities of the Rubber Chemicals business unit for the manufacture of additives for the rubber industry and the Butyl Rubber business unit are located at the Antwerp site.

Production facilities for the Engineering Plastics and Performance Chemical segments are located at the Bushy Park site in Charleston, South Carolina. Operations for the manufacture of plastic fibres such as Dorlastan® and chemicals for the rubber and paper industry are located here.

Production facilities for the Engineering Plastics segment are located at the Addyston, Ohio site. The ABS plastics manufactured there are also used in the automobile industry.

The Wuxi production site is located in an industrial population centre in the south east of the People's Republic of China and, in addition to the production sites in Quingdao and Shanghai (also in the People's Republic of China), is of strategic importance to LANXESS. Following the development of the site in 1995, production capacity was gradually expanded. Currently, leather chemicals of the Leather business unit are manufactured at the site. In addition, textile processing chemicals of the Textile Processing Chemicals business unit are manufactured in Wuxi for various types of processes in the textile industry, such as pre-treatment, dyeing auxiliaries and textile printing.

The production site in Sarnia, Ontario, Canada, is assigned to the Performance Rubber segment. Rubber products for the tyre and rubber industry are manufactured in the production operations of the Butyl Rubber and Technical Rubber Products business units.

The majority of LANXESS' operations use hazardous substances during production, involve work with such substances or manufacture them. The safety of procedures and facilities, and hence the safety of humans and the environment, constitutes an important objective for LANXESS. LANXESS uses various methods and programmes to ensure safe operation of facilities.

LANXESS approaches both its safety inspections of industrial sites and ensuring of the safe operation of new facilities in a systematic manner. The approach is set forth in guidelines. The status of safety inspections is recorded and updated. Moreover, regular training sessions are conducted.

In all of its plants, LANXESS has taken technical and organisational precautions to minimise the effects of possible incidents causing damage. The relevant precautions are specified in emergency response plans which are constantly updated.

LANXESS focusses its manufacturing processes around safety, quality, profitability and environmental protection. Therefore, LANXESS has set up an integrated management system for most sites which meets the requirements of ISO 9001:2000 and ISO 14001. Central quality management is responsible for setting up and maintaining the management system, the performance status of which is reviewed by means of regular internal and external audits.

In order to ensure product quality, the respective plants inspect the materials and additives prior to their use to check their identity and/or specification requirements. In order to achieve a high level of process safety and keep reject levels to a minimum, the plants maintain their production facilities in accordance with stipulated maintenance and servicing plan, and regularly train their employees. The production plants identify quality-relevant process parameters and monitor them during production.

For the products manufactured by LANXESS and destined for sale, internal specifications or written specifications prescribed by customers generally exist. Such specifications stipulate the respective quality features and, where applicable, application features.

The customers of the LANXESS Group place their orders through 36 domestic and foreign LANXESS companies, through 37 distribution agencies of the Bayer Group, as well as through several hundred independent distribution partners (independent distributors and sales agents). A number of customers also avail themselves of the opportunity to place orders via an Internet portal for chemical products (''ELEMICA'') — a so-called ''B2B'' solution — or a LANXESS-specific Internet tool (''LanxessONE'').

Newly-produced goods are either converted during production or retained in tanks for filling into road and rail tankers, railway boiler cars or ships. The Company's own storage facilities as well as external storage facilities are used for intermediate storage. Goods are delivered to customers from distribution warehouses, customers' consignment warehouses or centrally from factory warehouses. Due to the wide range of products manufactured in Europe, European customers are supplied principally from the European LANXESS sites. As a rule, customers in other regions — to the extent possible — are also supplied from regional production sites. The SAP R/3 computer system is used to support logistical handling of orders for customers to be supplied from the European and most of the U.S. sites, while orders in other regions are processed using local standard systems.

Export and import activities necessary for international goods transactions are handled by regionally-centralised organisational units (so-called ''Order Process Centers''). This applies both to the direct supply of customers — including the associated credit operations — and to the supply of the LANXESS Group's storage facilities. The Order Process Centers also assume responsibility for procuring transport services provided by shipping companies operating both regionally and globally. Deliveries to consignment warehouses are coordinated exclusively by the Order Process Center in Europe. Other goods-related services, such as the filling or storage of products, are managed centrally by LANXESS GmbH in the German Lower Rhine plants.

The regional Order Process Centers of the LANXESS Group are located in Cologne, Germany and Pittsburgh, U.S.A. In addition, Order Process Centers are currently being set up in Sao Paulo, Brazil, Mexico City, Mexico, Hong Kong, Singapore, and Tokyo, Japan. The duties of these units will also include inventory management for local storage facilities and supply processing for local business.

LANXESS also centrally monitors from Germany the Group's worldwide receivables arising from goods and services supplied to customers (receivables management). Nevertheless, customer-related activities relating to the determination of payment terms, notice procedures and determination of customer credit limits are carried out by the local LANXESS companies or business units.

Customers, Marketing and Distribution

LANXESS distributes its products globally to several thousand customers in more than 140 countries. As a rule, these customers include the leading companies in their respective industries. The LANXESS Group's customer base is spread broadly: In 2003, the Company generated less than 20% of its sales through its ten most important customers. In 2003, sales generated by companies belonging to the Bayer Group constituted less than 10% of total sales. Customers of the LANXESS Group operate especially in the chemicals and polymers, automobiles and transport, tyres, construction, electrical engineering and electronics, and life sciences industries. In addition, LANXESS companies supply enterprises in the leather, paper and textile industries and are active in niche markets such as the market for halogen-free flame retardants and cold sterilisation for beverages. The business units of the LANXESS Group and a large proportion of its customers — particularly in Europe and North and South America — can look back on many years of joint business relations which form the basis for today's solid customer loyalty.

The LANXESS Group's activities in marketing and distribution are generally managed independently by the respective business units using their own sales organisations. This facilitates a high level of customer proximity and individual marketing strategies, which are reviewed using customer satisfaction surveys and customer wish enquiries, among others. Depending on customer needs and purchaser structures, customers are serviced globally on a centralised basis by Key Account Managers (e.g., Technical Rubber Products) or (especially in case of a large number of local customers) by regionally independent business units (e.g., Styrenic Resins). In countries where certain business units generate only minor sales revenue, local distribution organisations are generally not created for these business units and several business units are jointly represented by joint sales representatives or external dealers. In market sectors in which LANXESS provides additional services in the form of technical application support (e.g., in the Textile and Leather segments), application technicians provide on-site support to local distribution employees from regional or global technical centres. In specific areas, a worldwide network of technical service laboratories is available for the support of application technicians (e.g., Material Protection Products). At present, LANXESS is not participating in any major electronic auction procedures for customer orders. The possibility, however, that LANXESS will take part in such procedures in future cannot be excluded.

In countries in which LANXESS is not represented through a foreign affiliate, LANXESS also relies on the sales organisation of the Bayer Group. In this respect, local distribution is primarily handled by Bayer Group companies on the basis of agency agreements offering the option of independent distributorship. This distribution structure is currently used primarily in the countries or regions of Northern Europe (Sweden, Finland, Denmark, Norway and the Baltic States), Central and Eastern Europe (Poland, the Czech Republic, Slovakia and Hungary), Russia and the other CIS states, as well as Korea and Taiwan in Asia. The establishment of LANXESS' own distribution structures in certain regions is currently under review. The Company expects that the corresponding sales will be approximately €0.7 billion in 2005 (see also ''*Business Transactions and Legal Relationships with Related Parties — Business Transactions and Legal Relationships with the Bayer Group*'').

In addition, LANXESS distributes its products via several hundred independent distribution partners (independent distributors and sales agents) worldwide which are integrated into the networks of the business units. In particular those customers only purchasing small quantities of products are serviced in cooperation with local or regional distribution partners.

Product-related marketing activities by the LANXESS Group are generally independently managed by the business units. In this respect, central offices cooperate with the respective business units in selecting new product names in order to achieve Group-wide agreement. In future, LANXESS plans to provide particularly important products using word-picture marks. A link to the name ''LANXESS'' is to be established by means of an ''X'' supersign with a red bar. LANXESS is currently conducting a centrally-planned global campaign to establish the name ''LANXESS''. LANXESS' marketing activities also include participation in the key global industry trade fairs and application-specific regional trade fairs.

Capital Expenditures

LANXESS bases the scope of its capital expenditures on its current cash budget. The funds are allocated to the business units in accordance with strategic requirements. In this respect, the Company takes into account both the need for so-called ''basic capital expenditures'' and for so-called ''growth investments''. The basic capital expenditures serve to maintain business operations and comprise the following types of expenditures:

- Expenditures for replacement and maintenance work in order to ensure continued availability of the facilities;
- Expenditures to ensure safety at the production facilities;
- Expenditures to improve quality and efficiency; and
- Expenditures to comply with environmental protection provisions.

In the case of growth investments, the Company takes into account both the return and enhanced value generated by the investments, as well as the establishment and further development of its business activities.

Details about the most important capital expenditures made in the last two fiscal years and about the current and budgeted LANXESS capital expenditures are provided in the section entitled ''*Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources — Capital expenditures*''.

Research and Development

The research and development activities of the LANXESS Group are aimed at further developing the existing product range, developing new areas of application for products and improving product quality by optimising production procedures and reducing production costs.

In organisational terms, the research and development units of the LANXESS Group are allocated to the individual business units. This is intended to ensure that development activities are strictly oriented around the business units' requirements and those of their markets and customers. Thus, for example, business units involving a high proportion of commodities (products with a high level of market maturity), such as Basic Chemicals, concentrate on constantly improving their production facilities and processes (process optimisation). Other business units, such as Material Protection Products, Semi-Crystalline Products and Leather, focus their research and development activities increasingly on optimising their products and their products' quality, as well as developing new products oriented around market requirements and the special needs of customers. Through strict orientation around the requirements of the respective business units, relinquishment of basic research, critical project selection and systematic use of existing development synergies (e.g., by using application technologies that have already been developed for substances with similar structures), LANXESS plans to structure its research and development efficiently and to minimise R & D expenses as a whole.

Globally, LANXESS has research and development units at various locations, with principal sites in Leverkusen, Dormagen, Krefeld-Uerdingen (all Germany) and Sarnia (Canada). Other R & D centres are located in Madurai (India), Woodbridge (U.S.A.) and Ede (the Netherlands).

As at 30 September 2004, LANXESS employed approximately 800 employees in its worldwide research and development units. In fiscal years 2003 and 2002, based on the Combined Financial

Statements, the Group spent approximately €168 million (approximately 2.7% of sales) and €149 million (approximately 2.2% of sales), respectively, on research and development.

In the Performance Rubber segment, the bulk of the research and development activities are performed by the Technical Rubber Products business unit. The research and development activities of this business unit focus on optimising existing products and processes and on the ecological structuring of production processes. In addition, new products and product lines are developed and supported until they are ready for market launch. In this respect, LANXESS cooperates with institutes at various universities. The most recent result of Technical Rubber Products' development activities was the new Therban® AT product line, introduced at the ''K 2004'' trade fair in October 2004.

The research and development activities of the Engineering Plastics segment focus on the discovery and development of new areas of application for existing products. This applies, in particular, to the thermoplastics Durethan® and Pocan®, and the plastic-metal hybrid technology developed for them. In addition, the research and development units support ongoing business, especially with respect to compound products — for example, by improving the ability to process the products — and work on projects for quality and efficiency optimisation.

In the Chemical Intermediates segment, the R & D activities concentrate largely on the Custom Manufacturing division of the Fine Chemicals business unit. Here, individual manufacturing processes for customer-specific intermediate products are developed as a service, and the relevant products are manufactured. Custom Manufacturing is intended to enable the customer to concentrate on its own core competencies and to reduce development times. In contrast to all other R & D activities conducted by the LANXESS Group, in this case development services thus constitute an integral part of the service provided. The principal customers are pharmaceutical companies, manufacturers of crop protection products and companies that market chemical specialties such as electronic chemicals, aromas and flavourings. Development activities in Customer Manufacturing are currently undertaken in Leverkusen by approximately 190 employees. In addition, new technologies are licensed from external partners, such as the Massachusetts Institute of Technology, U.S.A., or the Max-Planck Institute for Coal Research (Max-Planck Institut für Kohlenforschung), Mülheim, or developed with outside partners, including the Max-Planck Institute for Coal Research, Ludwig-Maximilian University, Munich, and the Swiss College of Technology (Eidgenössische Technische Hochschule), Zurich.

In the Performance Chemicals segment, the focus is on application-related product optimisation. In many markets — such as the textiles and leather markets — product life cycles are short and products are subject to rapid changes, some of which are caused by developments in the fashion industry. In order to be able to react quickly to such market changes, a need for constant and flexible development work exists. For this reason, the development units of the Performance Chemicals segment operate very close to the market, in some cases as part of joint projects with customers.

Patents, Licences and Trademarks

The internationally-oriented industrial property rights strategy of LANXESS is aimed at effective patent protection for its own inventions and effective trademark protection for its own product names. LANXESS places high priority on protecting its own innovations through industrial property rights. In this context, the Company believes that the loss of individual rights or licences will not have a material adverse affect on LANXESS business activities. Monitoring of industrial property rights is centrally managed from Germany, except with regard to industrial property rights registered in the names of United States or Canadian affiliates. These industrial property rights, which are principally attributable to the business managed from the United States or Canada, are administered there independently.

Patents and know-how

The patent rights which are to be transferred as part of the Spin-off at the request of LANXESS and within five years of the Spin-off taking effect cover all of the patents necessary for the LANXESS business activities. In total, these entail approximately 1,800 patent families worldwide, with approximately 8,000 patents or patent applications in all important industrial nations. The patent portfolio is wide-ranging and covers the various business units of the Group. LANXESS acquires patent rights by asserting its rights to employee inventions and submitting them for registration and by licensing third-party patents. In addition to patents, LANXESS possesses confidential know-how.

Certain patents are of particular importance to individual business units:

In the Performance Rubber segment, patents and patent applications are of particular importance, *inter alia*, as regards polybutadiene rubbers, where they are of particular relevance to anionic and Ziegler-Natta-catalysed polybutadiene rubbers (Polybutadiene Rubber). Moreover, patents and patent applications are particularly important with respect to technical rubber products, rubber gels (Technical Rubber Products) and with respect to modified butyl rubber compounds, which can be used for the manufacture of high quality rubber products for the tyre and rubber industry (Butyl Rubber).

For business activities in the Engineering Plastics segment, patents and patent applications used for the manufacture of ABS polymers and finished ABS products (Styrenic Resins) are of particular importance, in addition to patents and patent applications with respect to stabilised metal building components, the processing and treatment of glass fibres as fillers for polymers and with respect to the manufacture of polyamides and polybutylene terephtalate (Semi-Crystalline Products). Fibre-related patents and patent applications are focused on additives and stabilisers for fibre manufacture or application thereof (Fibers).

Important patents and patent applications of business units in the Chemical Intermediates segment principally concern the manufacture of starting and intermediate products for crop protection, active ingredients used in pharmaceuticals and other high quality fine chemicals such as starting products for cosmetics (Fine Chemicals), aromatics chemistry such as the production of aromatic compounds for chlorination and nitration and amino compounds (Basic Chemicals) and inorganic pigments for use in colouring construction materials and technical oxides, such as iron oxide, for use as adsorbers in drinking water and wastewater (Inorganic Pigments).

For the business units of the Performance Chemicals segment, patents and patent applications are particularly important with respect to wood preservation, industrial preservatives and disinfection (Material Protection Products), the manufacture of dichromate (Leather), textile pre-treatment, dyeing auxiliaries and textile finishing (Textile Processing Chemicals) and paper dyes and fluorescent whitening agents, process chemicals and functional chemicals (Paper). Moreover, the patent portfolio includes, among other things, industrial property rights for the production of monodisperser ion exchangers, for the manufacture of special ion exchangers for water purification and their use in power plants, and patents and patent applications with respect to the adsorption of heavy metals from groundwater and drinking water (ion exchange resins). Finally, patents and patent applications with respect to additives for rubber, plastics and lubricating oils (RheinChemie), in the area of specialty chemicals (e.g., for anti-reversion agents), radiation protection agents, and vulcanisation activators (Rubber Chemicals), and with respect to dyes for optical data storage and for plastics (Functional Chemicals) are of particular importance.

Trademarks

The trademark rights, which are to be transferred as part of the Spin-off at the request of LANXESS, cover approximately 300 active trademark families and a total of approximately 8,700 trademark registrations. The trademark portfolio is currently being reviewed to determine those trademarks important for LANXESS' business activities. In future, the Group will, in general, register new marks in all countries, in which significant sales of the relevant product are expected. The business name ''LANXESS'' and numerous product markings are trademark protected. Based on the Group's four segments, the following trademarks are of particular importance to LANXESS:

For the Performance Rubber segment, the trademarks Buna™ (not registered in the United States) and Taktene® (Polybutadiene Rubber), Perbunan®, Therban® and Levapren® (Technical Rubber Products) are particularly noteworthy. The trademark Buna™ is subject to an agreement with Buna Dow Leuna Olefinverbund GmbH, pursuant to which the parties grant each other a licence to use Buna™ as a trademark and company name.

Important trademarks in the Engineering Plastics segment include Durethan® and Pocan® (Semi-Crystalline Products); Novodur®, Lustran®, Absolac™, Absolan™, Triax® and Centrex® (Styrenic Resins) and Dorlastan® and Atlas® (Fibers).

For the Chemical Intermediates segment, the trademark Bayferrox® (Inorganic Pigments) is particularly important.

For the Performance Chemicals segment, the most important product trademarks include Preventol®, Tektamer®, Velcorin®, Metasol® and Biochek® (Material Protection Products); Chromosal®, Tanigan®, Levaderm® and Euderm® (Leather); Diadavin®, Tannex® and Tanaprint® (Textile Processing Chemicals); Levacell®, Pontamine® and Astra™ (Paper); Rhenogran®, Aflux® and Stabaxol® (RheinChemie); Vulkanox® and Vulkacit® (Rubber Chemicals) and Lewatit® and Ionac® (Ion Exchange Resins) and Macrolex® (Functional Chemicals).

Licences

The patent licence agreements with Bayer MaterialScience AG are particularly important. Pursuant to these agreements, the parties grant each other a licence (some exclusive, some non-exclusive) with respect to certain patents, limited in scope to certain fields of activity of the licensee (see ''*Business Transactions and Legal Relationships with Related Parties — Business Transactions and Legal Relationships with the Bayer Group*'').

Moreover, the licence agreement concluded during the course of the Spin-off with Bayer AG, granting the affiliated companies of the LANXESS Group an exclusive and royalty-free licence to use certain marks containing the letter combination ''BAY'' for an indefinite period, is also important (see the subsection herein entitled ''— *Products Portfolio*'').

In addition, LANXESS is party to a large number of other licence agreements. The following agreements are particularly important to individual business units:

Pursuant to a non-exclusive licence agreement with the Massachusetts Institute of Technology, U.S.A., LANXESS is entitled to use the so-called ''Buchwald Technology'' which relates to the coupling reactions for aromatics. The products manufactured under this procedure constitute suitable starting materials for agricultural and pharmaceutical chemicals (Fine Chemicals). Pursuant to licence agreements relating to ion oxides entered into with Toda Kogyo Corp., Hiroshima, Japan, LANXESS has been granted a non-exclusive licence to manufacture special magnetic particles for magnetic toners and non-exclusive licences in industrial property rights for compacted ion oxide pigments which are used for colouring cement or mortar (Inorganic Pigments).

Moreover, LANXESS has granted MeadWestvaco Corp., Delaware and Stamford, Connecticut, a non-exclusive right to manufacture certain microcapsules in the United States and for the worldwide distribution of carbonless copy paper (Paper). The patent and know-how licence agreement with Weifang Weipeng Chemical Co. Ltd. (''Weifang Weipeng'') which, as part of a joint venture project with Weifang Yaxing Chemical Co. Ltd. (''Weifang'') under which LANXESS agreed to relocate its production of hydrazine hydrate to the People's Republic of China was originally executed by Bayer Chemicals AG and later transferred to LANXESS, grants Weifang Weipeng a non-exclusive right, *inter alia*, to manufacture azodicarbonamide (ADC) and also provides the necessary know-how for this purpose. ADC is used as a primary component for blowing agents which LANXESS sells, for example, under the trademarks Porofor® and Genitron®. Furthermore, a patent licence and know-how agreement was executed with LANXESS Yaxing Chemicals Co. Ltd, the joint venture company formed together with Weifang. Under this agreement, LANXESS grants the joint venture company a non-exclusive right to manufacture hydrazine hydrate and provides it with the necessary know-how (Functional Chemicals).

In addition, LANXESS GmbH is party to a variety of intra-Group licence agreements. These licence agreements create a legal basis for other LANXESS companies (for example, those having their registered office abroad) to use LANXESS GmbH's technology.

With respect to its own trademarks, LANXESS GmbH will enter into new licence agreements with LANXESS Group companies and, where applicable, with joint venture companies. Licence agreements will continue to be concluded with downstream manufacturers (pursuant to so-called ''supporting trademarks'') as will agreements with respect to manufacturing and distribution licences, except where LANXESS becomes party to agreements already in place.

Employees and Pensions

The following table provides an overview of the number of employees (headcount) of the LANXESS Group as of 31 December 2002, 31 December 2003 and 30 September 2004, broken down according to segments and functions:

Segment	As of 31 December 2002	As of 31 December 2003	As of 30 September 2004
Performance Rubber	3,151	2,999	3,133
Engineering Plastics	3,844	3,658	3,698
Chemical Intermediates	4,265	4,059	3,925
Performance Chemicals	5,129	4,881	5,041
Service Functions and Corporate Center	5,071	4,826	3,822
Total	21,460	20,423	19,619

The decline in the number of employees is attributable above all to rules concerning age-related retirement and to ordinary employee turnover. In the first nine months of 2004, the staff cutbacks associated with the shutdowns of the plants in Marl and Goch (Germany) also played a role. The total number of employees also includes those employees currently distributing LANXESS products pursuant to agency agreements entered into with the Bayer Group. As of 30 September 2004, this entailed approximately 400 employees. After the Spin-off takes effect, these employees will continue to belong to the Bayer Group. As a result, the number of employees attributable to the LANXESS Group will decline compared to the total number of employees reported as of 30 September 2004.

In fiscal year 2002, an average of approximately 21,730 employees were attributable to the business activities combined in the LANXESS Group, approximately 3,230 of whom were in the Performance Rubber segment, approximately 3,900 in the Engineering Plastics segment, approximately 4,330 in the Chemical Intermediates segment and approximately 5,200 in the Performance Chemicals segment, while approximately 5,070 held service and Corporate Center positions. In fiscal year 2003, approximately 20,940 employees were attributable to the relevant business activities, approximately 3,070 of whom were in the Performance Rubber segment, approximately 3,750 in the Engineering Plastics segment, approximately 4,160 in the Chemical Intermediates segment, and approximately 5,010 in the Performance Chemicals segment, while approximately 4,950 held service and Corporate Center positions. Until 30 September 2004, approximately 19,850 employees were in the LANXESS Group in 2004, approximately 3,170 of whom were in the Performance Rubber segment, approximately 3,740 in the Engineering Plastics segment, approximately 3,970 in the Chemical Intermediates segment, and approximately 5,100 in the Performance Chemicals segment, while approximately 3,870 held service and Corporate Center positions.

In fiscal years 2002 and 2003, LANXESS AG, as a so-called ''shelf company'' (*Vorratsgesellschaft*), did not have any employees. As of 30 September 2004, 56 employees were employed at the LANXESS Corporate Center, which currently constitutes an organisational unit within Bayer AG. Their employment contracts will pass to LANXESS AG when the Spin-off takes effect. The Company assumes that the number of employees at the LANXESS Corporate Center will increase to approximately 90 as a result of the creation of new functions once the Spin-off takes effect.

LANXESS has made pension commitments in order to secure the retirement pensions of its employees. In this regard, as of 31 December 2003, €283 million of the defined benefit obligations for pensions were attributable to unfunded pension obligations, and €835 million were attributable to funded pension obligations. As of the same date, the defined benefit obligations for other post-employment benefits totalling €146 million were completely unfunded.

The respective defined benefit obligations are faced in the balance sheet with provisions for pensions and other post-employment benefits of €408 million, consisting of pension obligations of €279 million and obligations similar to pension obligations of €129 million. Pension obligations are faced on the asset side with other assets from pension commitments amounting to €89 million. See the description in the section ''*Notes to the Balance Sheets — (26) Provisions for pensions and other post-employment benefits*'' in the Notes to the Combined Financial Statements for fiscal year 2003 in the financial section. The possibility of future increases in pension provisions and annual contributions to the pension fund cannot be excluded. If LANXESS continues to make additional pension commitments to executives under individual agreements, further pension obligations on the part of LANXESS are created, which are not covered by the above-mentioned pension provisions.

As part of the Spin-off, a General Works Agreement to Safeguard Sites and Employment III (*Gesamtbetriebsvereinbarung für Standort- und Beschäftigungssicherung III*) (hereinafter referred to as ''SOS III'') was concluded (see ''*Further Details and Explanation of the LANXESS Spin-off*''). The Company is currently reviewing all collective bargaining agreements applicable to the LANXESS Group's plants with a view to adapting such agreements to the changed overall conditions. The Company's Board of Management has already adopted resolutions regarding specific personnel-related issues. Initial talks and negotiations with employee representatives in connection with the planned measures have commenced. The parties to these talks and negotiations have been unable to agree on individual issues to date.

Employee Participation Programme

In 2005, the Company plans to launch an employee participation programme in the form of a stock purchase programme for LANXESS Group employees. The individual components of this stock purchase programme are currently being developed. The Company is particularly considering granting employees covered under collective bargaining agreements, as well as lower and middle management employees, an opportunity to purchase at a discounted price employee shares in LANXESS AG directly after disbursement of the annual profit sharing payment. The shares purchased will be subject to a lock-up period. It is expected that the amount of the price discount will be determined on the basis of the Company's financial condition and will be reset annually by the Company's Board of Management. The number of shares offered for purchase would be contingent upon the share price prevailing at the time at which they are granted and the remuneration level of the qualified employee.

Programme for Executives

In order to establish an incentive system aimed at increasing the company's value in the long term, plans exist to offer a long-term incentive programme sometime in 2005 for employees at the top management level of the LANXESS Group. This programme is to provide for variable compensation depending on the stock market performance of LANXESS Shares and the attainment of certain company financial targets. The programme is to consist of two components, namely, a Stock Appreciation Rights Plan (virtual stock option plan) and an Economic Value Plan (long-term cash bonus based on an increase in company value). The Company's new Supervisory Board, which takes office at the expiry of the date on which the Spin-off takes effect (no sooner than the end of 28 January 2005), will begin discussing a stock participation programme for the Board of Management after it takes office.

Real Property and Operating Sites

LANXESS operates production sites in 18 countries. Moreover, in a large number of countries, the Group, as either owner or lessee, uses land with office buildings, warehouses, research and development facilities and other facilities.

As of 30 September 2004, LANXESS GmbH and its direct and indirect subsidiaries owned total land surface area of approximately 19,580,000 m^2. Of this area, approximately 4,440,000 m^2 is developed, and approximately 805,000 m^2 has been built upon. The foregoing figures do not include the approximately 1,114,000 m^2 of surface area at the site in Antwerp, Belgium, which was transferred to LANXESS on 1 October 2004.

In addition, LANXESS uses real property with a total land surface area of approximately 500,000 m^2 — approximately 430,000 m^2 of which is developed, and approximately 220,000 m^2 of which is built upon — under hereditary building rights (*Erbbaurechten*) or pursuant to foreign long-term lease arrangements that are similar to a grant of hereditary building rights. The following table provides an overview of the real property holdings used on the basis of such arrangements as of 30 September 2004.

Hereditary Building Rights and Similar Long-Term Lease Arrangements*

Location	Area/Space (approx.)**	Name of Owner	Total Term
Antwerp (Belgium)	96,500 m^2	Bayer Antwerpen NV	99 Years
Shanghai (PR China)	49,900 m^2	PR China	50 Years
Wuxi (PR China)	35,800 m^2	PR China	42 Years
Wuxi (PR China)	16,300 m^2	PR China	49 Years
Qingdao (PR China).........	28,400 m^2	PR China	50 Years
Greppin (Germany)	19,300 m^2	Bayer Bitterfeld GmbH	Indefinite
Marl (Germany)	117,800 m^2	Degussa	99 Years
Filago (Italy)................	11,600 m^2	Bayer SpA Italy	30 Years
Singapore (Singapore)	29,400 m^2	Juong Town Corporation	30 Years
Tarragona (Spain)	80,000 m^2	Bayer Polimeros S.L	99 Years
Alcantarilla (Spain)	17,000 m^2	Derivados Quimicos S.A	50 Years

* 56,000 m^2 of land at the Dormagen site, currently used under a hereditary building right held by Bayer AG, was sold to LANXESS GmbH pursuant to the land purchase agreement between LANXESS GmbH and Bayer AG dated 30 December 2004.

** Rounded figures.

LANXESS GmbH currently also uses real property located at the factory site of the chemical park sites in Leverkusen, Dormagen, Krefeld-Uerdingen and Brunsbüttel, pursuant to lease agreements with Bayer Industry Services GmbH & Co. OHG. On 30 December 2004, LANXESS GmbH entered into a land purchase agreement with Bayer AG with respect to an area totalling approximately 937,000 m^2 on the above-mentioned factory site, which will enter into effect at the end of the first calendar day following the Spin-off. The area largely involves land parcels that have not yet been surveyed. Approximately 552,000 m^2 of the land sold has been built upon. The purchase price for the real property and operating equipment is approximately €256 million. Possession, use and encumbrances pertaining to the land sold will pass to LANXESS GmbH once the land purchase agreement enters into effect. Ownership of the land will be conveyed to LANXESS GmbH as soon as the land register (*Grundbuch*) requirements for this purpose have been met.

The transfer to LANXESS of foreign real property totalling approximately 74,000 m^2 is still pending. The relevant agreements have already been concluded. The Company expects that the conveyances will be effected during the course of 2005.

The following table provides an overview of LANXESS' most important sites as of 30 September 2004:

LANXESS' Most Important Sites

Site	Area (approx.)*	Ownership/Lease/ Hereditary Building Right/Purchased from Bayer AG**	Use of the Site
Leverkusen Chemical Park Site	369,500 m^2	Purchased from Bayer AG**	Production, administration, marketing, research and development, storage, technical service
Dormagen Chemical Park Site	225,800 m^2	Purchased from Bayer AG**	Production, administration, marketing, research and development, storage, technical service
Krefeld-Uerdingen Chemical Park Site	260,500 m^2	Purchased from Bayer AG**	Production, administration, marketing, research and development, storage, technical service
Antwerp (Belgium)***	1,114,000 m^2/ 96,500 m^2/ 27,700 m^2	Ownership/Hereditary building rights/lease	Production, administration, marketing, research and development, storage, technical service
Orange, Texas (U.S.A.)	3,395,000 m^2	Ownership	Production, marketing, technical service
Sarnia, Ontario (Canada)	1,926,000 m^2	Ownership	Production, administration, marketing, research and development, storage, technical service

* Rounded figures.

** Land parcels that have not been surveyed on the factory sites of the chemical park sites in Leverkusen, Dormagen and Krefeld-Uerdingen, and which were purchased by LANXESS pursuant to the land purchase agreement between LANXESS GmbH and Bayer AG dated 30 December 2004.

*** Land with an area of approximately 1,114,000 m^2 at the Antwerp site was transferred to LANXESS on 1 October 2004.

Environment

The acquisition, production and distribution of many products manufactured by LANXESS require the use, storage, transport and removal of poisonous and hazardous materials, chemicals and substances. LANXESS is subject to comprehensive environmental protection laws, other statutes, technical rules and standards, which are constantly developing and becoming ever more stringent. These concern, among other things, the restriction of air pollution, discharges into above-ground and underground waterways, other emissions into the environment, the production, handling, storage, transport, use and treatment or removal of waste, and compliance with safety provisions at the work place to provide protection against hazardous substances.

One example of increased risk due to intensified environmental legislation is the Environmental Liability Directive 2004/35/EC dated 21 April 2004, which must be implemented in EU Member States by 30 April 2007. Pursuant thereto, companies in the chemicals industry will be subject to extensive obligations to refrain from certain actions as well as duties of remediation with respect to any events of hazard or damage that occur after 30 April 2007. This applies to damage to biological diversity (protected species and natural living environments) in addition to soil and waterways. The risks with regard to costs for companies in the chemicals industry will critically depend on the implementing legislation of the Member States. Thus, for example, Member States can restrict liability for approved emissions and development risks to cases of culpable conduct. However, they are under no obligation to do so.

The extensive environmental statutes, regulations and other provisions applicable to the LANXESS Group's business may result in LANXESS having to remove or restrict contamination, deposits or other effects from the emission of chemicals at relevant sites.

Given that LANXESS' production plants have already been used for industrial purposes for a long time — in some cases for more than 100 years — significant contamination could be present on LANXESS' sites. Within the LANXESS Group, there has been soil and groundwater contamination at some sites in the past; the possibility that such contamination will occur or be discovered at other locations cannot be excluded. In addition, LANXESS is responsible for a large number of industrial sites containing, in some cases, pre-existing contamination requiring securing or remediation. Frequently, the associated costs can hardly be estimated. Examples of risks associated with pre-existing contamination to which LANXESS is exposed are described in the section entitled ''*Risk Factors — Risks relating to the Business of LANXESS — Obligations arising from environmental protection laws and liability for pre-existing contamination*''. Claims may be asserted by federal or state regulatory authorities, and also by private organisations and individuals. In some countries in which the LANXESS Group operates, LANXESS could be exposed to other legal consequences over and above the remediation of environmental damage, such as the payment of damages or penalties. A particular liability risk with respect to environmental damage exists for the LANXESS sites in New Jersey, U.S.A. Pursuant to the ''Natural Resource Damages'' initiative of the New Jersey Department of Environmental Protection, all companies whose past industrial activities may have contributed to the environmental damage, are held accountable for the remediation of such damage — on the basis of unclear criteria — by way of class action lawsuits.

To the extent that cost estimates are presented below, they are generally based on assumptions concerning the most likely extent of damage and the most likely cost of remediation (''most likely case'').

Increasingly stringent legal provisions on the restriction of emissions of pollutants have necessitated measures to reduce emissions at a number of LANXESS production sites. Such provisions include, in particular, those contained in the VOC Directive (Directive 1999/13/EC on the limitation of emissions of volatile organic compounds dated 11 March 1999) and also, for German production sites, the pollution control rules of the Technical Instruction on Air Pollution Control dated 24 July 2002 (TA Luft 2002). In the case of facilities that meet the requirements under TA Luft 1986 but not, however, the requirements of TA Luft 2002 (so-called ''existing facilities''), the competent authorities may generally demand that the necessary remediation of the facility be completed on or before 30 October 2007, and that all requirements be met by such time. As a whole, LANXESS estimates the costs for the technological modernisation of its plants at all sites until October 2007 pursuant to TA Luft 2002 and other emissions legislation at approximately €80 million.

The wastewater treatment plants operated at LANXESS' production sites must constantly be adapted to qualitatively expanded discharge requirements. Because of emerging changes in the law, LANXESS anticipates investment requirements of approximately €20 million for wastewater treatment plants for all sites in coming years.

Financial risks arising from inspection and remediation liabilities also exist with regard to approximately 30 sites in the United States, which were or are owned by LANXESS or were operated by LANXESS, or with regard to sites at which LANXESS' waste was stored or treated. Liability on the part of LANXESS may arise, *inter alia*, pursuant to the U.S. environmental protection act generally referred to as ''Superfund'' (Comprehensive Environmental Response, Compensation, and Liability Act or ''CERCLA''), the Resource Conservation and Recovery Act (''RCRA'') and similar U.S. state statutes and regulations. Pursuant to CERCLA, potentially both the owner and the operator of the affected facility at the time of contamination are responsible for a Superfund property. At most of the relevant U.S. sites, numerous companies — including the LANXESS Group — have been advised that the U.S. Environmental Protection Agency (''EPA''), individual state authorities and private entities and individuals assume that the relevant companies might be responsible for remediation pursuant to the above-mentioned legislation or regulations thereunder. At other U.S. sites, the LANXESS Group is the sole responsible party.

A change in ownership of a given land parcel might also result in inspection and remediation liabilities, e.g., as a result of an obligation on the part of the buyer to assume responsibility for remediation and to provide security for any disposal costs.

As of 30 September 2004, LANXESS had set aside provisions for environmental protection liabilities totalling €85 million. For other potential risks associated with environmental damage events, see the section entitled ''*Risk Factors — Risks relating to the Business of LANXESS — Obligations arising from environmental protection laws and liability for pre-existing contamination*''.

In a master agreement concluded contemporaneously with the spin-off and acquisition agreement, Bayer AG and LANXESS AG agreed on which of the contract parties, as between themselves, bears the liability for property-related environmental contamination that was caused or arose prior to the Spin-off date (1 July 2004). Generally speaking, the legal consequence of the liability of a given contracting party is that it is generally required fully to indemnify the other contracting party and its affiliated companies for any liability *vis-à-vis* authorities or other third parties arising out of public and private law with respect to environmental contamination on the relevant property. The provisions allocating liability for environmental damage essentially attribute liability, based on the condition of a particular property (*Zustandshaftung*), to the contracting party which used such property (or whose affiliated companies used such property) as of the relevant date. The liability provisions also contain individual elements of the principle of causation-based liability (*Verursachungshaftung*). In effect, liability attaches to the relevant property concerned and, in simplified terms, differentiates as follows:

In principle (subject to any possibility of release that is foreseen), LANXESS AG is liable for any and all environmental contamination on the so-called ''LANXESS properties''. These essentially entail real property used abroad by LANXESS on the effective date in Germany and abroad which the companies of the LANXESS Group have, in some cases, particularly abroad, already obtained, or will obtain from Bayer AG. Bayer AG is liable, in principle (also subject to any possibility of release that is foreseen) for any and all environmental damage on the so-called ''Bayer properties''. These essentially entail any and all real property owned by Bayer AG or its affiliated companies and used by LANXESS (with the exception of the LANXESS properties). With respect to liability for environmental contamination on the real property of other third parties, the contracting parties have agreed that LANXESS will be liable therefor if the environmental contamination was caused by a LANXESS property via the groundwater. In addition, the master agreement also contains special provisions for allocating liability in relation to environmental contamination on specific properties (including landfills) and for liability for environmental damage under certain acquisition agreements.

The master agreement caps LANXESS' liability for environmental contamination of real property at €350 million. However, in simplified terms, this liability cap applies only to remedial action ordered, agreed upon or actually carried out by the end of 2009. Otherwise, LANXESS AG and its affiliated companies bear unlimited liability for environmental contamination.

Regulatory Provisions

The LANXESS Group is subject to applicable legislative and regulatory provisions that govern its business operations in every country in which it operates. These include, in particular, provisions concerning technical safety and environmental protection, provisions concerning filing, registration and labelling, provisions concerning the handling of chemicals, building provisions, employment law provisions and provisions governing job protection and work safety.

Environmental regulations are of particular importance to the LANXESS business. The most important ramifications of these laws are described in the section entitled ''— *Environment*''.

The regulatory environment for companies in the chemicals and related industries is subject to constant change and is continuously changing at the international, and, above all, the supra-national and national levels, in order to conform to technological progress and the increased safety needs and environmental awareness. This tightening of requirements could have adverse effects on LANXESS' production costs and product portfolio.

Of great significance for the business activities of LANXESS will be the implementation of the proposed EC regulation on the Registration, Evaluation, Authorisation and Restriction of Chemicals (''REACh''), the draft of which was submitted by the European Commission on 29 October 2003. The current system for general industrial chemicals distinguishes between new substances that were first brought onto the market after September 1981 and that must be inspected and assessed for risks to human health and the environment in accordance with Directive 67/548/EEC (deemed to be registered substances for purposes of REACh), and so-called ''existing substances'', the existence of which in the market was known in September 1981. 99% of all substances on the market are existing substances. Approximately 140 of these substances currently count as prioritised substances and are subject to comprehensive risk assessments by the authorities of the member states in accordance with the EC Regulation on the evaluation and control of the risks of existing substances (Regulation (EEC) No. 793/93). In the Commission's opinion, the current procedure for risk assessment is neither efficient nor effective and is to be replaced by the REACh system.

- REACh prescribes a general registration duty for substances manufactured or imported in quantities in excess of one tonne. Under the Commission's proposal, unregistered substances may not be manufactured or imported.

- With respect to substances giving rise to particular concern, an authorisation system for use and market introduction of such applications will be launched. This affects substances that fall into the following categories: ''carcinogenic, mutagenic and reproductively toxic'' (CMR), ''persistent, bio-accumulative, toxic'' (PBT) and ''very persistent, very bio-accumulative'' (vPvB). The requirements under the authorisation procedure are risk-based: It is incumbent upon the applicant to prove that the risks in relation to use of the relevant substance are reasonably controlled or that these are outweighed by the socio-economic benefits of their introduction into the markets. A duty to substitute these substances using appropriate alternative substances or technologies may apply.

In order to facilitate the transition to the REACh system for those substances that are already on the Common Market, the draft regulation provides for the gradual introduction of the registration requirements over three years (for substances in the CMR group categories 1 and 2 in a quantity in excess of 1 t/a and for other substances in a quantity of 1000 t/a), six years (substances in a quantity of 100 to 1000 t/a) and up to eleven years (substances in a quantity in excess of 1 t/a and hazardous substances in products) after the regulation enters into effect.

As a company in the chemicals industry, LANXESS will be affected by the additional technical, organisational and financial expenses necessarily associated with the registration, evaluation and authorisation mechanisms. Additional costs will arise specifically from the preparation of chemical safety reports to be submitted for general registration purposes (Chemical Safety Report — CSR), the substance safety assessments necessary for these purposes (Chemical Safety Assessment — CSA), determining exposure and the expanded requirements for safety data sheets (Safety Data Sheet — SDS). During the course of the authorisation procedure, it may turn out that individual products of LANXESS will no longer be able to be manufactured profitably.

The regulation is not expected to enter into effect before the end of 2006 or the beginning of 2007. During parliamentary debate, the draft regulation may yet be subjected to various amendments or stopped entirely. Nevertheless, LANXESS has commenced preparations that should facilitate application of the new regulatory framework contemplated in the Commission's proposal. Thus, for example, production quantities are being recorded in accordance with the quantity thresholds for the planned registration procedure and classified according to substances and preparations. Moreover, LANXESS has commenced gap analyses in relation to the chemical-physical and toxilogical properties of the chemicals. Computer systems are being upgraded with a view to preparing CSR, CSA and SDS.

In total, LANXESS currently estimates that the costs associated with the launch of the REACh system in the eleven years allocated for full registration of all substances subject to the regulation will be €200 million.

The biocide products manufactured by LANXESS are exempted from the planned REACh regulations. They remain subject to the special authorisation procedure for biocide products under EC Directive 98/8/EC, which was implemented in Germany pursuant to sections 12a to12j of the German Chemicals Act (*Chemikaliengesetz*). The inspection and authorisation requirements will apply by no later than 2010, and in some cases prior to that date, with respect to all biocide products brought onto the market Community-wide if the relevant active ingredient was evaluated at an earlier time and included in Schedule I of the EC Directive. LANXESS assumes that this will be the case for wood preservation products.

Other future costs for companies in the chemicals industry could arise from the implementation of the ''Strategy for Environment and Health'' proposed by the European Commission in 2003 (SCALE Initiative). The aim of SCALE is to develop a Community-wide system for interlinking information about the condition of the environment, the ecological system and human health and thereby to improve, among other things, the evaluation of so-called ''cocktail effects'', combined pressures and accumulated effects on human health. It is currently unforeseeable if and when the SCALE plan of action, which initially applies for the 2004 to 2010 period, will become binding Community law.

Competition laws and regulations are also relevant to LANXESS' business. Thus, for example, advertising for hazardous substances and biocide products is subject to particular restrictions pursuant to Article 26 of Directive 67/548/EEC on the approximation of the laws, regulations and administrative provisions relating to the classification, packaging and labelling of dangerous substances and Article 22 of Directive 98/8/EC (in Germany, in conjunction with the provisions of the German Chemicals Act and the hazardous substances regulation (*Gefahrstoffverordnung*)).

Furthermore, the products manufactured and distributed by LANXESS are subject to numerous product-specific laws and regulations, in particular under European Community law. In addition to chemicals and hazardous substances laws, LANXESS must comply, above all, with the Community legal framework for biocide products, crop protection products, pharmaceuticals, medical products and for food and consumer goods, as well as EC Directive 2000/53/EC on End-of-Life Vehicles, the detailed disposal and labelling provisions of which affect plastics used in motor vehicles and thus indirectly affect LANXESS' product portfolio. With respect to food law, Directive 2002/72/EC relating to plastic materials and articles intended to come into contact with foodstuffs, for example, is notable. The provisions of this directive concerning migration thresholds must be observed in relation to LANXESS' plastic consumer goods. Amendments to the legal framework applicable to a given LANXESS product could be associated with significant capital expenditures.

Litigation/Regulatory Proceedings

The Company is not currently aware, except with respect to the proceedings described below or above under ''— *Environment*'', of any court cases, arbitrations or proceedings before administrative authorities to which either LANXESS AG or any of its subsidiaries is a party that could have a material impact on the financial condition of LANXESS or did have such impact within the last two fiscal years. The Company is also not aware of any threat of any such proceedings.

Antitrust Proceedings

Bayer AG is involved in a number of antitrust-related regulatory proceedings and civil lawsuits in the United States, Canada and Europe with respect to the LANXESS business.

As part of the Spin-off, the activities of the former Rubber Business Group of Bayer AG were transferred to the LANXESS Group. Investigative proceedings were and are being conducted by antitrust authorities in the United States, Canada and Europe in relation to various products that were or are attributable to such business activities. In the United States and Canada, a number of private class actions and individual actions are pending in this regard. Additional actions for damages can be expected in the United States, and also in Canada.

Commencing in September of 2002, the U.S. Department of Justice launched criminal investigations against Bayer AG based on various violations of Section 1 of the Sherman Act. The proceedings were based on the charge that Bayer AG had engaged in illegal price fixing with respect to various chemicals for rubber production (the period 1995 to 2001) and nitrile rubber (the period May 2002 until the end of December 2002). The investigations resulted in two indictments before the U.S. District Court for the Northern District of California in San Francisco. Bayer AG admitted its guilt to the Department of Justice in two separate settlements dated 14 July 2004 and 13 October 2004, and accepted fines of U.S.$66 million for the price fixing with respect to rubber chemicals and U.S.$4.7 million for the price fixing with respect to nitrile rubber. Both settlements were approved by the court. LANXESS established provisions totalling €20 million in the Combined Financial Statements to cover its portion of these fines, as determined by the terms of the Spin-off. Of this amount, a provision of €12 million was established for the Technical Rubber Products business unit in the Performance Rubber segment and a provision of €8 million was established for the Performance Chemicals segment, the bulk of which related to the Rubber Chemicals business unit.

The antitrust investigations by the European Commission and by the Canadian Competition Bureau with respect to the above-mentioned price-fixing arrangements are continuing. It is likely that the European Commission will impose a significant fine. For this purpose, as well as for the additional European investigation described below, with respect to which Bayer AG was not the first company to cooperate with the authorities, LANXESS has established a provision of €15 million. In light of the status of the proceedings — the European Commission has not yet sent the so-called Statement of Objections containing a provisional summary of the charges — it is currently impossible to make a more detailed reliable estimate as to any risk of a fine. The Company believes that there is also the risk of a fine in Canada, which cannot yet be quantified.

Administrative antitrust investigations are also pending in some other cases against Bayer AG in conjunction with various other products that are also attributable to the former Rubber Business Group. In certain cases, only Europe is affected. In one case, the Commission is conducting the investigation itself, while in another case it has left the proceedings to the antitrust authorities of the Member States. Two other cases involve the United States and Canada in addition to Europe. In all cases, Bayer AG is cooperating with the competent antitrust authorities. In all but one of these additional cases, Bayer AG was the first affected company to file the relevant application with all competent antitrust authorities that have a special cooperation programme (‘‘leniency programme’’). The Company expects that a significant fine will be imposed on it with respect to the investigation in which Bayer AG was not the first company to cooperate with the authorities. It is not currently possible to estimate the amount of this fine. With respect to the remaining investigations, the Company considers the prospects good that no fine will be imposed on Bayer AG.

In the United States and Canada, various class actions and individual actions are pending against Bayer AG, several of its subsidiaries and two subsidiaries of LANXESS (RheinChemie Rheinau GmbH and RheinChemie Corp., Trenton, New Jersey) with respect to the foregoing violations of antitrust law. In these proceedings, the plaintiffs — direct and indirect purchasers of the relevant rubber products — are claiming not-yet quantifiable damages (including treble and punitive damages), which could be potentially significant. Additional lawsuits seeking damages can be expected in both the United States and Canada.

The financial risk associated with all of the proceedings mentioned above (with the exception of criminal proceedings in which penalties have already been imposed), including the financial risk associated with future civil damage actions, is currently not quantifiable. The Company expects that significant expenses will be required during the further course of the criminal proceedings and civil damage actions.

In a master agreement, LANXESS AG and Bayer AG have agreed to specific terms and conditions concerning the antitrust proceedings relating to the former Rubber Business Group of Bayer AG. With respect to liabilities arising out of proceedings (whether in the form of fines, damages, punitive damages or claims on the disgorgement of excess revenues arising from the antitrust violation) that had at least commenced prior to 1 July 2004 or in respect of which a company had taken steps prior to 1 July 2004 before an antitrust authority with a view to commencing such proceedings, LANXESS AG will bear 30% and Bayer AG 70% of such liabilities, as between themselves. Furthermore, LANXESS AG's liability is limited to a total of €100 million. In addition, any tax disadvantages arising thereby due to limited deductibility for tax purposes are to be reimbursed. The reimbursement payments are limited to €50 million per calendar year. The Company considers it possible that the indemnity obligation of up to a total of €100 million, in addition to the tax indemnity, will fully materialise. In accordance with the terms of a master agreement, LANXESS AG and Bayer AG are to agree on rules for handling the proceedings (for more details concerning the master agreement, see the section entitled ''*Business Transactions and Legal Relationships with Related Parties — Business Transactions and Legal Relationships with the Bayer Group*'').

A number of class actions were filed in the United States against RheinChemie Corp. and RheinChemie Rheinau GmbH, in addition to Bayer Corporation, Pittsburgh, Pennsylvania and other companies. The class actions are based on Section 1 of the Sherman Act and charge the defendants with price fixing with respect to, among other things, adipic acid-based polyester polyols during the period from February 1998 to 2002.

Ficobel

On 29 June 2002, the French company, Ficobel S.A.S., Puteaux, France, brought proceedings against LANXESS Elastomères S.A.S., Lillebonne, France (a wholly-owned subsidiary of LANXESS GmbH) for payment of €9,688,324.62 plus interest based on a steam supply agreement between the two companies relating to steam supply in the years 2000 to 2003. Alternatively, the agreement should be renegotiated pursuant to the ''hardship clause''. Should the negotiations fail, LANXESS Elastomères S.A.S. should under the claim be ordered to pay a penalty of €7,075,919.00 plus taxes. Moreover, the plaintiff asserted a claim based on procedural grounds for €30,000.00. The defendant, LANXESS Elastomères S.A.S., asserted a counterclaim for damages of €675,000.00, repayments of €2,953,700.00 (in each case plus interest) as well as a claim based on procedural grounds for €25,000.00. In addition, as security for enforcement of the expected judgment, it filed an application that Finergaz S.A. — the parent company of Ficobel S.A.S. which had provided a guarantee of performance of the agreement by Ficobel S.A.S. in a comfort letter given to LANXESS Elastomères S.A.S. — be joined to the proceedings.

On 30 June 2004, the Tribunal de Commerce de Paris ordered LANXESS Elastomères S.A.S. to pay Ficobel S.A.S. €9,688,324.60 plus interest for the supply of steam and €20,000.00 for procedural costs, and to pay Finergaz S.A., which had been joined to the proceedings, €2,000.00 in costs on procedural grounds. Defendant LANXESS Elastomères S.A.S. filed an appeal against the judgment with the Cour d'Appel on 13 October 2004.

Ficobel S.A.S. could assert additional claims associated with the explosion of one of the generators used by Ficobel S.A.S. on the grounds of the production facility. In this respect, Ficobel S.A.S. has commenced proceedings against LANXESS Elastomères S.A.S. and other parties to secure evidence.

PolymerLatex GmbH & Co. KG

In an extrajudicial dispute, settled by means of an agreement dated 28 October 2004, LANXESS Elastomères S.A.S. and PolymerLatex GmbH & Co. KG disputed the validity of a contract manufacturing agreement in place between them. In accordance with the terms of the settlement, the dispute was settled against payment of a net amount of €4.5 million by PolymerLatex GmbH & Co. KG to LANXESS Elastomères S.A.S.

Prosytec

Since 1994, a total of 148 proceedings before various French courts have been instituted against LANXESS S.A.S., Puteaux, France, Bayer AG and Bayer Polysar International S.A., Fribourg, Switzerland, based on the delivery of allegedly faulty raw materials (Butyl XL 20/ Butyl XL 10000) to Prosytec S.A. The proceedings were instituted by Prosytec S.A., its insurers and its end customers. The amount at issue for all proceedings totalled approximately €150 million. With the exception of a few minor proceedings, these disputes have since been decided at the highest judicial level in favour of the defendants LANXESS S.A.S., Bayer AG and Bayer Polysar International S.A. In particular, Prosytec's appeal in the largest proceeding involving approximately €104 million was dismissed in July 2004 by the Cour de Cassation. Only in a counterclaim for damages filed by LANXESS S.A.S. was LANXESS S.A.S. ordered to pay costs of the other parties in the amount of approximately €85,000.00.

Rütgers Elbechemie GmbH

In connection with the sale of the H-acid production of the Bayer Group in Brunsbüttel, Bayer AG had promised Rütgers Elbechemie GmbH, Castrop-Rauxel, that it would assume the shutdown costs in the event of the shutdown of production by Rütgers Elbechemie GmbH. Differences of opinion concerning the amount of the payment due were settled by means of a settlement agreement entered into in June 2004, pursuant to which Bayer Chemicals AG paid a final one-off amount of €4.8 million. The agreement was assigned to LANXESS as part of the combination of the chemicals and polymers activities in LANXESS GmbH and its subsidiaries.

Asbestos Litigation

The Bayer Group is currently involved in a number of asbestos-related disputes in the United States. These disputes passed to the LANXESS Group as part of the Spin-off with respect to several sites.

Silicon dioxide ''Silica'' Case

Lawsuits have been filed in Graves County, Kentucky, against Bayer Corporation — as the legal successor to Mobay Corporation, New Jersey, of Miles, Inc., Indiana, and of Agfa Corporation, New York — together with other defendants, by former employees and other third parties in connection with alleged injury to health based on the alleged handling of materials containing silicon or use of products containing silicon. Based on the current status of the proceedings, the possibility that sites passing to LANXESS under the Spin-off will also be affected, thereby triggering liability on the part of LANXESS, cannot be excluded.

Albemarle Corporation

Bayer Chemicals Corporation, Pittsburgh, Pennsylvania filed for a declaratory judgment against Albemarle Corporation, Richmond, Virginia (''Albemarle'') before a Federal District Court. The court was asked to issue a binding declaration with respect to the contents of certain provisions in a supply agreement between Albemarle and Bayer Chemicals Corporation. The District Court ruled in favour of Bayer Chemicals Corporation. Albemarle filed a counter-claim and appealed against the lower court's decision. Should the Court of Appeals reverse the judgment of the District Court and reach the opposite conclusion, such a ruling would result in a payment obligation on the part of LANXESS, inasmuch as LANXESS has become a party to the dispute by virtue of the combination of the chemicals and polymers activities in LANXESS GmbH and its subsidiaries.

National Drying Machinery Company

Bayer Chemicals Corporation, Pittsburgh, Pennsylvania brought an action for damages in state court in Pennsylvania against National Drying Machinery Company, Philadelphia, Pennsylvania, U.S.A. The complaint is based upon the delivery of an allegedly faulty pigment dryer at the end of 1999, the faults in which were allegedly not cured in the subsequent period. Should the court rule against National Drying Machinery Company, LANXESS, as the legal successor to Bayer Chemicals Corporation, could be awarded damages in a not insignificant amount, inasmuch as LANXESS has become a party to the dispute by means of the combination of the chemicals and polymers activities in LANXESS GmbH and its subsidiaries.

Troy Chemical Corporation

Troy Chemical Corporation Inc., New Jersey, U.S.A. (hereinafter referred to as ''Troy Chemical Corporation''), and Bayer AG had entered into a production, licensing and marketing agreement for the Material Protection Products business unit (MPP), which now belongs to LANXESS. Bayer AG terminated this agreement in 1998. In 2001, Troy Chemical Corporation instituted arbitration proceedings before the International Chamber of Commerce and demanded, among other things, damages of at least U.S.$3 million based on an alleged breach of contract. In September 2003, the complaint was dismissed in full and Troy Chemical Corporation was ordered to pay the costs incurred by all the parties. No further legal remedies are available to Troy Chemical Corporation.

Bomanite Corporation/QC Construction Products LLC

On 5 January 2005, LANXESS Corporation was served with notice of a claim by Bomanite Corporation, Madera, California, U.S.A. and QC Construction Products LLC, Delaware and Madera, California, U.S.A. against LANXESS Corporation in the Superior Court of California, Madera County. In addition to LANXESS Corporation, the suit also names, *inter alia*, Bayer Corporation and Bayer Chemicals Corporation. The suit alleges various breaches of the duty to supply Bomanite Corporation with products pursuant to an existing supply agreement, misappropriation of trade secrets and breaches of other agreements for which damages in the amount of at least U.S.$650,000, an unspecified amount of punitive damages, injunctive relief and other types of remedies are sought.

LANXESS has agreed to indemnify Bayer Corporation and Bayer Chemical Corporation against any and all liability possibly arising out of this litigation. As the litigation is at an early stage, it is not possible to estimate potential liability at this time. However, if a judgment is entered against Bayer Corporation, Bayer Chemicals or LANXESS, the ultimate payment liability could have an adverse effect on LANXESS' financial position and results of operations.

TransAlta Energy Corporation

A long-term agreement is in place between LANXESS Inc. and TransAlta Energy Corporation, Calgary, Alberta, Canada, (''TransAlta'') concerning the supply of steam and electricity to the plant in Sarnia, Ontario, Canada. Pursuant to this agreement, LANXESS is obliged to purchase a certain amount of steam annually. Should LANXESS purchase different amounts of steam from those stipulated, LANXESS must pay damages to TransAlta for any shortfall. Due to the shutdown of various operations, LANXESS purchased significantly lower amounts for the period from October 2002 to December 2003 than had been agreed. At the beginning of 2004, TransAlta claimed damages of CAN$15 million. LANXESS is countering this claim by asserting that TransAlta had not provided sufficient proof of corresponding damage. At present, no litigation is pending. The supply agreement provides for arbitration proceedings in the event of disputes.

LANXESS Rubber N.V., Belgium (Taxes)

LANXESS Rubber N.V., a wholly-owned subsidiary of LANXESS GmbH, having its registered office in Belgium, was owned by the Polysar Group which Bayer purchased in 1990 from the Canadian seller, Nova Chemicals Corporation. As part of an external audit conducted around that time, the Belgian tax office evaluated various business activities with affiliated companies differently and thereupon ordered back tax payments, currently amounting to approximately €117 million (including interest) after deduction of payments already made. An appeal was filed against the relevant tax assessment notices and a suspension of enforcement of the tax assessment notices was granted against provision of security, which was provided in the form of a guarantee by a Bayer company for the current and future suspension period. Based on the existing expert opinions provided by external consultants, it can be assumed that, taking into account the payments already made, the actual tax risk related to the audit findings will not exceed the amount of €1.7 million for which provisions have been established. Moreover, the Bayer Group has an obligation towards LANXESS to bear any tax liability incumbent upon LANXESS Rubber N.V. that exceeds the amount of the established provisions.

Insurance

Until the Spin-off takes effect, LANXESS AG and its future subsidiaries are insured through the group umbrella coverage of Bayer AG against destruction of or damage to their plants and the resulting operational disruptions under a property damage and business interruption insurance policy. Within this framework, the Company and its future subsidiaries also have insurance protection under business, product and environmental liability insurance policies and goods transportation insurance policies. Under Bayer AG's group insurance policies, the members of the governing bodies of the Company and all subsidiaries furthermore enjoy directors' and officers' insurance coverage. In the Company's opinion, LANXESS enjoys reasonable insurance protection, to an extent customary in the industry, prior to the Spin-off taking effect.

Before the Spin-off takes effect, the Company will acquire new insurance policies for itself and its future direct and indirect subsidiaries, which policies will enter into effect no later than the effective date of the Spin-off. The possibility that these changes in insurance coverage could create certain additional expenses for LANXESS cannot be excluded. The Company believes that, even after the Spin-off takes effect, the companies of the LANXESS Group will continue to enjoy reasonable insurance protection, to an extent customary in the industry, under the insurance policies newly to be acquired out by LANXESS AG.

General Information on LANXESS Aktiengesellschaft

Formation, Company Name, Registered Office, Fiscal Year and Term of the Company

LANXESS AG was formed on 28 October 1999 under the name SIFRI Beteiligungs Aktiengesellschaft, having its registered office in Frankfurt am Main. The company, formed as a so-called ''shelf company'' (*Vorratsgesellschaft)* without its own business operations, was recorded in the Commercial Register (*Handelsregister*) on 18 November 1999. LANXESS AG is a stock corporation under German law (*Aktiengesellschaft*).

The annual financial statements and management reports of the Company for the fiscal years 2001, 2002 and 2003 in accordance with the German Commercial Code (*Handelsgesetzbuch* or ''HGB'') are contained in the financial section of this Listing Memorandum. Since the Company had no business operations of its own as of 30 June 2004, an interim report as of this date is not included. Until 31 December 2004, the Company was not required to prepare consolidated financial statements in accordance with HGB. In fiscal years 2001, 2002 and 2003 LANXESS AG, as a shelf company, did not generate any sales.

Bayer AG acquired all the shares of the Company by means of a purchase and transfer agreement dated 9 and 13 July 2004. On 13 July 2004, the Company's Stockholders' Meeting resolved to change the company name to LANXESS Aktiengesellschaft and to move the registered office to Leverkusen. These resolutions were recorded in the Commercial Register for the Company on 3 September 2004. The Company was capitalised in accordance with case law parameters concerning the capitalisation of shelf companies. As a precautionary measure, the provisions of the German Stock Corporation Act (*Aktiengesetz*) concerning post-formation acquisition were applied with regard to agreements with Bayer AG if the relevant preconditions existed.

LANXESS AG is recorded in the Commercial Register of the Local Court of Cologne (*Amtsgericht Köln*) under registration number HRB 53652.

Its fiscal year ends on 31 December of each calendar year.

The Company has been formed for an indefinite term.

Corporate Purpose

Under the Company's articles of association, the corporate purpose of the Company is to engage in manufacturing, distribution and other industrial activities or the provision of services in the chemicals and polymers areas.

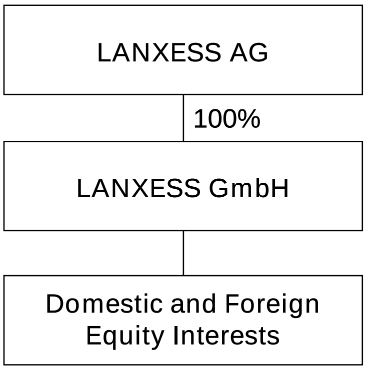
The Company is authorised to engage in any business that is related to, or directly or indirectly serves, that purpose.

The Company may establish, acquire and take participating interests in other enterprises, in particular those whose corporate purposes fully or partially cover the areas set forth above. It may bring companies in which it holds a participating interest under its uniform control or confine itself to the administration of such interest. It may carve out its operations, in whole or in part, to affiliated companies or may permit affiliated companies to perform its operations.

Creation and Structure of the LANXESS Group

Once the Spin-off takes effect, LANXESS AG, as the ultimate parent company of the LANXESS Group, will hold all of the shares in LANXESS GmbH — which itself is an operating entity and holds interests in over 50 domestic and foreign operating companies — and will largely perform the functions of a management holding company. An overview of the significant direct and indirect equity interests of LANXESS AG after the Spin-off takes effect is included in the section entitled ''*Description of LANXESS AG's Capital Stock*.'' The Board of Management of LANXESS AG plans to conclude a control and profit and loss transfer agreement with LANXESS GmbH, as the dependent company, and LANXESS AG, as the controlling company, and possibly to alter the legal ownership structure within the LANXESS Group.

The basic structure of the LANXESS Group after the Spin-off takes effect will be as follows:



The LANXESS Group will continue the majority of the chemicals and approximately one third of the polymers activities of the Bayer Group. These activities were consolidated in LANXESS GmbH (for details, see the summary of the business activities in the section entitled "*Further Details and Explanation of the LANXESS Spin-off*"). In creating the LANXESS Group, Bayer AG, as the transferring entity, will transfer to LANXESS AG, as the acquiring entity, all of the shares held by it in LANXESS GmbH by way of a spin-off (*Abspaltung zur Aufnahme*) pursuant to section 123 (2) No. 1 UmwG together with other of its assets and liabilities. In return for the spin-off of the assets and liabilities to it, LANXESS AG will issue 73,034,192 shares to Bayer AG's stockholders. In order to implement the Spin-off, Bayer AG and LANXESS AG entered into a notarised spin-off and acquisition agreement on 22 September 2004. This agreement entered into effect with the approval of the Stockholders' Meetings of Bayer AG and LANXESS AG held on 17 November 2004 and 21 December 2004, respectively. The actual Spin-off will enter into effect when the transaction is registered in the Commercial Register (*Handelsregister*) for Bayer AG at the Local Court of Cologne (*Amtsgericht Köln*). The registration is anticipated for 28 January 2005 (for details concerning the Spin-off, see the section entitled "*Further Details and Explanation of the LANXESS Spin-off*").

Stockholder Structure

As of the date of publication of this Listing Memorandum, Bayer AG, as sole stockholder, holds all currently outstanding 50,000 no-par shares of LANXESS AG.

These shares of the Company will be transferred by way of a spin-off pursuant to the German Transformation Act (anticipated for 28 January 2005) to LANXESS AG, which will issue them to Bayer AG's stockholders together with the new shares created by means of the capital increase carried out for purposes of implementing the Spin-off. When the Spin-off takes effect, all LANXESS AG shares will be held by Bayer AG stockholders. Any given stockholder will hold the same percentage interest in LANXESS AG as in Bayer AG (a spin-off maintaining proportionality of ownership).

Immediately after the Spin-off takes effect, LANXESS will therefore no longer be affiliated with Bayer AG — a fact that is generally not affected by the mandatory convertible bearer bond issued by LANXESS AG to Bayer AG, which has a face value of €200,000,000, is divided into 2,000 individual bonds with a face value of €100,000 each and matures on 15 September 2007 (hereinafter referred to as the ''Convertible Bond''). This bond does not as such provide Bayer AG with any ownership interest in LANXESS AG. If, however, Bayer AG holds any or all individual bonds on the date the conversion right is exercised, which can be at any time between 20 July 2005 and 20 July 2007, or on the date of mandatory conversion, which will occur at maturity, Bayer AG will once again receive LANXESS AG shares. The extent of the ownership interest thus created will largely depend on the average listing price of the LANXESS shares during the first ten days of stock exchange trading and the average listing price of the LANXESS shares in the 20 trading days prior to exercise of the conversion right or the mandatory conversion date, as the case may be (see the section entitled ''*Business Transactions and Legal Relationships with Related Parties — Business Transactions and Legal Relationships with the Bayer Group — Convertible Bond issued by LANXESS AG to Bayer AG*'').

The Company assumes, based on the notices published to date pursuant to the German Securities Trading Act (*Wertpapierhandelsgesetz* or ''WpHG''), that no stockholder holds 5% or more of the voting rights in Bayer AG. If this situation were to remain unchanged until the Spin-off takes effect, no stockholder would hold an interest in LANXESS AG equal to or exceeding 5% at the time the Spin-off takes effect.

Earnings and Dividend Per Share, Dividend Policy, Distribution of Profits

The stockholders' participation in profits is determined by the proportion of the capital stock they hold. According to the Company's articles of association, the Stockholders' Meeting may subject the profit participation of new shares to different provisions in the event of capital increases.

The adoption of resolutions to distribute dividends on the Company's shares for a given fiscal year is a matter for the Annual Stockholders' Meeting held in the subsequent fiscal year, following a proposal by the Board of Management and the Supervisory Board. A dividend may only be distributed for a given fiscal year on the basis of a balance sheet profit shown in the Company's unconsolidated financial statements. In determining the balance sheet profit available for distribution, the result for the fiscal year, *i.e.*, annual surplus, must be adjusted for profits and losses carried forward from the previous year and for withdrawals from or allocations to reserves. German law requires that certain statutory reserves be created.

According to the Company's articles of association, the Board of Management and the Supervisory Board are authorised, when approving the unconsolidated annual financial statements, to allocate to other retained earnings, in whole or in part, the net income remaining after deduction of the amount to be allocated to statutory reserves plus any loss carry forward. Allocation of an amount greater than one half of the net income for the year to other retained earnings shall not be permissible if, as a result of such allocation, the other retained earnings would exceed one half of the capital stock.

As part of any resolution concerning the allocation of balance sheet profits, the Stockholders' Meeting may allocate additional amounts to retained earnings or carry them forward as profits. According to the Company's articles of association, the Stockholders' Meeting may resolve to distribute the entire or part of the balance sheet profit to the stockholders by way of distribution as dividend in kind.

All 73,034,192 no-par shares to be issued after the Spin-off enters into effect will carry full dividend rights for the fiscal year commencing 1 January 2004 and for all subsequent fiscal years.

Dividends are paid in compliance with the rules of the clearing system of Clearstream Banking AG, Frankfurt am Main. Details about any dividends approved by the Stockholders' Meeting and the paying agents nominated by the Company in such case are published in the electronic version of the Federal Gazette (*Bundesanzeiger*) and in at least one national publication designated by the Frankfurt Stock Exchange for statutory stock market notices.

The following overview shows the earnings and dividends per share of LANXESS AG for fiscal years 2001, 2002 and 2003, although it must be noted that LANXESS AG, as a shelf company, did not conduct its own operations throughout this time period:

	2001	2002	2003
	(in €)	(in €)	(in €)
Earnings per share (according to the German Commercial Code (''*Handelsgesetzbuch*''))	0.000003	–0.000003	–0.000002
Cash dividend per share*	0	0	0

* Based on the issued capital stock admitted to trading after the Spin-off enters into effect, divided into 73,034,192 no-par shares.

The following overview shows the consolidated earnings of the LANXESS Group attributable to each share based on the Combined Financial Statements for fiscal years 2002 and 2003:

	2002	2003
	(in €)	(in €)
Earnings per share (Combined Financial Statements)*	–1.63	–13.65

* Based on the issued capital stock admitted to trading after the Spin-off enters into effect, divided into 73,034,192 no-par shares.

At present, no statements can be made concerning LANXESS AG's future dividend policy. At the appropriate time, the Board of Management and the Supervisory Board of LANXESS AG will establish their dividend policy, taking into account the Company's results of operations, financial condition, business outlook and other factors. The possibility cannot be excluded, however, that LANXESS AG will not pay any dividends for the fiscal years ending 31 December 2004 and 31 December 2005.

Auditor

PwC Deutsche Revision Aktiengesellschaft, Wirtschaftsprüfungsgesellschaft, Hohenzollernring 21-23, 50672 Cologne (hereinafter referred to as ''PwC'') was appointed as the Company's auditor for fiscal year 2004. PWC Deutsche Revision Aktiengesellschaft, Wirtschaftsprüfungsgesellschaft, Friedrich-List-Strasse 20, 45128 Essen has audited the group financial statements (Combined Financial Statements according to IFRS) of the LANXESS Group as of 31 December 2003 and has issued an unqualified audit opinion in connection therewith. The unconsolidated financial statements of the Company as of 31 December 2001, 31 December 2002 and 31 December 2003 were audited by the auditor *Diplom-Volkswirt* Wolfgang Sell, Leopoldsweg 2, 61348 Bad Homburg, in accordance with the German Commercial Code (*Handelsgesetzbuch*), and an unqualified audit opinion was issued in connection with each such audit.

Notices, Paying Agent and Depository Agent

Pursuant to the Company's articles of association, company notices are published in the electronic version of the Federal Gazette (*Bundesanzeiger*). Any notices related to the shares will also be published in the electronic version of the Federal Gazette and in at least one national publication designated by the Frankfurt Stock Exchange for statutory stock market notices. Notices required under German securities laws are published in a national publication designated by the Frankfurt Stock Exchange for statutory stock market notices and in the print version of the Federal Gazette.

Deutsche Bank AG, Frankfurt am Main, serves as the paying and depository agent.

Description of LANXESS AG's Capital Stock

Capital Stock and Shares

LANXESS AG's capital stock currently amounts to €50,000.00, divided into 50,000 ordinary no par value bearer shares (no-par shares), each such no-par share currently representing a €1.00 portion of the capital stock. The capital stock in the amount of €50,000.00 is fully paid in. On 21 December 2004, the Company's Extraordinary Stockholders' Meeting resolved to increase the Company's capital stock in order to implement the Spin-off. The implementation of this capital increase was registered in the Commercial Register (*Handelsregister*) for the Company on 10 January 2005. Once the Spin-off is registered in the Commercial Register for Bayer AG, which is anticipated to occur on 28 January 2005, the Company's capital stock will amount to €73,034,192.00 and will be divided into 73,034,192 no-par shares, each such no-par share representing a €1.00 portion of the capital stock.

Each share carries one vote at the Company's Stockholders' Meeting. There are no restrictions on voting rights. The shares carry full participation rights from 1 January 2004, *i.e.*, for the entire 2004 fiscal year, and for each following fiscal year. Should the Company be dissolved, the assets remaining after the liabilities of the Company have been met will be allocated to the Company's shares on a *pro rata* basis.

All shares of the Company will be issued as no par value bearer shares (no-par shares). All shares of the Company are intended to be represented by one or more permanent global certificates deposited at Clearstream Banking AG, Frankfurt am Main, as depositary bank. Section 5(1) of the articles of association of the Company precludes stockholders from demanding individual certificates for their shares. The issuance of share certificates and all related details are left to the discretion of the Board of Management (section 5(2)).

Development of the Capital Stock

The capital stock has amounted to €50,000.00 since the Company's formation (see ''— *Capital Stock and Shares*'').

The capital increase, which will cause LANXESS AG's current capital stock of €50,000.00 to increase by €72,984,192.00 to €73,034,192.00 and will involve issuing 72,984,192 no-par bearer shares, will be implemented against a contribution in kind consisting of the assets and liabilities to be spun off, *i.e.*, in particular, Bayer AG's equity interest in LANXESS GmbH. The capital increase was approved by the Company's Extraordinary Stockholders' Meeting on 21 December 2004 and was registered in the Commercial Register (*Handelsregister*) for the Company on 10 January 2005. Pursuant to sections 125 sentence 1, 66 and 130(1) UmwG, the registration of the implementation of the capital increase is a prerequisite for the registration of the Spin-off in the Commercial Registers for LANXESS AG and Bayer AG. The capital increase will take effect once the Spin-off is registered in the Commercial Register for Bayer AG, which is anticipated to occur on 28 January 2005.

Authorised Capital

On 15 September 2004, LANXESS AG's Extraordinary Stockholders' Meeting resolved to create authorised capital (*genehmigtes Kapital*). The Board of Management was thereby authorised until 30 August 2009, subject to the Supervisory Board's approval, to increase the Company's capital stock by a total of up to €36,517,096.00 through one or more issuances of new no-par shares against contributions in cash or in kind. The Stockholders' Meeting directed the Board of Management to apply to have the authorised capital entered in the Commercial Register immediately after the capital increase that is to be implemented in connection with the Spin-off has taken effect. An application to register the resolution concerning the authorised capital in the Commercial Register is to be made once the Spin-off has taken effect.

In the event that use is made of the above authorisation to increase the capital stock, stockholders are generally entitled to subscription rights. However, the Board of Management is authorised, subject to the Supervisory Board's approval, to exclude stockholders' subscription rights in certain cases. In particular, the Board of Management is authorised to exclude subscription rights in order to avoid fractional amounts, to grant subscription rights to holders of warrants or convertible bonds issued by the Company or its subsidiaries, and in the event of capital increases against contributions in kind for purposes of acquiring companies, company assets or participating interests in companies. In the case of capital increases against cash contributions, the Board of Management is authorised to exclude subscription rights with respect to no more than 10% of the capital stock existing at the time of the resolution regarding the first use of the authorised capital, provided that the issue price of the new shares is not substantially lower than the market price of the shares already listed. Furthermore, the Board of Management may exclude subscription rights, with the Supervisory Board's approval, in the case of an exercise of conversion rights or upon performance of the Company's conversion obligation in connection with the convertible bond in the nominal amount of €200,000,000.00, to the extent necessary to allow the issuance of new no-par shares to the holders of the convertible bonds. This authorisation enables LANXESS AG, among other things, to service the conversion rights or conversion obligations under the convertible bond (see also ''*Business Transactions and Legal Relationships with Related Parties — Business Transactions and Legal Relationships with the Bayer Group — Convertible Bond issued by LANXESS AG to Bayer AG*'').

Authorisation to Purchase Treasury Shares

By resolution dated 21 December 2004, LANXESS AG's Extraordinary Stockholders' Meeting authorised the Board of Management, from the effective date of the Spin-off until 19 June 2006, to purchase treasury shares amounting to up to 10% of the Company's capital stock that exists after the Spin-off takes effect. This resolution takes effect as soon as the capital increase takes effect that was resolved upon in order to implement the Spin-off. The shares may only be purchased on the stock exchange. In this context, the purchase price paid by the Company (excluding incidental acquisition costs) may not deviate by more than 10% from the stock market price of the shares of the Company on the stock exchange in Frankfurt am Main, as determined during the opening auction in the Xetra trading system (or a similar successor system) on the relevant trading day.

The Board of Management may exercise this authorisation either in full in a single transaction or in parts over the course of several transactions. Shares may be purchased for any lawful purpose or in pursuit of one or more of the purposes set forth in paragraphs (1), (2) or (3) below. In the event that shares are purchased for any of the purposes set forth in (1) or (2) below, stockholders' subscription rights shall be excluded. Specifically, the following arrangements have been agreed:

(1) The Board of Management is authorised to sell the treasury shares purchased on the basis of the authorisation other than via the stock exchange or pursuant to a share offering to all stockholders. This authorisation is conditional upon the sale being made against cash payment and the price not being substantially less, and in any case not more than 5% less, than the stock market price of the Company's shares at the time of the sale. For purposes of the foregoing sentence, the applicable stock market price is the arithmetic mean of the Company's share price on the Frankfurt Stock Exchange over the five trading days prior to the sale, as determined by the closing auctions in the Xetra trading system (or a similar successor system) on those five trading days. This authorisation is limited to a total of 10% of the capital stock. This 10% limit is reduced by the amount of the capital stock represented by shares that are issued while this authorisation is in force pursuant to a capital increase that excludes subscription rights in accordance with section 186(3) sentence 4 of the German Stock Corporation Act (*Aktiengesetz*, hereinafter also referred to as ''AktG''). The 10% limit will also be reduced by the amount of the capital stock represented by shares that are issued to service warrant-linked bonds or convertible bonds, where such bonds are issued while this authorisation is in force to the exclusion of subscription rights based on an analogous application of section 186(3) sentence 4 AktG.

(2) The Board of Management is authorised to transfer treasury shares purchased on the basis of the authorisation to third parties, provided this is done for purposes of

acquiring companies, company assets or participating interests in companies, or for purposes of implementing mergers.

(3) The Board of Management is authorised to redeem the treasury shares purchased on the basis of this authorisation without requiring another stockholders' resolution.

The Board of Management may only exercise the authorisation described in paragraphs (1) and (2) above with the consent of the Supervisory Board. Moreover, the Supervisory Board may decide that the Board of Management must obtain the Supervisory Board's consent regarding measures to be taken on the basis of the resolution adopted at the General Stockholders' Meeting concerning share buy backs.

The authorisation to acquire treasury shares is a general authorisation. LANXESS AG's Board of Management will have to decide whether and on what conditions this authority should be exercised.

General Provisions concerning an Increase of Capital Stock

Pursuant to the German Stock Corporation Act, the capital stock of a stock corporation may be increased by resolution of the Annual Stockholders' Meeting, which must be adopted by a majority of at least three quarters of the capital stock represented at the time the resolution is adopted, unless the corporation's articles of association specify a different majority.

In addition, the Stockholders' Meeting may resolve to issue authorised capital. The issuance of authorised capital requires a resolution to be adopted by a majority of three quarters of the capital stock represented at the time the resolution is adopted, such resolution authorising the Board of Management to issue shares up to a specific amount within a period not exceeding five years. The nominal amount of the authorised capital may not exceed half of the capital stock existing at the time of the authorisation.

Moreover, the Stockholders' Meeting may resolve to create contingent capital for purposes of issuing shares (i) to holders of convertible bonds or other securities convertible into shares of the Company, (ii) as consideration in connection with a merger with another company or (iii) to executives and employees. Such resolution must be adopted by a three-quarters majority of the capital stock represented at the time the resolution is adopted. The nominal value of the contingent capital may not exceed half of the capital stock existing at the time the resolution is adopted and, where the contingent capital is created for purposes of issuing shares to executives and employees, may not exceed 10% of the capital stock available at the time the resolution is adopted.

General Provisions concerning Subscription Rights

According to the German Stock Corporation Act, every stockholder in principle has subscription rights to new shares (including convertible bonds, warrant-linked bonds, profit-sharing rights or participating bonds) that are issued in a capital increase. Subscription rights are freely assignable. Within a specified period prior to expiry of the subscription rights, trading of those subscription rights may take place on German stock exchanges. The Stockholders' Meeting may exclude subscription rights by a resolution passed by a majority of the votes cast and at least three quarters of the capital stock represented at the time the resolution is adopted. An exclusion of subscription rights also requires a report by the Board of Management justifying the exclusion of subscription rights by showing that the Company's interest in excluding the subscription rights outweighs the stockholders' interest in such rights. Without such justification, the exclusion of subscription rights upon the issue of new shares may be permissible if:

- the Company increases its capital stock against cash contributions;
- the amount of the capital increase does not exceed 10% of the existing capital stock; and
- the issue price of the new shares is not substantially below the stock market price of the shares.

Stockholders' Disclosure and Reporting Duties

Upon the admission of the shares to trading pursuant to official listing on the Frankfurt Stock Exchange (see ''*Stock Exchange Listing — Subject Matter of the Stock Exchange Listing, Timetable, Publications*''), LANXESS AG, as a company listed on the stock exchange, becomes subject to the provisions of the German Securities Trading Act (*Wertpapierhandelsgesetz*). The German Securities Trading Act provides that any person whose voting interest in a listed company attains, exceeds or falls below 5%, 10%, 25%, 50% or 75% through acquisition, sale or by other means, must provide written notice to the Company and to the Federal Financial Services Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht*) without undue delay, but no later than within seven calendar days of his or her voting interest attaining, exceeding or falling below the respective threshold. Such notice must also state the stockholder's current voting interest. The Company must publish this notice in an official national publication for statutory stock market notices approved by the stock exchanges in the Federal Republic of Germany without undue delay, but no later than nine calendar days following receipt of the notice. In connection with this requirement, the German Securities Trading Act contains several provisions designed to ensure that shareholdings are attributed to those persons who actually control the voting rights associated with the shares. For example, shares belonging to a company controlled by another are attributable to the controlling company, as are shares held by the first company for the controlling company's account or by a company controlled by the first company. If the above-mentioned notice is not provided, the stockholder is precluded from exercising the rights (including voting and dividend rights) attached to the shares for so long as such default continues. In addition, a fine may be imposed for the failure to comply with the notice requirements.

Equity Interests

The table below lists those of LANXESS AG's subsidiaries that have a book value of at least 10% of the LANXESS Group's stockholders' equity and/or which contribute at least 2% of the consolidated annual sales of the LANXESS Group or which are material for other reasons. The table also sets forth important information relating to these subsidiaries. As the annual financial statements for fiscal year 2003 were substantially affected by impairment charges, the percentage of Group net income (loss) generated by a subsidiary in fiscal year 2003 is not a meaningful measure of the subsidiary's materiality to the LANXESS Group. Therefore, for purposes of assessing the materiality of subsidiaries, the primary indicators were the subsidiary's book value as a percentage of the Group's stockholders' equity and the percentage of the LANXESS Group's external net sales generated by the subsidiary. In addition, companies were taken into account if they were regarded as material for other reasons. The classification was made on the basis of the Combined Financial Statements having regard to the respective legal structures or, with regard to subsidiaries that were not legally formed until 2004, having regard to the allocation of business activities under the relevant contractual agreements.

The Company will own, directly or indirectly, 100% of the capital stock of these subsidiaries once the Spin-off has been implemented. The book value of these holdings is taken from the financial statements of the LANXESS Group company that owns the equity interest (in most cases, LANXESS Deutschland GmbH). The earnings for the respective periods are taken from the financial statements and/or accounting systems prepared or in place in accordance with applicable national law.

Name, Registered Office	Area of Operations and Segment	Subscribed capital as of 30 Sept. 04	Book value of interests as of 30 Sept. 04 pursuant to IFRS	Reserves as of 30 Sept. 04 pursuant to IFRS	Company's receivables/ (liabilities) from/to subsidiaries as of 30 Sept. 04	Net income/ (loss) for the most recent fiscal year	Income from interests in fiscal year 2003
				(in thousands)			
LANXESS Deutschland GmbH, Leverkusen	Manufacturing and distribution All segments	€20,000	—[1]	€1,796,013	€0	—[2]	—[2]
LANXESS Corporation, Pittsburgh/Pennsylvania (U.S.A.)	Manufacturing and distribution All segments	U.S.$351,473	€119,841	$8,123	€197,762	—[2]	—[2]
LANXESS Elastomères S.A.S., Lillebonne (France)	Manufacturing and distribution Performance Rubber	€4,000	€0	€9,426	€0	€(16,206)	€0
LANXESS HOLDING HISPANIA, S. L., Barcelona (Spain)	Holding company All segments	€1,322	€18,871	€69,812	€0	—[2]	—[2]
LANXESS Inc., Sarnia, Ontario (Canada)	Manufacturing and distribution Performance Rubber	CAN$61,000	€37,074	CAN$74,770	€0	—[2]	—[2]
LANXESS International SA, Fribourg (Switzerland)	Distribution All segments	€640	€229,933	€41,535	€0	—[2]	—[2]
LANXESS N.V., Antwerp (Belgium)	Manufacturing and distribution Engineering Plastics and Performance Rubber	€38,863	€179,963	€99,133	€0	—[2]	—[2]
LANXESS Rubber N.V., Zwijndrecht (Belgium)	Manufacturing and distribution Performance Rubber	€3,350	€276,135	€79,862	€0	€24,339	€0
RheinChemie Rheinau GmbH, Mannheim	Manufacturing and distribution Performance Chemicals	€20,452	€26,716	€34,497	€0	€10,238	€0

1) LANXESS Deutschland GmbH will become a subsidiary of LANXESS AG when the Spin-off takes effect because the book value of the equity interest in LANXESS Deutschland GmbH will not be part of LANXESS AG's assets until then. The book value of the equity interest will be calculated based on the increase in the Company's capital stock associated with the contribution in kind.

2) The company was not legally established until fiscal year 2004, *i.e.*, in fiscal year 2003 it functioned merely as a shelf company with no operating business and its earnings were not connected with its current corporate purpose.

Information on the Governance Bodies of LANXESS Aktiengesellschaft

The governance bodies of the Company are the Board of Management (*Vorstand*), the Supervisory Board (*Aufsichtsrat*) and the Stockholders' Meeting (*Hauptversammlung*). The powers of these governance bodies are governed by the German Stock Corporation Act (*Akiengesetz*), the articles of association (hereinafter referred to as the ''Articles'') and the rules of procedure of the Board of Management and the Supervisory Board, both of which have yet to be adopted.

The Articles of the Company currently in effect, largely restated by the Extraordinary Stockholders' Meeting held on 1 December 2004, were amended by a resolution adopted at the Stockholders' Meeting held on 29 December 2004. The amendments will become effective only after the Spin-off has taken effect and the so-called status proceedings (*Statusverfahren*) with respect to the composition of the Supervisory Board, which are to be carried out subsequently, have been concluded. The amendments were essentially made in view of the Company's future stock exchange listing and the 16 member Supervisory Board to be formed in future in accordance with the German Co-Determination Act (*Mitbestimmungsgesetz*) of 1976. The following discussion refers to the version of the Articles in effect after the Spin-off has taken effect.

The Board of Management manages the business affairs of the Company in accordance with applicable law, the Company's Articles and the Board of Management's rules of procedure, which have yet to be issued. It represents the Company as against third parties.

The Board of Management must ensure that reasonable risk management and risk controlling are set up within the LANXESS Group, such that any developments that might jeopardise the continued existence of the Company are recognised at an early stage. Moreover, the Board of Management is obliged to report to the Supervisory Board on a regular basis — no less than quarterly — concerning the course of the business, in particular, the sales and the condition of the Company and its subsidiaries. At least once annually, the Board of Management must report on the planned business policy and other fundamental issues concerning the Company's and the Group's corporate planning. At the beginning of each fiscal year, the Board of Management must submit the annual corporate plan. In addition, the Board of Management must report to the Supervisory Board on transactions that might be of material importance to the Company's profitability or liquidity within a timeframe that enables the Supervisory Board to provide its opinion before the transactions are effected. In important cases, the Board of Management is obliged to report to the Chairman of the Supervisory Board. A transaction involving an affiliated company which could have a material effect on the Company's condition and of which the Board of Management has become aware is deemed to be an important case for these purposes. Pursuant to German law, individuals are prohibited from serving on a stock corporation's Board of Management and Supervisory Board at the same time.

The Supervisory Board appoints the members of the Board of Management and is entitled to dismiss them for good cause. The Supervisory Board advises the Board of Management with respect to the management of the Company's operations and supervises its management. Pursuant to the German Stock Corporation Act, the Supervisory Board is not permitted to manage the Company. Pursuant to the rules of procedure for the Supervisory Board, which are expected for the period following entry into effect of the Spin-off but which have not yet been adopted, the Board of Management must obtain the Supervisory Board's approval for specific transactions and measures, usually before the relevant transaction or measure is effected. The Supervisory Board's approval is generally not required for transactions conducted between the Company and its affiliated companies. The Board of Management must obtain the Supervisory Board's approval if it takes part in certain measures implemented by a company dependent on LANXESS AG.

The members of the Board of Management and Supervisory Board owe fiduciary duties and duties of care to the Company. In this respect, the members of these governance bodies must protect a broad range of interests, in particular, those of the Company, its stockholders, its employees and its creditors. Furthermore, the Board of Management must take into account the stockholders' rights to non-discrimination (*Gleichbehandlung*) and equal disclosure. Should the members of the Board of Management or the Supervisory Board breach their duties, they will be jointly and severally liable to the Company for damages. Insurance protection is in place for members of the Board of Management and the current Supervisory Board under a D&O insurance policy of the Bayer Group. For the period after the Spin-off takes effect, insurance protection will be in place under a new D&O insurance policy (see ''*Information Concerning the Business of LANXESS — Insurance*'').

A stockholder generally has no possibility of proceeding directly against members of the Board of Management or the Supervisory Board if the stockholder believes that the respective members have breached their duties towards the Company. Only the Company is entitled to demand damages from members of the Board of Management or the Supervisory Board. The Company may waive or settle compensation claims only after a period of three years has passed since the claim arose, and may do so only with the approval of the stockholders at the Stockholders' Meeting by a simple majority of votes cast and if no minority of stockholders, whose combined shares equal or exceed 10% of the capital stock, lodge an objection on the record.

Pursuant to German law, individual stockholders (as is the case for any other person) are not permitted to exert influence on the Company for purposes of causing a member of the Board of Management or the Supervisory Board to act to the detriment of the Company. Stockholders with a controlling influence may not use such influence to cause the Company to act against its own interests, unless the resultant detriment is compensated for. Any person who exercises his influence to cause a member of the Board of Management or Supervisory Board, a commercial attorney-in-fact (*Prokurist*) or an authorised representative to act to the detriment of the Company or its stockholders must compensate the Company and its stockholders for any resultant damage. In addition, the members of the Board of Management and of the Supervisory Board are jointly and severally liable if they have acted in breach of their duties.

Board of Management

Subject to the requirement in the Company's Articles that the Board of Management have at least two members, the number of members of the Board of Management is determined by the Supervisory Board. At present, the Company's Board of Management has four members. The Supervisory Board may appoint one member of the Board of Management as its Chairman and another member of the Board of Management as the Deputy Chairman. Holders of proxies for the members of the Board of Management may be appointed.

Members of the Board of Management are appointed by the Supervisory Board for a maximum term of office of five years. Reappointment or extension of the term of office, in each case for a maximum period of five years, is permissible. The current members of the Board of Management were appointed by the Supervisory Board of LANXESS AG on 2 September 2004 for a three-year term. On 6 December 2004, the appointments of 2 September 2004 were rescinded and the members of the Company's Board of Management were newly appointed on 7 December 2004 by virtue of a Supervisory Board resolution for a three-year term commencing when the Spin-off takes effect, but in any case expiring on 31 January 2008. The Supervisory Board may revoke, for good cause, the appointment of a member of the Board of Management prior to the expiry of his/her term of office, for example, in the event of a gross violation of duty or if the Stockholders' Meeting withdraws its confidence in the relevant member of the Board of Management.

Pursuant to the Company's Articles, the Board of Management may issue its own rules of procedure to the extent they are not issued by the Supervisory Board. It is anticipated that the Supervisory Board will adopt rules of procedure for the Board of Management prior to the Spin-off taking effect. Pursuant to these rules of procedure, resolutions of the Board of Management will be adopted by a simple majority of its members, unless applicable law or the Articles mandate other majorities. In the event a vote is tied, the Chairman will have the deciding vote.

The Company is represented by two Board of Management members acting jointly, or one Board of Management member acting jointly with a commercial attorney in fact.

The following individuals are currently members of the Company's Board of Management:

Dr. Axel Claus Heitmann (Chairman of the Board of Management) (45 years of age): After studying chemistry at the University of Hamburg and the University of Southampton (UK), Dr. Axel Claus Heitmann was awarded a science doctorate in 1988. In 1989, he joined Bayer AG. As part of a trainee programme, he held various positions between 1989 and 1991 in the Central Research Division and in the Applications Development and Manufacturing sections of the Rubber Business Group. After two years of management, he moved to Bayer UK Ltd., Newbury, Great Britain, as head of the Rubber Business Group's Bromsgrove site. In 1996, Dr. Axel Claus Heitmann became head of Manufacturing and Technology of Polymer Latex, which was the joint venture that had been newly-formed at that time by Bayer AG and Degussa AG. From March 1999 until 31 January 2002, he managed the Bayer subsidiary Wolff Walsrode AG. He then became the general manager of the Rubber Business Group of Bayer AG before being appointed to the Executive Committee of Bayer MaterialScience AG on 1 January 2002. Dr. Axel Claus Heitmann has been the Chairman of the Company's Board of Management since 2 September 2004.

Dr. Ulrich Koemm (member of the Board of Management) (54 years of age): After studying at the Technical University of Munich and being awarded a science doctorate, Dr. Ulrich Koemm initially worked as a scientist at the University of Kaiserslautern before being employed by Bayer AG in 1980 as a laboratory manager in Inorganic Chemicals research (AC). From 1983 until 1986, he was a research team leader and then — in AC Manufacturing — manager of the chrome plant and head of the fluorine department. In 1988, Dr. Ulrich Koemm joined Bayer S.A., Sao Paulo, Brazil, where he was responsible as the local general manager of the AC, LS and Pigments and Ceramics (PK) Business Groups. After returning to Bayerwerk Leverkusen, he was made head of manufacturing in the PK Business Group in 1992. In 1994, he was appointed head of manufacturing in the Inorganics Business Group (AI) and, in 1997, he was appointed head of the Inorganic Pigments Business Unit. In 1998, he became provisional head of the Inorganics Business Group. From April 1999 until mid 2002, he was general manager of the Coatings and Colorants Business Group(LS) of Bayer AG. Since 30 September 2003, Dr. Ulrich Koemm has been Chairman of the Board of Management of Bayer Chemicals AG, Leverkusen. As of the date the Spin-off takes effect, Dr. Ulrich Koemm will resign his office at Bayer Chemicals AG by agreement. Dr. Ulrich Koemm has been a member of the Company's Board of Management since 2 September 2004.

Dr. Martin Wienkenhöver (member of the Board of Management and Personnel Director) (48 years of age): Dr. Martin Wienkenhöver studied chemistry at the Westfälische Wilhelms University in Münster. After being awarded his science doctorate, he commenced his career in 1985 at Bayer AG as head of a development and formulating laboratory in the then-existing Dyes and Pigments Business Group. One year later he became a laboratory manager in dyes and pigments research. In 1998, Dr. Martin Wienkenhöver transferred to the Mobay Corporation, Pittsburgh, U.S.A., which was a U.S. Bayer subsidiary at that time, where he initially worked as group leader of research and development in the Dyes and Pigments Division and, from 1992, as the head of research and development in the Organic Products Division. In 1993, he returned to headquarters in Leverkusen where he initially headed dyes and pigments development and later worked as a key account manager in marketing. Thereafter, he was responsible for the Reactive Dyes Business Unit at DyStar Textilfarben GmbH, which was then a 50:50 joint venture between Bayer and Hoechst. In April 1999, he became general manager of the Basic and Fine Chemicals Business Group of Bayer AG. Since 30 September 2003, Dr. Martin Wienkenhöver has been a member of the Board of Management of Bayer Chemicals AG, Leverkusen. As of the date the Spin-off takes effect, Dr. Martin Wienkenhöver will resign his office at Bayer Chemicals AG by agreement. Dr. Martin Wienkenhöver has been a member of the Company's Board of Management since 2 September 2004.

Matthias Zachert (member of the Board of Management and Director of Finance (37 years of age): After being trained as an commercial assistant at former Mercedes Benz AG in Stuttgart, Matthias Zachert completed his studies in business administration from 1990 to 1995, specialising in finance, and spent time abroad in the United States and France. He then joined the young management programme of former Hoechst AG, where he was first appointed in 1996 as head of the IPO project for the carve-out of the pharmaceuticals business Hoechst Marion Russel (HMR). After holding other management positions at HMR, he was responsible in 1999 for integrating the finance departments of the pharmaceuticals companies HMR and Rhone-Poulenc

Rorer, which were consolidated into Aventis Pharma as a result of the merger between Hoechst and Rhone Poulenc. In January 2000, Matthias Zachert was appointed chief financial officer of the international region of this company, having its registered office in Paris. In summer 2002, he transferred to Kamps AG in Dusseldorf, as director of finance, where he was involved in that company's restructuring. Mr Zachert has been a member of the Company's Board of Management since 2 September 2004.

The members of the Board of Management may be contacted at the Company's business address.

The contracts with the members of the Board of Management provide for a three-year term commencing on the date the Spin-off takes effect.

In fiscal year 2004, the members of the Board of Management did not receive any remuneration from the Company. The remuneration paid to all current members of the Company's Board of Management by the companies of the Bayer Group totalled approximately €1,580,500. The Bayer Group has established pension provisions totalling €4,954,618 for members of the Board of Management.

After the Spin-off takes effect, the remuneration of the members of the Board of Management will be based on a compensation system that provides for a base salary and supplementary annual variable remuneration in the same amount. The total base salary of the members of the Company's Management Board will amount to €1,869,000 per year on the basis of the current agreements. The variable remuneration will be linked to the attainment of specified performance targets.

No sanctions for violation of domestic or foreign criminal or securities laws have been imposed on any member of the Board of Management in the past five years.

Dr. Ulrich Koemm and Dr. Martin Wienkenhöver currently hold 1,700 and 3,400 Bayer shares, respectively. Immediately after the Spin-off takes effect, they will hold 170 and 340 shares in LANXESS AG, respectively, in accordance with the allotment ratio. Dr. Martin Wienkenhöver currently also holds an option to acquire a small number of additional Bayer shares, which may be exercised from the beginning of 2005. The remaining members of the Board of Management currently do not hold any Bayer AG shares and, for this reason, will not hold any shares in the Company immediately after the Spin-off takes effect.

The Company currently has no loans outstanding to nor has it undertaken any guarantees or sureties on behalf of members of the Board of Management. During the current or prior fiscal years, the members of the Board of Management have not been and are not involved in any transactions outside the scope of business of the Company or in any transactions of an unusual nature, as regards either their form or substance, nor have they in earlier fiscal years been involved in any such unusual transactions that have not yet been fully concluded.

Supervisory Board

The Supervisory Board of LANXESS currently has three members who were elected by the hitherto sole stockholder, Bayer AG. Since LANXESS AG currently does not have any employees, the statutory provisions on co-determination relating to employee representation on the Supervisory Board do not yet apply, and no employee representatives are currently members of the Supervisory Board.

The current members of the Supervisory Board are Klaus Kühn, Cologne, Johannes Dietsch, Wermelskirchen, and Dr. Roland Hartwig, Odenthal. All Supervisory Board members hold various offices on supervisory bodies of companies affiliated with Bayer AG. Beyond this, they do not hold any other Supervisory Board offices. The current members of the Supervisory Board have, as agreed with the Company, resigned their office on expiry of the date on which the Spin-off takes effect, and no sooner, however, than upon expiry of 28 January 2005. On 29 December 2004, the hitherto sole stockholder, Bayer AG, appointed the following three persons as new Supervisory Board members, with effect from the day following the day on which the Spin-off takes effect, but no sooner than with effect from 29 January 2005: Dr. Rolf Stomberg, Hamburg, Dr. Friedrich Janssen, Essen and Mr Rainer Laufs, Kronberg.

The names and principal occupations of the members of the Supervisory Board of LANXESS Aktiengesellschaft who will serve on the Supervisory Board when the Spin-off takes effect are:

Name	Position	Additional Supervisory Board Appointments and Appointments at Comparable German and Foreign Supervisory Bodies of Business Enterprises
Dr. Rolf Stomberg	Chairman of the Board of Directors of Management Consulting Group plc, London	Member of the Supervisory Board of Deutsche BP AG, Hamburg Member of the Supervisory Board of Biesterfeld AG, Hamburg Member of the Board of Directors of Reed Elsevier plc, London, Great Britain Member of the Board of Directors of Smith & Nephew plc, London, Great Britain Member of the Supervisory Board of Reed Elsevier NV, Amsterdam, the Netherlands Member of the Supervisory Board of TPG Post Group, Amsterdam, the Netherlands Member of the Supervisory Board of Scania AB, Södertälje, Sweden
Dr. Friedrich Janssen	Member of the Board of Management of E.ON Ruhrgas AG, Essen	Member of the Supervisory Board of Gerling Versicherungs-Beteiligungs-AG, Cologne Member of the Supervisory Board of HDI Rechtsschutz Versicherungs-AG, Hanover Member of the Supervisory Board of STEAG AG, Essen Various appointments to the Supervisory Boards of companies associated with E.ON Ruhrgas AG, Essen Member of the Advisory Board of HDI Haftpflichtverband des Deutschen Industrie Versicherungsvereins auf Gegenseitigkeit, Hanover
Rainer Laufs	Former Chairman of the Board of Management of Deutsche Shell AG, Hamburg, currently an independent consultant	Member of the Supervisory Board of WCM Beteiligungs- und Grundbesitz AG, Frankfurt am Main Member of the Supervisory Board of Klöckner Werke AG, Duisburg

The appointment was made for the period ending upon the conclusion of the Stockholders' Meeting at which the actions of the Supervisory Board for the fiscal year ending 31 December 2004 are formally ratified.

Once the Spin-off takes effect, the provisions of the German Co-Determination Act of 1976 (*Mitbestimmungsgesetz* 1976) will apply with respect to the composition of the Company's Supervisory Board. The Company will employ its own employees. Furthermore, employees working at LANXESS Deutschland GmbH will be attributed to the Company. In the future, the Supervisory Board will consist of a total of 16 Supervisory Board members, eight of whom will be stockholder representatives, and eight of whom will be employee representatives. The stockholder representatives will be appointed by the stockholders at the Stockholders' Meeting in accordance with the provisions of the German Stock Corporation Act. The future election of the employee representatives will be constituted in accordance with the provisions of the German Co-Determination Act of 1976.

Because the statutory provisions hitherto applicable with respect to the composition of the Supervisory Board will change once the Spin-off takes effect, the Board of Management is obliged to conduct so-called ''status proceedings'' (*Statusverfahren*) pursuant to sections 97 *et seq.* of the German Stock Corporation Act immediately after the Spin-off takes effect. During the status proceedings, the Company's Board of Management will announce the new statutory provisions governing composition of the Supervisory Board. Provided there is no objection to the court having jurisdiction over the Company within one month of this announcement, the Supervisory Board of LANXESS AG will be composed in accordance with such provisions.

The future Supervisory Board members that have already been elected will remain in office even after the status proceedings. Their term of office will expire upon conclusion of the first Stockholders' Meeting of the Company called after the one-month period ends, but no later than six months following expiry of the period. A judicial appointment in accordance with the rules of the German Stock Corporation Act of the five stockholder representatives on the Supervisory Board not yet appointed is planned following expiry of the one-month period under the status proceedings. The same is planned with respect to all eight employee representatives on the Supervisory Board. Should the Court not establish the term of office of the court-appointed Supervisory Board members, the stockholder representatives' term of office will end upon election of the stockholder representatives by the Company's Stockholders' Meeting, and the term of office of the employee representatives will end upon completion of the election of the employee representatives in accordance with the provisions of the German Co-Determination Act of 1976. The new election of all stockholder representatives on the Supervisory Board is anticipated to occur at the Annual Stockholders' Meeting of the Company in 2005.

With a view to the expected status proceedings, the Company's Stockholders' Meeting already resolved on 29 December 2004, among other things, that the provisions of the Articles concerning the Company's Supervisory Board be amended in light of the different legal provisions governing composition of the Supervisory Board. The Board of Management was instructed to apply for registration of the amendments to the Articles in the Commercial Register after the Spin-off has taken effect and the one-month period under the status proceedings has expired without any objections.

Unless indicated otherwise below, the following description relates to the Supervisory Board and the Company's Articles after the adopted amendments to the Articles have been registered and the remaining stockholder representatives and all employee representatives have been judicially appointed.

The members of the Supervisory Board may be contacted at the Company's business address.

Unless the Stockholders' Meeting provides for a shorter term at the time of the election, the Supervisory Board members and, where applicable, their substitute members, will be elected in accordance with the Company's Articles and section 102 of the German Stock Corporation Act for the term ending on conclusion of the Stockholders' Meeting at which the actions of the Supervisory Board for the fourth fiscal year following commencement of the term (not counting the fiscal year in which the term commenced) are formally ratified.

If no elected substitute member is available, the election of a successor to a Supervisory Board member who leaves office before the expiry of his term of office will be valid for the remainder of the term of office of the vacating member, unless the Stockholders' Meeting stipulates a shorter term for the successor. At the time a Supervisory Board member is elected, a substitute may be appointed who will join the Supervisory Board if the Supervisory Board member leaves the board prematurely without any successor having been appointed. The term of office of any stockholder representative on the Supervisory Board who joins the Supervisory Board in this manner will expire no later than upon the expiry of the term of office of the vacating Supervisory Board member.

According to the Articles, any member of the Supervisory Board may resign his office without cause upon written two weeks' notice sent to the Chairman of the Supervisory Board or to the Board of Management. Dismissal of a stockholder representative on the Supervisory Board requires a majority of no less than three quarters of the votes cast. According to the rules of procedure of the Supervisory Board, which have yet to be adopted, the term of office of a Supervisory Board member shall in any event expire upon the conclusion of the Stockholders' Meeting following the 72nd birthday of the relevant Supervisory Board member.

The Supervisory Board will elect from its midst a Chairman and a Deputy Chairman in accordance with section 27 paragraphs 1 and 2 of the German Co-Determination Act of 1976. Unless a shorter term of office is stipulated at the time of their election, the term of office of the Chairman and the Deputy Chairman shall be equivalent to their term of office as member of the Supervisory Board. The election will be held following the Stockholders' Meeting at which the stockholder representatives on the Supervisory Board to be elected by the Stockholders' Meeting have been appointed; there is no special notice requirement for such meeting. Should the Chairman or his Deputy prematurely leave office, the Supervisory Board shall elect a successor at its next meeting.

The Supervisory Board Chairman is responsible for calling and chairing Supervisory Board meetings. The Supervisory Board has a quorum if no less than half of the members of which it is to be comprised in total participate in adopting the relevant resolutions. A member will also be deemed to have participated in the adoption of a resolution if he or she abstains during the vote.

The Supervisory Board can adopt resolutions by simple majority of the votes cast, unless applicable law prescribes other majorities. Should a vote on the Supervisory Board result in a tie, then the Chairman of the Supervisory Board will have two votes in a new election on the same issue that is the subject of the resolution and such vote again results in a tie. The Deputy Chairman of the Supervisory Board does not have a second vote.

According to the Company's Articles, the Supervisory Board issues its own rules of procedure. There are plans for the hitherto-serving Supervisory Board to issue its own rules of procedure before the Spin-off takes effect, which rules are to comply with the provisions of the German Corporate Governance Code.

According to the Articles of the Company currently in effect, the members of the Supervisory Board each receive fixed annual remuneration in the amount of €5,000, in addition to the reimbursement of their expenses. According to the Articles that will be in effect for the period after the Spin-off takes effect, the members of the Supervisory Board will be reimbursed for their expenses and will also receive fixed annual remuneration of €30,000. The remuneration for the Chairman will be three times this amount, and that of the Deputy Chairman one and one half times that amount. Any Supervisory Board members who are members of a committee will additionally receive one quarter of the mentioned remuneration, while Supervisory Board members who chair a committee will further receive an additional quarter of such remuneration. In any event, however, the maximum amount a given member of the Supervisory Board is to receive is three times the annual remuneration of €30,000. The Company will reimburse the Supervisory Board members for any expenses incurred in exercising the duties of their office, including any value added tax imposed on remuneration and reimbursement of expenses.

In fiscal year 2004, the current Supervisory Board members did not receive any separate remuneration for their work.

No sanctions for violation of domestic or foreign criminal or securities laws have been imposed on any of the current or the already elected three future members of the Supervisory Board in the past five years.

The future Supervisory Board member Dr. Stomberg currently holds 2,000 Bayer shares. Immediately after the Spin-off takes effect, he will hold 200 shares in LANXESS AG in accordance with the allotment ratio.

The Company currently has no loans outstanding to nor has it undertaken any guarantees or sureties on behalf of the current and the already elected future Supervisory Board members. During the current or prior fiscal years, the current and already elected future members of the Supervisory Board have not been and are not involved in any transactions outside the scope of business of the Company or in any transactions of an unusual nature, as regards either their form or substance, nor have they in earlier fiscal years been involved in any such unusual transactions that have not yet been fully concluded.

Stockholders' Meeting

The Stockholders' Meeting is held at the Company's registered office or in a German municipality having more than 100,000 inhabitants. Each no-par share is entitled to one vote at the Stockholders' Meeting.

According to corporate law, resolutions of fundamental significance require, in addition to a majority of votes cast, a majority of no less than three quarters of the capital stock represented at the adoption of the relevant resolution. Resolutions of fundamental significance include specifically:

- capital increases where subscription rights are excluded;
- capital reductions;
- the creation of authorised or conditional capital;
- split-up or a spin-off as well as the transfer of the Company's entire assets;

- the conclusion of inter-company agreements (in particular, control and profit and loss transfer agreements);
- a change in the Company's legal structure; and
- dissolution of the Company.

The Stockholders' Meeting may be called by the Board of Management, the Supervisory Board or by stockholders whose shares together constitute 5% of the capital stock. If it is in the Company's best interest, the Supervisory Board must call a Stockholders' Meeting. The Annual Stockholders' Meeting will be held within the first eight months of each fiscal year. According to the Company's Articles in effect for the period after the Spin-off takes effect, those stockholders who deposit their shares during business hours no later than the seventh day prior to the date of the Stockholders' Meeting with the Company, a German notary, a central depository for securities or another depositary specified in the notice of the Stockholders' Meeting and who leave them there until the conclusion of the Stockholders' Meeting are entitled to participate in the Stockholders' Meeting and to exercise their voting rights. The shares shall also be deemed to have been deposited with one of the above mentioned depositaries if, with the consent of such depositary, the shares are held for their account in a blocked bank account until the conclusion of the Stockholders' Meeting.

Neither German law nor the Company's Articles restrict the right of foreign stockholders or stockholders who are not residents of Germany to hold shares or to exercise the voting rights attached thereto.

Business Transactions and Legal Relationships with Related Parties

Business Transactions and Legal Relationships with the Bayer Group

Spin-off and Acquisition Agreement between LANXESS AG and Bayer AG

On 22 September 2004, Bayer AG and LANXESS AG entered into a notarised spin-off and acquisition agreement. This agreement sets forth the assets and liabilities to be spun off and governs details of the transfer of certain of Bayer AG's assets and liabilities (in particular, the entire equity interest in LANXESS GmbH) to LANXESS AG and of the shares in LANXESS AG issued to Bayer AG stockholders in return for the transfer. The Stockholders' Meetings of Bayer AG and LANXESS AG on 17 November 2004 and 21 December 2004, respectively, approved the spin-off and acquisition agreement. The Spin-off will become effective once it is registered in the Commercial Register (*Handelsregister*) for Bayer AG at the Local Court of Cologne (*Amtsgericht Köln*). The Board of Management of LANXESS AG anticipates that the registration will occur on 28 January 2005 (for more details concerning the Spin-off and the actions taken in preparation therefor, see ''*Further Details and Explanation of the LANXESS Spin-off*'').

Master Agreement between LANXESS AG and Bayer AG

On 22 September 2004, at the same time, Bayer AG and LANXESS AG entered into a master agreement which forms an integral part of the spin-off and acquisition agreement. Pursuant to the Master Agreement, both parties intend, among other things, to ensure the combination of the chemicals and polymers activities in LANXESS GmbH and its subsidiaries and that certain minimum standards will be observed in such combination, to conclusively determine the apportionment of liability as between LANXESS and the Bayer Group in the areas of environment, antitrust and product liability, and establish certain reciprocal rules of conduct and duties of cooperation for the period following the Spin-off.

Combination of the major parts of the chemicals and parts of the polymers activities

The combination of the chemicals and polymers activities in LANXESS GmbH and its subsidiaries was implemented by means of a number of individual measures both in Germany and abroad (see ''*Further Details and Explanation of the LANXESS Spin-off*''). Thus, in particular, Bayer Chemicals AG and Bayer MaterialScience AG were spun off to LANXESS GmbH, and the foreign business was transferred to subsidiaries of LANXESS GmbH using legally different methods. The catch-all provisions of the Master Agreement were intended to ensure, above all, that the LANXESS Group would in fact be established by means of the individual measures taken and also that certain principles and minimum standards would be observed. The objective is to ensure the worldwide ability to function of LANXESS.

Apportionment of liability as between LANXESS and the Bayer Group

The master agreement also contains general provisions governing the apportionment of liability as between LANXESS and Bayer Group. Pursuant to these provisions, LANXESS AG and its affiliated companies (as defined in section 15 of the German Stock Corporation Act (''AktG'')) are liable *vis-à-vis* the Bayer Group only for those liabilities existing at the time the Spin-off takes effect and that were allocated to them in the context of the measures taken to combine the chemicals and polymers activities. The equivalent applies to Bayer AG and its affiliated companies (section 15 AktG). Furthermore, LANXESS AG and Bayer AG have entered into additional agreements concerning the apportionment of liability as between themselves in other areas (for example, with respect to the preparation of the Combined Financial Statements).

With regard to liability for environmental contamination and antitrust violations as well as product liability, the master agreement provides the following special rules regarding the apportionment of liability as between the contracting parties:

Environmental contamination

With respect to liability for environmental contamination of real property which was caused or arose before 1 July 2004, the master agreement generally provides for liability based on the condition of the properties used by the relevant contracting party or its affiliated companies (section 15 AktG) on or before 1 July 2004 (*Zustandshaftung*). To this extent, that contracting party is generally required fully to indemnify the other contracting party and its affiliated companies (section 15 AktG) for any liability arising out of public and private law. The master agreement also contains individual elements of the principle of causation-based liability (*Verursachungshaftung*). If, for example, a party can provide evidence that the environmental contamination was caused by property used by the other party on 1 July 2004, the former party is exempt from liability as between the parties. As regards particular properties, the parties provided for a different apportionment of liability as between themselves. LANXESS will also be liable for environmental contamination in connection with certain sold companies, operations and plants in accordance with the relevant purchase and acquisition agreements.

The master agreement caps LANXESS' liability for environmental contamination of real property caused prior to 1 July 2004 at €350 million. However, in simplified terms, this liability cap applies only to remedial action ordered, agreed upon or actually carried out by 31 December 2009. Otherwise, LANXESS AG and its affiliated companies (section 15 AktG) bear unlimited liability for environmental contamination.

Antitrust violations

Pursuant to the master agreement, LANXESS is generally liable *vis-à-vis* the Bayer Group for all obligations and liabilities arising from antitrust violations which are allocable to the business activities of LANXESS. Conversely, the Bayer Group will be liable *vis-à-vis* LANXESS for any obligations and liabilities arising from antitrust violations which are allocable to its business activities. Pursuant to the master agreement, the liable party must reimburse the other party for any expenses incurred as necessary to discharge the antitrust liabilities.

The master agreement contains special provisions governing antitrust proceedings and civil litigation in connection with products of the former Bayer AG Rubber business unit that are now allocated to the LANXESS Group. If, prior to 1 July 2004, regulatory proceedings had at least been commenced or if a company had taken steps before an antitrust authority with a view to commencing proceedings, LANXESS will bear 30%, and the Bayer Group 70%, of any liability resulting therefrom. The LANXESS Group's liability in such proceedings is generally limited to a total of €100 million. In addition, any tax disadvantages arising thereby due to limited deductibility for tax purposes are to be reimbursed. Reimbursement payments will be limited to €50 million per calendar year. Costs of external assistance in these antitrust proceedings are likewise shared between the parties on a 30:70 basis but will not count towards the liability cap.

Product liability

The master agreement also contains provisions governing the apportionment of liability as between LANXESS and the Bayer Group in respect of product liability claims brought by third parties. Pursuant to these provisions, LANXESS is liable *vis-à-vis* the Bayer Group for any and all product liability claims arising from or connected with defective products which those of its businesses active as of 1 July 2004 introduced into the market prior to the taking effect of the Spin-off. The Bayer Group is liable for any product liability claims relating to other products which were introduced into the market prior to the taking effect of the Spin-off. The master agreement provides special provisions in respect of apportionment of liability for products of certain sold companies, operations, factories and plants.

Scope of application

The geographical scope of the master agreement extends directly to all worldwide business activities of LANXESS but generally not to the business activities in the United States. However, antitrust liability and environmental contamination allocable to LANXESS operations located in the United States will count towards the relevant liability caps. As regards the operations of

LANXESS located in the United States, agreements for the formation of LANXESS, particularly with respect to the transfer of the LANXESS business activities, were entered into with companies of the Bayer Group. To the extent the terms of these agreements are not entirely congruent with all the terms of the master agreement, Bayer AG and LANXESS AG have committed themselves, in the case of any material deviations, to ensure that the agreements in the United States are modified to reflect the fundamental provisions of the master agreement. The parties are currently making the relevant modifications.

Convertible Bond issued by LANXESS AG to Bayer AG

On the basis of the resolution adopted by its Stockholders' Meeting on 15 September 2004, LANXESS AG issued to Bayer AG a convertible bearer bond with a nominal value of €200 million, divided into 2,000 individual bonds each with a nominal value of €100,000 and a maturity date of 15 September 2007 (hereinafter referred to as the ''Convertible Bond'').

Under the terms of the Convertible Bond, LANXESS AG is obliged to pay 6% annual interest. However, since interest payments must be made on a quarterly basis, the effective interest rate is 6.136%. Nevertheless, LANXESS AG is entitled under certain conditions to defer interest payments until the final maturity date of 15 September 2007, in which case the deferred interest payments, together with any interest accrued thereon, will be payable upon exercise of the conversion right. LANXESS AG's obligations arising under the Convertible Bond to pay the principal and interest as well as all other amounts arising under the individual bonds will be subordinated to the senior and non-subordinated claims of all other creditors of LANXESS AG.

The bondholder — currently Bayer AG — may convert the Convertible Bond into shares in LANXESS AG between 20 July 2005 and 20 July 2007 (conversion right (*Wandlungsrecht*)). In addition, LANXESS AG is obliged to convert the Convertible Bond into shares on 15 September 2007 (conversion duty (*Wandlungspflicht*)). Save in exceptional cases, the Convertible Bond is not redeemable in cash.

The conversion ratio — *i.e.*, the number of shares to be delivered by LANXESS AG upon conversion of the individual bonds — is contingent upon the arithmetic average of the volume-weighted daily closing prices of the LANXESS shares as quoted on the XETRA-System of Deutsche Börse AG for the 20 successive trading days ending on the third trading day immediately preceding the mandatory conversion date (15 September 2007) or, in the event of the exercise of the conversion right, the day the conversion right is exercised, rounded to the nearest whole cent (''Reference Share Price''), which is calculated as follows: If the Reference Share Price is less than or equal to the arithmetic average of the volume-weighted average closing prices of the LANXESS shares as quoted on the XETRA-System of Deutsche Börse AG on the first ten trading days of the LANXESS Shares beginning on and including the day of their initial listing, rounded to the nearest whole cent (''Initial Share Price''), the conversion ratio will be calculated by dividing the nominal amount of the individual bond by the Initial Share Price. If the Reference Share Price is greater than or equal to the Initial Share Price multiplied by 1.15 (''Conversion Price''), the conversion ratio will be the number of shares that result from dividing the nominal value of the bond by the Conversion Price. If the Reference Share Price is neither less than or equal to the Initial Share Price nor greater than or equal to the Conversion Price, the conversion ratio will be the number of shares that result from dividing the nominal value of the bond by the Reference Share Price. The Initial Share Price and the Conversion Price will be adjusted in the event that LANXESS AG undertakes certain capitalisation measures and provided that LANXESS AG does not make use of other options.

In a joint letter dated 15 September 2004, Deutsche Bank Aktiengesellschaft and Morgan Stanley & Co. International Limited have confirmed that the interest rate of the Convertible Bond and the conversion premium as set out in the terms and conditions of the Convertible Bond are broadly consistent with those of similar instruments that exist in the international capital markets.

Should Bayer AG hold the Convertible Bond, either in whole or in part, at the time the conversion right is exercised or the conversion duty arises, it will obtain an ownership interest in LANXESS AG. The extent of the ownership interest will significantly depend on the percentage of the Convertible Bond that Bayer AG still holds and on the Initial Share Price and Reference

Share Price of the LANXESS shares at the time. In the Joint Spin-off Report prepared in connection with the Spin-off, Bayer AG stated that, in the event of a conversion, it does not intend to retain, for the long term, the LANXESS Shares to which it will become entitled.

Supply and Service Relationships

Overview

Extensive global business relationships are in place between LANXESS AG and the Bayer Group. The Company estimates that in 2005 the Bayer Group will supply approximately €0.5 billion worth of goods and services to LANXESS Group companies. This figure does not include services provided by Bayer Industry Services GmbH & Co. OHG (BIS) and its subsidiaries. In 2005, LANXESS anticipates that it will obtain approximately €0.5 billion worth of site-specific services at the chemical park sites from this company (including its subsidiaries). Furthermore, the Company estimates that in 2005 the Bayer Group will purchase goods and services in the amount of approximately €0.7 billion from LANXESS Group companies. Most of these goods and services will be supplied to the Bayer MaterialScience and Bayer CropScience subgroups.

In a number of countries in which LANXESS does not have its own foreign affiliates, it conducts its local distribution through Bayer Group companies. The Company anticipates that sales realised in this manner will amount to approximately €0.7 billion in 2005. Conversely, companies within the LANXESS Group distribute Bayer Group products in some countries on the basis of commercial agency and exclusive dealer arrangements. These sales will, however, not be significant.

The material individual supply and service relationships between LANXESS and the Bayer Group are as follows:

Framework agreements for the supply of goods and services

Framework agreements between LANXESS GmbH, on the one hand, and Bayer MaterialScience AG, Leverkusen, Bayer CropScience AG, Monheim, Bayer HealthCare AG, Leverkusen, Bayer Industry Services GmbH & Co. OHG, Leverkusen, Bayer Technology Services GmbH, Leverkusen, and Bayer Business Services GmbH, Leverkusen, respectively, on the other hand, form the basis for the majority of the supply and service relationships.

The framework agreements generally — and to varying degrees — contain so-called ''sunk costs'' provisions (*Remanenzkostenregelungen*) (in many cases staggered) and ''take-or-pay'' provisions. Under these provisions, in the event of a termination of the agreement or if the quantities purchased are less than the minimum agreed amount, the customer must reimburse the supplier for any fixed costs which cannot be directly defrayed or reduced upon termination of the agreement or in the event of a shortfall in the quantities purchased. Moreover, the framework agreements contain provisions as to limitation of liability according to amount and type of loss.

Supply and Service Relationships between LANXESS GmbH and companies of the Bayer MaterialScience Subgroup

The framework supply agreements and the framework agreement for the provision of services between LANXESS GmbH and Bayer MaterialScience AG have been entered into for an indefinite term. The framework agreement for the provision of services may be terminated on an annual basis; the framework supply agreements may not be terminated prior to 31 December 2009. This does not preclude shorter terms for individual supply and service relationships.

Individual agreements in accordance with the framework supply agreement between LANXESS GmbH and Bayer MaterialScience AG

The following individual agreement as well as, in particular, other individual agreements in respect of 1. 6-hexanediol, phthalic anhydride, polybutylene terephthalates, trimethylol propane and the conversion of nitrobenzol into aniline have been concluded and appended to the framework supply agreement between LANXESS GmbH and Bayer MaterialScience AG.

Adipic acid

The most significant individual agreement in terms of sales is the supply agreement between LANXESS GmbH and Bayer MaterialScience AG in respect of adipic acid. Pursuant to this agreement, Bayer MaterialScience is obliged to purchase a bulk of its requirements for adipic acid as the minimum contractual quantity through LANXESS GmbH. The agreement expires on 31 December 2009.

Framework supply agreement between Bayer MaterialScience AG and LANXESS GmbH

Significant individual agreements have been concluded on the basis of the framework supply agreement between Bayer MaterialScience AG and LANXESS GmbH, in particular in respect of the supply of aniline, azeotrope nitric acid and polycarbonate by Bayer MaterialScience AG to LANXESS GmbH. An individual agreement in respect of the supply of formaldehyde with a five-year term is currently being negotiated.

Agreements outside the scope of the framework agreements

Agreements outside the scope of the framework agreements between LANXESS GmbH and Bayer MaterialScience AG include an agreement to supply products for the leather, paper and textile industries as well as agreements for contract manufacturing in respect of polybutylene and polybutylene terephthalate compounds (Bayer MaterialScience to LANXESS) and polycarbonate/ABS-blends (LANXESS to Bayer MaterialScience). In addition, there are the following material contracts for the supply of goods and services.

ABS-intermediates

A supply agreement in respect of ABS-intermediates has been concluded between various LANXESS companies and certain companies of the Bayer MaterialScience subgroup. Under this supply agreement, the contracting Bayer parties agree to purchase ABS-powder, ABS-pre-compounds, bulk-ABS and SAN exclusively from the LANXESS contracting parties. The agreement has a minimum term ending on 31 December 2007 and provides for a right of extraordinary termination by the contracting Bayer parties in the event that the LANXESS business activities to which the ABS-Intermediates activities are allocable are transferred to a third party outside the LANXESS Group which is in direct competition with the contracting Bayer parties.

Alphamine (1, 5-naphthylenediamine)

As of 1 February 2005, an individual and a supplemental agreement is anticipated to take effect between LANXESS GmbH and Bayer MaterialScience AG, pursuant to which Bayer MaterialScience AG will be obliged to purchase from LANXESS GmbH specified minimum quantities of alphamine (1, 5-naphthylenediamine) accounting for a large part of its requirements. A formula will be used to calculate the supply price per unit. The agreement is expected to have a binding minimum term which expires on 31 December 2015 and to include a provision in respect of sunk costs. In order to assure the supply to Bayer MaterialScience AG of alphamine (1, 5-naphthylenediamine), it will be entitled to acquire the intellectual property rights to the alphamine manufacture on the termination of the agreement or shutdown of the plants. In the event of a sale by LANXESS of the plants, the alphamine business, or the related intellectual property rights by LANXESS, Bayer MaterialScience AG will be granted a purchase right to the respective object of sale. These agreements will replace the agreement between LANXESS GmbH and Bayer MaterialScience AG concerning the supply of alphamine (1, 5-naphthylenediamine).

Electrolysis products (chlorine, sodium hydroxide, hydrogen and hydrochloric acid)

Pursuant to a supply contract between Bayer MaterialScience AG and LANXESS GmbH, Bayer MaterialScience AG is obliged to supply certain minimum quantities of chlorine, sodium hydroxide, hydrogen and technically-distilled hydrochloric acid. In return, LANXESS GmbH is obliged to supply Bayer MaterialScience AG with certain minimum quantities of hydrochloric acid and saline solution. The term of the agreement expires on 31 December 2009.

Contract manufacturing of electronics chemicals

A contract manufacturing agreement in respect of certain electronics chemicals is in place between LANXESS GmbH and H.C. Starck GmbH, pursuant to which H.C. Starck GmbH is obliged to purchase a portion of its total requirements with regard to individual products from LANXESS GmbH, which portion will decrease over the term of the agreement. The agreement has a minimum term ending on 31 December 2009. The agreement may also be terminated early if the parties fail to reach an agreement on requisite price adjustments. However, in this case, H.C. Starck GmbH is obliged to reimburse to LANXESS GmbH the relevant sunk costs.

Supply and transport of carbon monoxide

The agreement in respect of the supply of carbon monoxide entered into by Bayer AG and Messer Griesheim GmbH in 1999 and having a term of 15 years was assigned to Bayer MaterialScience AG in the context of the 2002 carve-out of Bayer AG's chemicals and polymers business areas into independent companies. Bayer MaterialScience AG subsequently entered into an individual agreement with Bayer Chemicals AG, a legal predecessor to LANXESS GmbH, in accordance with the framework agreement between both parties in respect of the supply and transport of carbon monoxide at the Dormagen site. In proportion to its share of the quantities, Bayer Chemicals AG (and thus LANXESS GmbH) will assume the arrangements made in the agreement with Messer Griesheim GmbH and will therefore be deemed, as between LANXESS GmbH and Bayer MaterialScience AG, as if it were a contracting partner of Messer Griesheim GmbH.

Polychloroprene

This agreement relates to polychloroprene in both solid and liquid form. Pursuant to the agreement, LANXESS GmbH supplies Bayer MaterialScience AG with a stipulated annual minimum quantity of polychloroprene. The agreement is binding upon the parties until 31 December 2009. Each party has a right of extraordinary termination if the other party transfers the business unit to which the respective products are attributable to a third party outside the LANXESS Group or outside the Bayer Group, which transferee also operates in the production or sale of polychloroprenes. Bayer MaterialScience AG has a right of extraordinary termination subject to an obligation to compensate for any sunk costs, provided that Bayer MaterialScience AG was not in a position during the prior calendar year to purchase a defined percentage of the agreed minimum quantity.

Supply and Service Relationships between LANXESS GmbH and companies of the Bayer CropScience subgroup

The framework supply agreements which are currently still being negotiated as between LANXESS GmbH and Bayer CropScience AG are anticipated to be for indefinite terms. These agreements provide for minimum contract quantities and take-or-pay rules. They may not be terminated before 31 December 2009. This does not preclude the possibility of shorter terms for individual supply relationships. Provisions governing sunk costs have also been provided for in individual cases.

Individual agreements in accordance with the framework supply agreement between LANXESS GmbH and Bayer CropScience AG

Individual supply agreements will be concluded on the basis of the contemplated framework supply agreement between LANXESS GmbH and Bayer CropScience AG in respect of the supply by LANXESS GmbH of the following to the companies of the Bayer CropScience subgroup: 1, 2-propylendiamin, 3-trifluormethylacetophenon, 3, 5-dichlorphenyl isocyanate and benzylamine.

Agreements outside of the scope of the framework agreements

The following are significant agreements for the supply of goods and services which are not within the scope of the framework agreements between LANXESS GmbH and Bayer CropScience AG:

Distribution agreement in respect of active ingredients

Bayer CropScience AG and LANXESS GmbH have entered into a distribution agreement relating to chemical substances used in material protection. Pursuant to this agreement, Bayer CropScience AG has granted LANXESS GmbH the exclusive right to distribute defined products in its own name and for its own account. In return, LANXESS GmbH is obliged to use, in defined areas of application, exclusively products obtained from Bayer CropScience AG, provided that Bayer CropScience AG is able to supply an appropriate product for the application in question. Bayer CropScience AG has also granted LANXESS GmbH the right to use, free of charge, certain Bayer CropScience AG trademarks for sales and distribution purposes. The agreement has a minimum term which expires at the end of 2009. Should a third party outside the LANXESS Group and in competition with Bayer CropScience AG or one of its subsidiaries gain control over LANXESS GmbH or its material protection business, Bayer CropScience AG will have a right of extraordinary termination.

Agreement for the provision of regulatory services

In connection with the above-mentioned distribution agreement, the parties have entered into a service agreement. Pursuant to this agreement, Bayer CropScience AG is obliged to allow LANXESS GmbH access to data and registrations pertaining to certain chemical substances used for material protection for purposes of marketing such products and to provide corresponding services. In return, LANXESS GmbH is likewise obliged to allow access to its corresponding data and registrations should Bayer CropScience AG require these for areas of application outside the defined material protection applications. The agreement has the same term as the above-mentioned distribution agreement.

Supply and Service Relationships between LANXESS GmbH and companies of the Bayer HealthCare Subgroup

A framework agreement in respect of supplies to be made by LANXESS GmbH to Bayer HealthCare AG is to be concluded between LANXESS GmbH and Bayer HealthCare AG. The agreement will provide for a minimum term expiring on 31 December 2009.

LANXESS GmbH and Bayer HealthCare AG have entered into the following individual agreements intended to be in accordance with the framework supply agreement:

Moxifloxacin

LANXESS GmbH and Bayer HealthCare AG have concluded a supply agreement in respect of moxifloxacin, pursuant to which LANXESS GmbH is obliged, in 2005, to supply moxifloxacin and Bayer HealthCare AG is in return obliged to purchase a specified quantity of the product at a fixed price per unit. The agreement has a fixed term, which expires on 31 December 2005.

Agreement in respect of sunk costs

In the context of the relocation of moxifloxacin production from LANXESS GmbH to Bayer HealthCare AG, the latter is obliged to pay certain contractually-stipulated sunk costs.

Pyrrolopiperidine and trifluorchinoloncarbon acid

LANXESS GmbH and Bayer HealthCare AG have entered into agreements in respect of the supply of pyrrolopiperidine and trifluorchinoloncarbon acid, preliminary phase substances of the active ingredient moxifloxacin. Pursuant to these agreements, Bayer HealthCare AG is obliged to purchase specified minimum quantities of the products from LANXESS GmbH annually. The parties have agreed to index-linked prices dependent on the quantity supplied. The agreements have fixed terms, which expire on 31 December 2008.

Supply and Service Relationships between LANXESS GmbH and Bayer Industry Services GmbH & Co. OHG and its Subsidiaries

LANXESS and Bayer AG jointly use the chemical park sites in Leverkusen, Dormagen, Krefeld-Uerdingen and Brunsbüttel. These are operated by Bayer Industry Services GmbH & Co. OHG (''BIS''), in which LANXESS GmbH holds a 40% interest (for a description of LANXESS GmbH's equity interest in BIS, see ''— *LANXESS GmbH's equity interest in Bayer Industry Services GmbH & Co. OHG* '').

LANXESS GmbH and BIS have entered into a framework agreement governing the provision of mandatory and elective services as defined in the framework agreement. The mandatory services (*Pflichtleistungen*) comprise infrastructure services in respect of, for example, the basic infrastructure of the chemical park sites, the electricity grid, the plumbing system, the site railway network, the port facilities, sewage treatment plants, plant security and other mandatory services. The agreement will apply for the same term as the site agreement for the chemical park sites. In principle, each party has the right to routinely terminate, either in whole or in part, any or all of the individual agreements concluded in accordance with the framework agreement in respect of elective services (*Wahlleistungen*), however not before 31 December 2006.

In addition to the previously-concluded individual agreements in respect of the supply of energy services described below, BIS and LANXESS GmbH will enter into, in particular, agreements in respect of environmental services, technical services, infrastructure services, security/environmental protection/regulatory approvals/chemical analysis and plant security in accordance with the above-mentioned framework agreement.

Energy services

BIS and LANXESS GmbH have entered into an agreement for the supply of steam, electricity, pressurised air, cooling air, natural gas, water for industrial use, nitrogen and oxygen to the chemical park sites at Leverkusen, Dormagen and Krefeld-Uerdingen. The agreement has a term of five years and an option to extend.

Agreement in respect of logistics services between Chemion GmbH and LANXESS GmbH

Chemion GmbH is a wholly-owned subsidiary of Bayer Industry Services GmbH & Co. OHG and provides logistics services, including tank farm-related services, to LANXESS GmbH. A corresponding agreement is being negotiated. It will primarily concern logistics services to be provided to the sites in the Lower Rhine region.

Supply and Service Relationships between LANXESS GmbH and Bayer Technology Services GmbH

On the basis of a series of individual contracts in accordance with a framework agreement in respect of the supply of goods and services, Bayer Technology Services GmbH provides LANXESS GmbH with engineering and procedural services, for example in the areas of process technology, materials technology, logistics, planning and construction of plants and process analysis technology. LANXESS GmbH is obliged to purchase contractually-prescribed minimum quantities of goods and services. Should the minimum quantities not be purchased, LANXESS GmbH will be obliged to pay compensation therefor. The agreement has a minimum term, which expires on 31 December 2008. Should LANXESS GmbH terminate the framework agreement upon due notice or fail, beginning in 2009, to meet the minimum quantity requirements prescribed for the year 2008, it will have to bear any sunk costs incurred by Bayer Technology Services GmbH in connection with the termination or the purchase shortfalls.

Supply and Service Relationships between LANXESS GmbH and Bayer Business Services GmbH

On the basis of a framework agreement entered into by Business Services GmbH and LANXESS GmbH, Business Services GmbH provides services in the areas of information technology, personnel management and consulting to LANXESS GmbH and LANXESS AG. The nature and scope of these services are specified in individual agreements. The framework agreement stipulates that, in the event of a premature termination of the agreement, LANXESS GmbH must bear any sunk costs. The framework agreement has a minimum term, which expires on 31 December 2010.

By means of an individual agreement entered into in accordance with the above-mentioned framework agreement, Bayer Business Services GmbH is obliged to provide services in respect of SAP applications, comprising both SAP software support and hardware services. The agreement has a term expiring on 31 December 2010. After a minimum three-year term and allowing for payments of sunk costs, the agreement may be terminated either in whole or in part.

Other significant individual contracts govern services in respect of IT operations (e.g., networks) and personnel systems.

Supply and Service Relationships between LANXESS N.V. and Bayer Antwerp N.V.

Until 31 December 2008, LANXESS N.V., Bayer Antwerp N.V. and Bayer International Comm.V. make up a so-called ''technical operating entity'' under Belgian law. LANXESS N.V and Bayer Antwerp N.V. entered into a framework agreement with an indefinite term which governs the reciprocal services provided by the contracting parties at the site. This framework agreement encompasses more than 50 service agreements with a total volume in excess of €50 million. The terms of most of the agreements, concurrent with the duration of the technical operating entity, expire at the end of 2008. The most sizeable individual agreement relates to the supply of energy, primarily steam, by LANXESS to the Bayer Group, which has a term expiring in February 2015.

Supply and Service Relationships between LANXESS Corporation and Bayer MaterialScience LLC and/or Bayer Corporate and Business Services LLC

Bayer MaterialScience LLC (BMS LLC) and LANXESS Corporation are parties to a framework agreement on certain production-relevant services at formerly joint sites. The framework agreement governs, among other things, the commercial and technical parameters of the services, damages and liability.

The key individual contracts (''term sheets'') relate to:

- Services provided by BMS LLC for the production of maleic anhydride for LANXESS Corporation at the Bayer MaterialScience site in Baytown, Texas, U.S.A. The agreement has a term expiring on 2 January 2013.
- The sale of excess steam from the production of maleic anhydride to BMS LLC.
- Services provided by BMS LLC to LANXESS Corporation for the production of iron oxide-pigments at the Bayer MaterialScience site in New Martinsville, West Virginia, U.S.A. The agreement has a term expiring on 30 June 2007.

In addition, LANXESS Corporation and BMS LLC and/or Bayer Corporate and Business Services LLC (BCBS) have entered into framework agreements in respect of certain administrative, laboratory and warehousing services which BMC LLC or BCBS provides for LANXESS Corporation, primarily for the site in Pittsburgh, Pennsylvania, U.S.A. Of the great number of individual contracts (''term sheets''), those governing information services are the most important. Depending on the service covered, they typically have terms of one to six years.

Supply of styrene

Bayer MaterialScience LLC and LANXESS Corporation have entered into an agreement governing the supply of styrene. Pursuant to this agreement, LANXESS Corporation has agreed to purchase a contractually-prescribed minimum quantity of styrene from Bayer MaterialScience LLC. The agreement has a minimum term, which expires on 31 December 2005.

Agency agreements between LANXESS GmbH and companies of the Bayer Group

In a number of countries in which LANXESS is not represented through a foreign affiliate, local distributions are also consummated through companies of the Bayer Group (so-called ''agency companies''). The agency companies function primarily as sales agents. In addition, some agency companies also sell a range of LANXESS products as independent distributors. The Company anticipates sales consummated through the agency companies to amount to approximately €0.7 billion in fiscal year 2005.

The mostly standardised contracts with the agency companies grant a right to market and sell in the respective regions. If products are sold as a result of an agency company's brokering efforts, the agency company will be paid a commission. LANXESS also has the right to make direct sales to customers. In the event of such sales, however, LANXESS also has to pay a commission to the relevant agency company. The agreements have been entered into for indefinite terms. They may be terminated as of 30 September 2005 and thereafter at the end of each calendar year. LANXESS also has the option of terminating the agreements with respect to certain products or product groups. The agreement provide for a right of extraordinary termination in the event that more than half the shares of a party are transferred to a third party outside the LANXESS or Bayer Group. In general, the agency companies have the right to post-termination compensatory claims in the event the agreements are terminated. The size of these claims will be based generally on the average total annual commissions generated as well as the average annual profits earned from the independent distribution business. In the event an agreement is terminated during the first year of its term, the agency company may in the alternative seek a compensatory payment based on sunk costs.

The companies of the LANXESS Group also distribute Bayer Group products on the basis of agency and distribution agreements, albeit to a lesser extent. Thus, for example, LANXESS has the sole distribution right for certain material protection products from the Bayer CropScience subgroup.

Addendum Tax Agreement between LANXESS GmbH and Bayer AG

On 14 October 2004, LANXESS GmbH and Bayer AG entered into an addendum tax agreement. This agreement governs the allocation of certain additional income tax charges which could result from measures taken to combine the chemicals and polymers activities in LANXESS GmbH. Under this agreement, if future income tax charges with respect to the current assets transferred to LANXESS GmbH increase as a result of a change in valuation applied by the tax authorities to the acquisition balance sheet which LANXESS GmbH filed for tax purposes, the present value of such additional charges will be split on a 50:50 basis between Bayer AG and LANXESS GmbH under certain conditions. Reduced tax charges on other balance sheet items will be treated on a standardised basis (see also ''*Risk Factors — Risks relating to the Spin-off and Strategic Realignment of LANXESS — Tax consequences in connection with the Spin-off and the preparatory measures implemented for this purpose*'').

Agreements on industrial property rights

In connection with the Spin-off transaction, the legal relations between the Bayer Group and LANXESS with respect to industrial property rights were reorganised.

In addition to other assets and liabilities, rights (including licences and expectancies) to certain domestic and foreign patents, utility patents, trademarks, domains, copyrights and registered designs as well as any applications for the registration of such rights, to the extent such rights affected the business activities that were spun off, were transferred by Bayer Chemicals AG and Bayer MaterialScience AG to LANXESS GmbH by way of spin-off (see ''*Further Details and Explanation of the LANXESS Spin-off — First Step — Combination of Major Parts of the Chemicals and Parts of the Polymers Activities*'').

Pursuant to agreements dated 10 September 2004, Bayer AG also granted LANXESS GmbH the right to demand that certain industrial property rights (patents, utility patents, registered designs, trademarks and domains) be assigned or re-registered, to the extent such rights are solely or primarily allocable to those business activities transferred by Bayer Chemicals AG and Bayer MaterialScience AG to LANXESS GmbH.

In addition, Bayer AG and Bayer MaterialScience AG, on the one hand, and LANXESS GmbH, on the other, entered into various licence agreements (all having the same date) for specific industrial property rights. The legal relationship between the Bayer Group and LANXESS, as regards these agreements, may be described as follows:

Patents, utility models and registered designs

LANXESS GmbH is entitled, within five years following the effective date of the Spin-off from Bayer AG, to demand the assignment and re-registration of industrial property rights (patents, utility patents and registered designs), which are primarily or solely allocable to the LANXESS business activities. Even prior to this date, LANXESS is entitled to use such industrial property rights.

As against Bayer AG and Bayer MaterialScience AG, LANXESS enjoys a partially exclusive, partially non-exclusive licence to use certain patents which were not assigned to LANXESS GmbH because they are allocable primarily to Bayer MaterialScience AG's remaining business activities, but which nevertheless are used by LANXESS GmbH. The licence is limited to LANXESS GmbH's business activities. In return, LANXESS GmbH has granted Bayer MaterialScience AG a partially exclusive and partially non-exclusive licence to certain patents which were assigned to LANXESS GmbH because they are allocable primarily to its business activities, but which nevertheless are also used by Bayer MaterialScience AG. The licence is limited to Bayer MaterialScience AG's business activities.

Pursuant to the spin-off and acquisition agreement between Bayer Chemicals AG and LANXESS GmbH, LANXESS GmbH was granted an exclusive, royalty-free and transferable licence to use those domestic and foreign industrial property rights (patents and utility patents) which, while relating to the chemicals activities transferred by Bayer Chemicals AG, are nevertheless primarily allocable to other operating areas of the Bayer Group. The above-mentioned licence to LANXESS GmbH is limited to the chemicals activities transferred by Bayer Chemicals AG.

Finally, Bayer AG and Bayer MaterialScience AG, one the one hand, and LANXESS GmbH, on the other hand, executed an option contract in which the parties have agreed under certain conditions to enter into negotiations with respect to granting non-exclusive patent licences. The licences may be used only with respect to the respective business activities conducted by the licensee.

Trademarks and domains

Bayer AG has granted LANXESS GmbH and its affiliated companies (section 15 AktG) a non-exclusive, worldwide, royalty-free and non-transferable licence to use all trademarks and/or trademark registration applications of the word mark ''Bayer'' and any trademarks containing the word ''Bayer'' or the ''Bayer cross'' symbol for a period of one year beginning on the date the Spin-off enters into effect. This licence is limited to the chemicals and polymers activities transferred by the Bayer Group to LANXESS GmbH and is granted for purposes of identifying the products manufactured or distributed and the services provided by LANXESS GmbH or its affiliated companies (section 15 AktG) and identifying its business names. After the expiry of this period, products that had already been manufactured by that date may be sold and distributed for two additional years under the relevant trademarks. Any domains containing the word ''Bayer'' will be maintained for an interim period.

Certain trademarks and trademark registration applications containing the word ''Bay'' were licensed by Bayer AG to LANXESS GmbH and its affiliated companies (section 15 AktG) on an exclusive and royalty-free basis for an indefinite period of time. These licences relate to the chemicals and polymers activities transferred by the Bayer Group to LANXESS GmbH.

With respect to other trademarks or trademark registration applications and domains which contain neither the word ‘‘Bayer’’ nor the letters, words or symbols ‘‘Bayer’’, the ‘‘Bayer cross’’ or ‘‘Bay’’ and which are allocable solely to LANXESS business activities, LANXESS GmbH is entitled to demand, within five years following the effective date of the Spin-off, that these industrial property rights be assigned to and re-registered in the name of LANXESS GmbH or one of its third-party designees. Even prior to this date, LANXESS is entitled to use such industrial property rights.

Land Purchase Agreement between LANXESS GmbH and Bayer AG

Pursuant to a notarised land purchase agreement dated 30 December 2004 between Bayer AG and LANXESS GmbH, Bayer AG sold land parcels from its real property at the chemical park sites in Leverkusen, Dormagen, Krefeld-Uerdingen and Brunsbüttel to LANXESS GmbH, which parcels have not yet been surveyed. The land purchase agreement will enter into effect upon the expiry of the calendar day (anticipated to be 29 January 2005) following the day on which the Spin-off between Bayer AG and LANXESS AG is recorded in the Commercial Register (*Handelsregister*) for Bayer AG. The parcels for sale involve the vast majority of those areas that LANXESS GmbH had previously used at the above-mentioned sites. The properties are to be sold together with all rights and significant fixtures related thereto. Generally also included in the sale are any appurtenances relating to the relevant parcel as well as any operating equipment belonging to the parcels and buildings, to the extent that Bayer AG owns these items. Operating equipment, which does not qualify as significant fixtures, and appurtenances will not be sold with the property, however, to the extent beneficially owned by Bayer HealthCare AG, Bayer Chemicals AG, Bayer MaterialScience AG, Bayer CropScience AG, Bayer Industry Services GmbH & Co. OHG, Bayer Business Services GmbH or Bayer Technologies GmbH, unless they are intended to pass to LANXESS GmbH pursuant to the spin-off agreements concluded in September 2004 between Bayer Chemicals AG and LANXESS GmbH and between Bayer MaterialScience AG and LANXESS GmbH. The properties are sold subject to a disclaimer of liability by Bayer AG with respect to the size, quality and features of the parcels. Specifically, Bayer AG disclaims any liability for any latent or hidden qualitative defects. The net purchase price for the real property (including any buildings thereon, and the appurtenances and operating equipment sold therewith) totals €256 million. The purchase price was determined on the basis of an appraisal and is fixed. The purchase price will not be affected by any future surveys of individual parcels. Possession, use, risk and encumbrances, as well as general duties to maintain pedestrian and vehicular safety on the property, will pass to LANXESS GmbH when the land purchase agreement becomes effective. The conveyance of title in performance of the agreement will be made as soon as the relevant land register (*Grundbuch*) requirements are met, in particular, once the surveys of the parcels have been completed. Should the land register requirements to complete the conveyance of title not be met for legal reasons, either in whole or in part, Bayer AG and LANXESS AG have agreed to find an alternative solution which, in terms of the economic outcome, is as similar to a transfer of ownership as possible. Pursuant to the land purchase agreement, LANXESS GmbH and Bayer AG consider that a suitable alternative solution, in place of the transfer of title which cannot be carried out, would be to grant to LANXESS GmbH various easements to the properties sold, according to which LANXESS GmbH would be able to use the land for its own operating purposes to the exclusion of Bayer AG. In this case, the purchase price would be reduced in accordance with a specified procedure. To this extent, the parties have waived any rescission and damages claims.

Site agreement between LANXESS GmbH, Bayer Industry Services GmbH & Co. OHG and Bayer AG

On 30 December 2004, LANXESS GmbH and Bayer AG and Bayer Industry Services GmbH & Co. OHG (‘‘BIS’’) entered into a site agreement relating to the chemical park sites at Leverkusen, Dormagen, Krefeld-Uerdingen and Brunsbüttel. This agreement will enter into effect contemporaneously with the land purchase agreement, *i.e.*, upon the expiry of the calendar day following the day on which the Spin-off is entered in the Commercial Register (*Handelsregister*) for Bayer AG. LANXESS AG is also party to the site agreement, however only insofar as it accounts for the performance of the obligations of LANXESS GmbH under the site agreement.

The site agreement governs, among other things, the future use of chemical park land, as well as the buildings, plants, infrastructure facilities and other installations thereon. In this connection, the site agreement sets forth operating duties and establishes rules on environmental protection, plant security and prevention of hazards. Pursuant to the site agreement, the contracting parties also grant one another reciprocal status quo protection with respect to their respective uses of the site to date. In this context, each of the contracting parties has the right in future to continue the business activities in which they or their affiliated companies had previously been engaged on the chemical park sites and to continue the use of the land, buildings, plants and other installations in the current scope, and to do so both on their own property and on the property of the other contracting party. To the extent that Bayer AG or LANXESS AG have elected to discontinue their use of land, buildings, plants and other installations on the properties of the other party, they are generally subject to an obligation to demolish and remove the buildings, plants and installations previously used by them. BIS is obliged to demolish and remove the buildings, plants and other installations on certain of Bayer AG's properties.

The site agreement also contains provisions regarding future projects at the sites. Thus, the contracting parties must coordinate and agree, using a specified procedure, on future construction projects, installation of plants and changes in use, with the objective of avoiding any material harm being caused by the relevant projects to the other contracting parties' interest as a user of the site and of enabling the existence and orderly continued development of the chemical park site in future.

Furthermore, the site agreement governs the future role and responsibilities of BIS as the so-called ''chemical park site operator'' and prescribes its rights and duties in this connection. Pursuant to the site agreement, the companies of the Bayer Group and LANXESS Group must in future purchase certain services from BIS in its role as the chemical park site operator (so-called ''mandatory services''). These services include primarily infrastructure services with respect to, for example, the basic infrastructure of the chemical park site, the electricity grid, the pipeline bridges and pipeline network, the railway and port infrastructure, the transfer and management of wastewater, as well as plant security and chemical park site documentation.

LANXESS GmbH's equity interest in Bayer Industry Services GmbH & Co. OHG

Since 1 July 2004, LANXESS GmbH has held a 40% interest in Bayer Industry Services GmbH & Co. OHG (''BIS''), which in turn holds all the shares of Chemion GmbH, a company affiliated through a profit (loss) transfer agreement. The remaining 60% interest in BIS is held by Bayer AG. LANXESS GmbH holds no shares in Bayer Industry Services Geschäftsführungs-GmbH, which serves as the management company handling the business affairs of BIS.

In connection with the LANXESS GmbH's equity interest in BIS, Bayer AG, Bayer Industry Services Geschäftsführungs-GmbH and LANXESS GmbH entered into an admission and shareholders' agreement (*Aufnahmevertrag und Gesellschaftervereinbarung*) on 17 September 2004.

Bayer AG and LANXESS GmbH also entered into a shareholders' agreement on 17 September 2004. On the basis of this agreement, LANXESS GmbH has the right to appoint a managing director of Bayer Industry Services Geschäftsführungs-GmbH as well as two members of the supervisory board of this company. Moreover, the parties agreed that LANXESS GmbH and its affiliated companies (section 15 AktG) should receive the services from BIS on terms and conditions that are no less favourable than those, which BIS grants to Bayer AG or any companies in which Bayer AG holds, either directly or indirectly, a majority interest.

On the basis of the BIS partnership agreement, LANXESS GmbH is entitled to certain voting, inspection and disclosure rights, which allow it to exert influence as a minority partner over BIS management. Thus, for example, a list of certain significant transactions may only be entered into by BIS with the approval of LANXESS GmbH. The partnership agreement furthermore imposes a non-compete covenant on LANXESS GmbH. According to this covenant, LANXESS GmbH and its affiliated companies (section 15 AktG) may not — either themselves or through others — engage in any business activities at the chemical park sites in Leverkusen, Dormagen, Krefeld-Uerdingen and Brunsbüttel that compete with BIS business activities. Exceptions to these covenants primarily involve certain transactions required to meet the parties' own needs (specifically energy supply and procurement, water supply and ventilation or waste disposal, maintenance work and training services), business activities that had been conducted by LANXESS GmbH or its affiliated companies (section 15 AktG) on 1 July 2004 within the scope existing on that date and the leasing and marketing of LANXESS parcels on the chemical park sites.

Additional agreements

In addition, the following significant agreements are currently being negotiated or have already been executed between LANXESS and Bayer:

A so-called ''shareholder agreement'' is expected to be executed between LANXESS (Pty) Ltd., South Africa, Bayer (Pty) Ltd., South Africa, and Bayer Mining Holdings (Pty) Ltd., South Africa, and is intended to govern the rights of LANXESS (Pty) Ltd. and Bayer (Pty) Ltd. as the stockholders of Bayer Mining Holdings (Pty) Ltd.

At the end of 2004, LANXESS and the Bayer Group agreed to extend the payment dates with respect to the supply of selected goods and services by the Bayer Group to LANXESS. This payment extension covered a volume of approximately €130 million, scheduled on a rolling basis until the third quarter of fiscal year 2006.

The Management Boards at LANXESS AG and Bayer AG have reached an agreement that the sponsorship volumes attributable to LANXESS in fiscal year 2004 (€4.9 million) would be continued and progressively lowered from that level over the next three years — 75% in fiscal year 2005, 50% in fiscal year 2006 and 25% in fiscal year 2007. In this regard, a cooperation agreement is currently being prepared. Furthermore, the LANXESS Board of Management has announced its intention that, in regard to donation funding of non-profit company organisations, the donations made in fiscal year 2004 and attributable to LANXESS (€5 million) would be continued from 2005 until 2007 commensurately with the reductions made under the sponsorship programmes.

RheinChemie GmbH and Bayer MaterialScience AG are currently negotiating small portfolio adjustments. These adjustments relate to the reciprocal transfer of certain business activities relating to additives in the polyurethane chemicals area. The Company expects that the relevant agreements will be executed in the first half of 2005.

In connection with the €200 million Convertible Bond issued to Bayer AG, the Company entered into an agreement with Bayer AG, pursuant to which Bayer AG would initially waive a portion of the 6% interest owed to it under the Convertible Bond. The waiver is subject to a condition subsequent, namely, if and when the Spin-off enters into effect. As a matter of precaution, the rules concerning post-formation acquisitions (*Nachgründungen*) were observed.

An agreement is in place between Bayer AG and LANXESS GmbH on the basis of which Bayer AG, acting through the LANXESS Corporate Center established within Bayer AG, provides services to LANXESS GmbH that are allocable to the areas of activity of the LANXESS Corporate Center. The LANXESS Corporate Center is an independent organisational department of Bayer AG's Corporate Center in which the principal management and control functions of the LANXESS Group are combined and administered.

Business Transactions and Legal Relationships with Other Related Parties

Indemnification of Company Management Board Members

Pursuant to agreements entered into between Bayer AG and members of the Company's Board of Management, Bayer AG is obliged to indemnify the Management Board members with respect to possible personal liability for breach of the duties incumbent upon them as members of the Management Board. The obligation to indemnify relates, in particular, to breach of duty as to the use of financial information in connection with the Spin-off and the listing of the LANXESS shares. There is no duty to indemnify board members if the liability is based on a grossly negligent (*grob fahrlässig*) or intentional breach of duty. The fact that the financial information prepared by Bayer AG may not have been subjected to an otherwise customary intensive review constitutes neither gross negligence nor intentional breach. If and to the extent a claim for indemnity exists, Bayer AG will also forbear from taking action against the members of the Board of Management for breach of their employment or service contracts.

Positions on Supervisory or Management Bodies

The Company's Management Board members — Dr. Axel C. Heitmann, Dr. Ulrich Koemm, Dr. Martin Wienkenhöver and Matthias Zachert — hold various positions on the supervisory bodies of companies affiliated with LANXESS GmbH. In addition, Dr. Ulrich Koemm and Dr. Martin Wienkenhöver are members of the Bayer Chemicals AG (Leverkusen) Board of Management. At the close of the day on which the Spin-off enters into effect, both Board of Management members will resign amicably their offices in Bayer Chemicals AG.

The current Supervisory Board members continue to hold various positions on supervisory bodies of companies affiliated with Bayer AG.

Further Details and Explanation of the LANXESS Spin-off

In accordance with the concept for the strategic realignment of the Bayer Group resolved upon by the Board of Management of Bayer AG in November 2003, the Bayer Group will in future concentrate on its core business areas health, nutrition and high-tech materials, which are primarily driven by innovation and technology, through its subgroups Bayer HealthCare, Bayer CropScience and Bayer MaterialScience. The LANXESS Group, headed by LANXESS AG, will continue to operate the majority of the chemicals activities and approximately one third of the former polymers activities of the Bayer Group which are no longer part of the Bayer Group's strategic core business.

In simplified terms, the realignment of the Bayer Group is being implemented in two steps.

As a first step, implemented over the course of 2004, almost all of the chemicals and polymers activities to be continued within the LANXESS Group, including the foreign businesses and certain service and corporate center functions, were combined within LANXESS GmbH (which is currently 100% owned by Bayer AG) and its direct and indirect subsidiaries.

As a second step, the entire equity interest in LANXESS GmbH will be spun off into LANXESS AG pursuant to the German Transformation Act. As part of the transaction, Bayer AG stockholders will receive shares in LANXESS AG.

First Step — Combination of Major Parts of the Chemicals and Parts of the Polymers Activities

Spin-offs from Bayer Chemicals AG and Bayer MaterialScience AG

The domestic business activities of the LANXESS Group originate almost entirely from Bayer Chemicals AG and Bayer MaterialScience AG. These business activities were transferred together with all rights and obligations to LANXESS GmbH by way of spin-offs (*Abspaltung zur Aufnahme*) pursuant to section 123 (2) No. 1 UmwG. In return therefor, Bayer AG was in each case granted one share in LANXESS GmbH. Each spin-off was executed with economic effect as of 1 July 2004.

In the case of Bayer Chemicals AG, the transfer was implemented pursuant to a Spin-Off and Acquisition Agreement concluded in September 2004 between Bayer Chemicals AG as transferring entity and LANXESS GmbH as acquiring entity. Such transfer covered the majority of the chemicals activities of Bayer Chemicals AG. Bayer Chemicals AG's equity interests in GE Bayer Silicones Verwaltungs GmbH, GE Bayer Silicones GmbH & Co. KG, DyStar Holding Inc. and Wolff Walsrode AG were not transferred.

In the case of Bayer MaterialScience AG, the transfer was implemented pursuant to the Spin-off and Acquisition Agreement concluded in September 2004 between Bayer MaterialScience AG as transferring entity and LANXESS GmbH as acquiring entity. The transfer covered the polymers activities of the strategic business units BR/Butyl, Technical Rubber Products, Rubber Chemicals, RheinChemie, Fibers, Semi-Crystalline Products and the ABS/SAN portion of the strategic business entity Styrenics of Bayer MaterialScience AG.

Both spin-offs took effect upon their registration in the Commercial Registers (*Handelsregister*) at the respective domiciles of Bayer MaterialScience AG and Bayer Chemicals AG on 30 September 2004.

In addition to the other current and non-current assets, Bayer Chemicals AG and Bayer MaterialScience AG transferred to LANXESS GmbH, in particular, any rights allocable to the relevant business activities (including rights of use and contingent rights) in domestic and foreign patents, utility models, trademarks, domains, copyrights and design patents and applications for such rights (hereinafter referred to as ''Industrial Property Rights'') as well as all rights in the Industrial Property Rights held by Bayer AG as trustee for Bayer Chemicals AG and Bayer MaterialScience AG. Furthermore, all rights in software allocated to the respective business activities — to the extent that these were not subject to any third-party rights — and all other know-how was transferred. In addition, new agreements governing the use of certain other Industrial Property Rights were executed between Bayer AG, Bayer Chemicals AG, Bayer

MaterialScience AG and the Bayer service companies, on the one hand, and LANXESS GmbH, on the other hand (see ''*Business Transactions and Legal Relationships with Related Parties — Business Transactions and Legal Relationships with the Bayer Group*'').

In addition, the liabilities from operating activities allocable to the respective business activities, as well as certain financial obligations that were separately allocated, were also transferred to LANXESS GmbH in the context of the spin-offs.

Claims by LANXESS GmbH against Bayer Chemicals AG or against Bayer MaterialScience AG in relation to the nature or amount of the assets and liabilities transferred were excluded to the extent legally permissible.

The spin-offs from Bayer Chemicals AG and Bayer MaterialScience AG to LANXESS GmbH have had an effect on the liability of LANXESS GmbH (see ''*— Effects on Liability*'').

Consolidation of the Foreign Business

To the extent that foreign business activities had not already been transferred in the context of the spin-offs from Bayer Chemicals AG and Bayer MaterialScience AG to LANXESS GmbH, primarily due to different legal frameworks, the foreign chemicals and polymers business in the individual countries was transferred to LANXESS GmbH and its subsidiaries on the basis of applicable local law using different legal methods.

Where foreign companies were already engaged solely or predominantly in business activities allocable to LANXESS, such companies' shares were generally transferred to LANXESS GmbH or to one of its direct or indirect subsidiaries.

Otherwise, transfer generally took place by a multistep process. As a first step, the relevant chemicals and polymers activities were transferred to a country company assigned to LANXESS. Subsequently, the shares of the relevant country companies were transferred to LANXESS GmbH or one of its direct or indirect subsidiaries.

In other cases, LANXESS GmbH initially established a subsidiary, to which the relevant chemicals and polymers activities were subsequently transferred (as in France and the United States, for example). In certain cases, other configurations were chosen for legal and/or tax reasons.

The transfers of the foreign business were substantially effected as of or after 1 July 2004. Irrespective thereof, each of the parties has, from an economic perspective, as a rule adopted the same position as if the transfers had been effected as of 1 July 2004. At present, certain business activities have yet to be transferred (see ''*Risk Factors — Risks relating to the Spin-off and Strategic Realignment of LANXESS — Pending measures for the establishment of the LANXESS Group and actions in connection with the Spin-off*'').

Transfers from the Bayer Service Companies

Certain service-related operating units of the service companies Bayer Business Services GmbH, Bayer Industry Services GmbH & Co. OHG and Bayer Technology Services GmbH were transferred to LANXESS GmbH and its subsidiaries at the same time as the spin-offs from Bayer Chemicals AG and Bayer MaterialScience AG took effect. All of the transfers were carried out with economic effect as of 1 July 2004. Likewise, in various foreign countries, service functions were transferred to LANXESS companies.

LANXESS GmbH's Equity Interest in Bayer Industry Services GmbH & Co. OHG

With economic effect as of 1 July 2004, LANXESS GmbH acquired a 40% interest in Bayer Industry Services GmbH & Co. OHG against a cash contribution (see ''*Business Transactions and Legal Relationships with Related Parties — Business Transactions and Legal Relationships with the Bayer Group*'').

Land Purchase Agreement

Bayer AG and LANXESS GmbH entered into a land purchase agreement on 30 December 2004, pursuant to which LANXESS GmbH will acquire virtually all of the real property it currently uses in Germany as well as additional real properties in Germany (together with any fixtures and appurtenances) (regarding the land purchase agreement, see ''*Business Transactions and Legal Relationships with Related Parties — Business Transactions and Legal Relationships with the Bayer Group*''). Ownership of almost all of the foreign real properties used by LANXESS has been transferred to LANXESS.

Formation of the LANXESS Corporate Center

A separate, organisationally independent department has been established within the Corporate Center of Bayer AG. The principal management and control functions of the LANXESS Group are combined and administered within this department (''LANXESS Corporate Center''). As of 30 September 2004, a total of 56 employees worked at the LANXESS Corporate Center. The four members of LANXESS AG's Board of Management who also have contracts of employment with Bayer AG, which terminate upon the taking effect of the Spin-off, presently head the LANXESS Corporate Center.

Second Step — The Spin-off

After the combination of the chemicals and polymers activities in LANXESS GmbH and its direct and indirect subsidiaries, the separation from the Bayer Group will be consummated by way of a spin-off (*Abspaltung zur Aufnahme*) pursuant to section 123 (2) No. 1 UmwG. Pursuant to this provision, Bayer AG, as transferring entity, will transfer its entire equity interest in LANXESS GmbH and other portions of its assets and liabilities in their entirety to the acquiring entity, LANXESS AG. In return for the spin-off of the assets and liabilities to it, LANXESS AG, as acquiring entity, will issue shares in LANXESS AG to Bayer AG's stockholders.

In the course of the Spin-off, Bayer AG will essentially transfer the following assets and liabilities in their entirety to LANXESS AG:

- Bayer AG's entire equity interest in LANXESS GmbH;
- all 50,000 no-par bearer shares in LANXESS AG held by Bayer AG;
- all assets and liabilities, together with all rights and obligations, allocable to the LANXESS Corporate Center; and
- two loans receivable of Bayer AG in the total nominal amount of €100 million.

For purposes of implementing the Spin-off, Bayer AG and LANXESS AG entered into a notarised Spin-off and Acquisition Agreement on 22 September 2004. The Spin-off and Acquisition Agreement sets forth the details of the transfer of Bayer AG's above-mentioned assets and liabilities to LANXESS AG. The so-called spin-off balance sheet (*Abspaltungsbilanz*) appearing below was made an exhibit to this Spin-off and Acquisition Agreement. It solely serves to determine, and only shows, those assets and liabilities of Bayer AG that are part of the assets and liabilities to be spun off from Bayer AG pursuant to the Spin-off and Acquisition Agreement.

Spin-off Balance Sheet as of 1 July 2004

	(€)
ASSETS	
NONCURRENT ASSETS	
Property, Plant and Equipment	
Furniture, fixtures and other equipment	11,250.00
Investments	
Investments in affiliated companies	738,838,720.41
Other loans	69,845.19
	738,908,565.60
	738,919,815.60
CURRENT ASSETS	
Receivables from affiliated companies....	100,000,000.00
Other assets	36,050.00
	100,036,050.00
	838,955,865.60

	(€)
STOCKHOLDERS' EQUITY AND LIABILITIES	
STOCKHOLDERS' EQUITY	
Capital stock	73,034,192.00
Capital reserve	763,213,707.28
	836,247,899.28
PROVISIONS	
Provisions for pensions and other post-employment benefits...	2,023,433.00
Other provisions	684,533.32
	2,707,966.32
	838,955,865.60

The spin-off balance sheet was derived from the balance sheet of Bayer AG prepared as of 30 June 2004, 24:00 hours, which had been, within the framework of the spin-off, submitted to the Commercial Register as the so-called final balance sheet (*Schlussbilanz*) of the transferring entity in accordance with the provisions of German transformation law. As a result of its function, the spin-off balance sheet was neither the subject of an auditor's opinion nor subject to an auditor's review.

In accordance with the arrangement between the Company and Bayer AG contained in the Spin-off and Acquisition Agreement, the spin-off balance sheet contains only the value of the spun-off assets and liabilities that is, at the time the Spin-off takes effect, to be recognised in the Company's commercial accounts as of 1 July 2004, 0:00 hours. The capital stock existing immediately after the Spin-off takes effect is shown in the line item ''Capital stock'' under Stockholders' Equity. Any net assets contributed in excess of this amount were reported in ''Capital reserve'' in accordance with the arrangement in the Spin-off and Acquisition Agreement. The spin-off balance sheet does not make a statement about the net assets and financial position of the Company as of 1 July 2004, 0:00 hours, or any time thereafter.

Bayer AG and LANXESS AG entered into a so-called master agreement simultaneously with the Spin-off and Acquisition Agreement. Among the aims of the parties in concluding the master agreement were to ensure implementation of the combination of the chemicals and polymers activities in LANXESS GmbH and its subsidiaries and that certain minimum standards will be observed in such combination, conclusively determine the apportionment of liability as between the Bayer Group and the LANXESS Group in the areas of environment, antitrust and product liability, and establish certain reciprocal rules of conduct and duties of co-operation for the period after the Spin-off (regarding the master agreement and the other agreements concluded in connection with the Spin-off, see ''*Business Transactions and Legal Relationships with Related Parties — Business Transactions and Legal Relationships with the Bayer Group*'').

The Spin-Off and Acquisition Agreement became effective with the approval of the Stockholders' Meetings of Bayer AG and LANXESS AG on 17 November 2004 and on 21 December 2004, respectively. However, the Spin-off itself will only become effective once it is registered in the Commercial Register (*Handelsregister*) for Bayer AG at the Local Court of Cologne (*Amtsgericht*

Köln). LANXESS AG's Board of Management anticipates that the registration in the Commercial Register for Bayer AG will occur on 28 January 2005.

As between Bayer AG and LANXESS AG, the assets and liabilities to be spun off are to be transferred with economic effect as of 1 July 2004. As between Bayer AG and LANXESS AG, from that point onward, transactions pertaining to the assets and liabilities of Bayer AG that are to be spun off will be carried out for the account of LANXESS AG.

As part of the Spin-off, no-par bearer shares in LANXESS AG will be granted to the stockholders of Bayer AG at the time the Spin-off takes effect. In addition to shares issued in the context of an increase in LANXESS AG's capital, which was approved by the Stockholders' Meeting on 21 December 2004, for purposes of implementing the Spin-off, the 50,000 no-par bearer shares transferred by Bayer AG to LANXESS AG in the course of the Spin-off will also be issued to Bayer AG stockholders. The capital increase, which will cause LANXESS AG's current capital stock of €50,000.00 to increase by €72,984,192.00 to €73,034,192.00 and will involve issuing 72,984,192 no-par bearer shares, will occur against a contribution in kind consisting of the assets and liabilities to be spun off, *i.e.*, in particular, the equity interest in LANXESS GmbH. One LANXESS AG share will be issued for every ten Bayer AG shares (regarding the allotment procedure and fractional interest arrangement), see ''*Stock Exchange Listing — Allotment Procedure*'').

The Spin-Off and Acquisition Agreement, together with its annexes, was audited in draft form by the auditing firm Stüttgen & Haeb AG, Dusseldorf, which was appointed by the Regional Court of Cologne (*Landgericht Köln*) to act as the joint auditor for the Spin-off. The auditing firm Stüttgen & Haeb AG declared the following with respect to the audit results in the Spin-off audit report dated 20 September 2004:

''The draft Spin-Off Agreement prepared on September 20, 2004 contains the complete and accurate information required by § 126 German Transformation Act (*Umwandlungsgesetz*). In particular, the transferred assets and liabilities are clearly defined or definable in the draft Spin-Off Agreement and its appendices.

Given that all shares of LANXESS AG, Leverkusen, will be issued to the stockholders of Bayer AG, Leverkusen, company valuations are irrelevant for the determination of the subscription ratio. This being said, we confirm that we have no objections regarding the subscription ratio according to which the stockholders of Bayer AG will receive one registered no-par share of LANXESS AG in exchange for every 10 registered no-par shares of the Company.''

In the context of LANXESS AG's capital increase against contribution in kind carried out for purposes of implementing the Spin-off, an audit of the capital increase against contribution in kind was conducted. At the same time, a post-formation acquisition audit was conducted. Both audits were conducted by PwC Deutsche Revision Aktiengesellschaft, Wirtschaftsprüfung-sgesellschaft, Essen. In the report dated 30 November 2004 and prepared by PwC Deutsche Revision Aktiengesellschaft, Wirtschaftsprüfungsgesellschaft with respect to the audit of the capital increase against contribution in kind and with respect to the post-formation acquisition audit, both conducted at LANXESS Aktiengesellschaft, Leverkusen, PWC stated as follows with respect to the audit results:

''After concluding our duly-conducted audit pursuant to section 125 and section 67 UmwG (analogous), section 52(4) and section 34 AktG (analogous), sections 125 and 69 UmwG and sections 183(3) and 34 AktG on the basis of the certificates, books and writings, as well as the clarifications and backup material, provided to us, we confirm that the value of the contribution in kind to be made in connection with the Spin-off equals the minimum issuance amount of the shares to be issued in consideration therefor. The information contained in the report of the Supervisory Board with respect to the post-formation acquisition is accurate and complete. The value of the assets and liabilities to be acquired equals the amount of the consideration to be granted therefor.''

Bayer AG's closing balance sheet for the period ending 30 June 2004 was also audited by PwC Deutsche Revision Aktiengesellschaft, Wirtschaftsprüfungsgesellschaft, Essen, and was issued with an unqualified auditor's opinion.

The Company is responsible for the expenses incurred in connection with the implementation of the capital increase and amounting to approximately €100,000. Above and beyond this, Bayer is responsible for the expenses incurred in connection with the Spin-off and the external expenses, including the remuneration of the Global Coordinators, incurred in connection with the admission of the LANXESS shares to the stock exchange.

The Spin-off from Bayer AG to LANXESS AG will have an effect on the liability of LANXESS AG (see ''— *Effects on Liability*'').

General Works Agreement to Safeguard Sites and Employment III

In the context of the Spin-off of LANXESS, the Boards of Management or managing directors, as the case may be, of Bayer AG, Bayer HealthCare AG, Bayer CropScience AG, Bayer MaterialScience AG, Bayer Chemicals AG and the service companies Bayer Business Services GmbH, Bayer Technology Services GmbH and Bayer Industry Services GmbH & Co. OHG each concluded a largely identical so-called General Works Agreement to Safeguard Sites and Employment III (*Gesamtbetriebsvereinbarung für Standort- und Beschäftigungssicherung III*) (hereinafter referred to as ''SOS III'') with the Bayer general works council in June/July 2004. Among other things, SOS III generally precludes the dismissal of employees for operational reasons (*betriebsbedingte Beendigungskündigungen*) until 30 December 2007. Since SOS III continues to apply as a collective agreement, this preclusion applies to all employees of LANXESS AG and LANXESS GmbH.

Effects on Liability

The Spin-off will affect LANXESS AG's liability as follows:

Pursuant to section 133 (1) and (3) UmwG, LANXESS AG is jointly and severally liable for the fulfilment of obligations that remain incumbent upon Bayer AG and that existed before the Spin-off took effect, provided that such obligations mature within five years from the date of the announcement that the Spin-off has been registered in the Commercial Register for Bayer AG, and that claims against LANXESS AG based on such obligations are asserted as prescribed by law. Bayer AG and LANXESS AG have agreed as between themselves that Bayer AG will indemnify LANXESS AG against claims based on obligations incumbent upon Bayer AG.

Pursuant to sections 22, 125 and 133 UmwG, creditors of LANXESS AG may, within a period of six months after the Spin-off takes effect, demand collateral from the Company to secure their claims. This applies if the creditors are unable to obtain satisfaction of their claims at the respective time, give written notice of the grounds and quantum of their claims and provide credible evidence that the Spin-off jeopardises the satisfaction of their claims.

The spin-offs from Bayer Chemicals AG and Bayer MaterialScience AG to LANXESS GmbH will have the following effects on liability:

Pursuant to section 133(1) and (3) UmwG, LANXESS GmbH is jointly and severally liable for the fulfilment of obligations that remain incumbent upon Bayer Chemicals AG and Bayer MaterialScience AG and which existed before the respective spin-off took effect, provided that such obligations mature within five years from the date of the announcement that the respective spin-off has been registered in the Commercial Register for Bayer Chemicals AG or Bayer MaterialScience AG, as the case may be, and such obligations give rise to claims against LANXESS GmbH which are asserted in a lawsuit. Bayer Chemicals AG, Bayer MaterialScience AG and LANXESS GmbH have agreed that if LANXESS GmbH is sued on the basis of the obligations incumbent upon either of the other two companies, the relevant company will indemnify LANXESS GmbH.

Pursuant to sections 22, 125 and 133 UmwG, creditors of LANXESS GmbH may, within a period of six months after the announcement that the respective spin-off has been registered in the Commercial Register for Bayer Chemicals AG or Bayer MaterialScience AG, as the case may be, demand collateral from LANXESS GmbH in order to secure their claims. This applies if the creditors are unable to obtain satisfaction of their claims at the respective time, give written notice of the grounds and quantum of their claim, and provide credible evidence that the spin-off jeopardises the satisfaction of their claims.

Taxation in the Federal Republic of Germany

The following section contains a short summary of certain key German tax principles that may be or may become relevant with respect to the acquisition, holding or transfer of shares. This summary does not purport to be a comprehensive or exhaustive description of all German tax considerations that may be relevant to stockholders. The summary is based upon the domestic German tax laws in effect as of the date of the preparation of this Listing Memorandum and upon the double taxation treaties currently in force between Germany and other countries. Provisions in both areas may change, possibly with retroactive effect.

Prospective purchasers of the shares offered herein are advised to consult their tax advisors as to the tax consequences of the acquisition, holding and transfer of shares, and as to the procedures that must be followed to receive a refund of German withholding tax (*Kapitalertragsteuer*). Such tax advisors will be able also to appropriately consider the particular tax situation of each individual stockholder.

Taxation of the Company

Profits earned by German corporations, whether they are distributed or retained, are generally subject to a uniform corporate income tax (*Körperschaftsteuer*) at the rate of 25%, plus a solidarity surcharge (*Solidaritätszuschlag*) of 5.5% thereon (resulting in a total tax liability of approximately 26.4%).

95% of dividends or other profit shares received by the Company from domestic or foreign corporations are generally exempt from corporate income tax. The remaining 5% of such income is considered non-deductible operating expenses and, as such, are subject to corporate income tax (plus solidarity surcharge). The same applies to profits earned by the Company from the sale of shares in another domestic or foreign corporation.

In addition, German corporations are subject to trade tax (*Gewerbesteuer*) with respect to income from permanent business establishments in Germany. The effective rate of the trade tax depends on the local municipalities in which the Company maintains its permanent business establishments. Trade tax generally amounts to between approximately 15% and 25% of the trade tax base, depending on the local tax multiplier (*Hebesatz*) of the municipality. Trade tax qualifies as a deductible business expense for purposes of calculating the corporate income tax base and trade tax base.

Profit shares received from domestic or foreign corporations and capital gains from the sale of shares in other corporations generally are afforded the same treatment for trade tax purposes as for income tax purposes. Nevertheless, 95% of profit shares are tax-exempt only if the Company has held at least 10% of the capital stock of the distributing corporation at the beginning of the relevant tax assessment period. Additional limitations apply with respect to profit shares received from foreign corporations.

Effective 1 January 2004, tax losses carried forward for corporate and trade tax purposes, to the extent these exceed €1 million, may only be set off against up to 60% of taxable income. Tax loss carry forwards that are not utilised may be carried forward indefinitely and can generally neutralise future taxable income subject to the above-mentioned 60% limit. This provision already applies to LANXESS for fiscal year 2004.

Taxation of Stockholders

Stockholders are taxed in connection with the holding of shares (taxation of dividends), the sale of shares (taxation of capital gains) and the royalty-free transfer of shares (estate and gift tax).

Taxation of Dividends

Dividend withholding tax

The Company must generally withhold and remit to German tax authorities, for the account of its stockholders, a withholding tax (*Kapitalertragsteuer*) in the amount of 20% on dividends distributed by the Company, plus a solidarity surcharge of 5.5% on the amount of the withholding tax (a total of 21.1%). The withholding tax base is the amount of dividends approved for distribution by the Company's Stockholders' Meeting.

Withholding tax is generally withheld regardless of whether and, if so, to what extent dividends are tax-exempt at the level of the stockholder and regardless of whether the stockholder is a resident or non-resident of Germany.

Where dividends are distributed to a company domiciled in another member state of the European Union within the meaning of Article 2 of the so-called Parent-Subsidiary Directive (EC Directive 90/435/EEC of the Council dated 23 July 1990), the withholding of the withholding tax may be waived entirely upon application, provided that additional requirements are met. This also applies to dividends distributed to a permanent business establishment located in another European Union member state of such a parent company or of a parent company that is a tax resident of Germany.

The withholding tax rate for distributions to non-resident stockholders is reduced in accordance with the applicable double taxation treaty, if any, between Germany and the stockholder's country of residence, provided that the stockholder's shares are not held as assets of a permanent German business establishment or fixed base in Germany or as business assets for which a permanent representative in Germany has been appointed. The withholding tax is generally reduced by refunding to non-resident stockholders, upon application to the German tax authorities (Bundesamt für Finanzen, Friedhofstrasse 1, 53225 Bonn), the difference between the total amount withheld, including solidarity surcharge, and the amount of withholding tax actually owed under the applicable double taxation treaty (generally 15%). Forms for the refund procedure may be obtained from the Bundesamt für Finanzen (www.bff-online.de) or the German embassies or consulates.

Resident stockholders

If a stockholder (natural person or corporation) is a tax resident of Germany (*i.e.*, a person or a corporation whose residence, habitual abode, registered domicile or place of management is located in Germany), any withholding tax (including solidarity surcharge) withheld and remitted to the German tax authorities by the Company will be credited against the stockholder's personal income or corporate income tax liability or, if the withholding tax exceeds the amount of the stockholder's personal income or corporate income tax liability, is refunded to the stockholder in the amount of the overpayment.

If a natural person who is a tax resident of Germany holds shares as non-business (private) assets, 50% of all dividends are included in taxable investment income (the so-called ''half-income method''). These taxable dividends are subject to a progressive income tax rate (up to 42% beginning in 2005), plus a 5.5% solidarity surcharge thereon (assuming that the maximum tax rate of 42% applies, the total tax liability would be approximately 44.3%). Only one half of the expenses economically connected with these dividends are tax-deductible. Certain Company dividend distributions, which are deemed a repayment of capital for tax purposes, are not subject to dividend tax at the stockholder level, but may be taxable as capital gains. This could apply, for example, to future distributions of capital reserves by the Company.

Natural persons who hold shares as non-business (private) assets are entitled to a so-called ''savers' exemption'' (*Sparerfreibetrag*) in the amount of €1,370.00 (or €2,740.00 for married couples filing jointly) per calendar year with respect to their investment income. In addition, such persons are entitled to a blanket deduction in the amount of €51.00 (or €102.00 for married couples filing jointly) for income-producing expenses (*Werbungskostenpauschale*), unless proof of higher income-producing expenses is furnished. 50% of the stockholder's dividends and other investment income are subject to taxation only if and to the extent they exceed the savers' exemption after deduction of actual income-producing expenses (in the case of dividends, only a 50% deduction applies) or the blanket deduction for income-producing expenses.

If the shares are held as business assets, taxation depends upon whether the stockholder is a corporation, sole proprietor or partnership.

(i) Subject to certain exceptions for companies in the finance and insurance industry, generally 95% of dividends received by resident corporations are exempt from corporate income tax and the solidarity surcharge, while the remaining 5% of dividends are considered non-deductible business expenses and, as such, are subject to corporate income tax (plus solidarity surcharge). Moreover, actual business expenses directly related to the dividends are deductible. No minimum equity interest limit or minimum holding period applies. However, the full amount of any dividends remaining after deduction of business expenses economically connected with the dividends is subject to trade tax, unless the corporation held at least 10% of the Company's capital stock as of the beginning of the relevant tax assessment period.

(ii) If the shares are held as business assets of a sole proprietor, 50% of dividends are considered income for purposes of calculating the stockholder's corporate income tax liability. Only 50% of business expenses economically connected with the dividends are tax-deductible. If the shares are held by a permanent business establishment maintained in Germany by a trade or business, dividends are also subject to trade tax in the full amount, unless the taxpayer held at least 10% of the Company's capital stock as of the beginning of the relevant tax assessment period. Trade tax is generally credited against the stockholder's personal income tax liability in accordance with a blanket tax credit method.

(iii) If the stockholder is a partnership, personal income tax or corporate income tax is assessed only at the level of each partner. Taxation of each partner depends upon whether the partner is a corporation or natural person: if the partner is a corporation, 95% of dividends are generally tax-exempt (see subparagraph (i) above). If the partner is a natural person, 50% of dividends are subject to personal income tax, plus solidarity surcharge (see subparagraph (ii) above). If the shares are held by a permanent business establishment maintained in Germany by a trade or business of the partnership, the dividends are subject to trade tax at the level of the partnership. The personal income tax and corporate income tax exemptions described above — 95% exemption on dividends for corporations, 50% exemption on dividends for natural persons — apply here accordingly if the partnership held at least 10% of the Company's capital stock at the beginning of the relevant tax assessment period. Otherwise, the dividends are subject to trade tax in the full amount. If the partner is a natural person, then the trade tax paid by the partnership is generally credited against the partner's personal income tax liability in the form of a blanket tax credit.

Non-resident stockholders

If a stockholder (natural person or corporation) who is subject to non-resident taxation in Germany holds shares as business assets of a permanent German business establishment or fixed base in Germany or as business assets for which a permanent representative in Germany has been appointed, withholding tax (including solidarity surcharge) withheld and remitted to the German tax authorities by the Company is credited against the stockholder's personal income or corporate income tax liability or, if the withholding tax exceeds the amount of the stockholder's personal income or corporate income tax liability, is refunded to the stockholder in the amount of the overpayment. In all other cases, the withholding of withholding tax discharges any tax liability of the stockholder in Germany. A tax refund will be paid only if a double taxation treaty applies and if the dividends are distributed to a company domiciled in a member state of the European Union within the meaning of Article 2 of the so-called Parent-Subsidiary Directive (EC Directive 90/435/EEC of the Council dated 23 July 1990), or to a permanent business establishment located in another European Union member state of such a parent company or of a parent company which is a tax resident of Germany.

If the shares are held by a natural person as business assets of a permanent German business establishment or fixed base in Germany or as business assets for which a permanent representative in Germany has been appointed, 50% of dividends received by the stockholder are subject to German income tax, plus solidarity surcharge. If the shares are held as assets of a permanent business establishment maintained by a trade or business in Germany, dividends are also generally subject to trade tax in the full amount after deduction of any business expenses economically connected with the dividends, unless the taxpayer held at least 10% of the

Company's capital stock at the beginning of the relevant tax assessment period. Trade tax paid is generally credited against the stockholder's personal income tax liability in the form of a blanket tax credit.

Subject to certain exceptions for companies in the finance and insurance industry, generally 95% of dividends received by foreign corporations subject to non-resident taxation in Germany are exempt from corporate income tax and the solidarity surcharge, while the remaining 5% of dividends are considered non-deductible business expenses and, as such, are subject to corporate income tax (plus solidarity surcharge). If the shares are held as assets of a permanent business establishment in Germany, dividends are also subject to trade tax after deduction of any business expenses economically connected with the dividends, unless the corporation held at least 10% of the Company's capital stock at the beginning of the relevant tax assessment period.

Taxation of Capital Gains

Resident stockholders

Capital gains from the sale of shares held as non-business (private) assets by a natural person who is a tax resident of Germany are generally subject to income tax plus solidarity surcharge, if the shares are sold within one year of the date of acquisition. The tax base is generally 50% of the capital gains. Capital gains are not taxed if, in combination with other profits from personal sales transactions in the same calendar year, they total less than €512.00. Losses from the sale of shares may be offset only by gains from personal sales transactions in the same calendar year or, absent such gains, by gains from personal sales transactions in the previous year or subsequent years if certain requirements are met.

If the shares are held as non-business (private) assets of a natural person who is a tax resident of Germany, 50% of capital gains from the sale of shares are subject to taxation based upon the applicable individual income tax rate, plus a solidarity surcharge in the amount of 5.5% thereon, even after expiry of the above-mentioned one-year period, if the natural person or, in the event of a royalty-free transfer, the natural person's legal predecessor or, in the event of several successive royalty-free transfers, any legal predecessor of the natural person, has, at any point during the five years immediately preceding the transfer, held a direct or indirect interest in the Company of at least 1%. Generally, only 50% of the losses from the sale of shares and 50% of expenses economically connected with such sale may be claimed as tax deductions.

If the shares are held as business assets, then taxation depends upon whether the stockholder is a corporation, sole proprietor, or partnership.

(i) Subject to certain exceptions for companies in the finance and insurance industry, 95% of capital gains earned by taxpayers subject to corporate income tax are generally, irrespective of the amount and holding period of the investment, exempt from corporate income and trade tax (including solidarity surcharge), while the remaining 5% of capital gains are considered non-deductible business expenses and, as such, are subject to corporate income tax (plus solidarity surcharge) and trade tax. Losses from the sale of shares or any other reductions of profits related to the sold shares generally do not qualify as tax-deductible business expenses.

(ii) If the shares are held as business assets of a sole proprietor who is a resident of Germany for tax purposes, any capital gains are subject to income tax and the solidarity surcharge, and, if the shares are held as assets of a permanent business establishment maintained in Germany by a trade or business, are also subject to trade tax, regardless of whether the shares are sold within one year of the date of acquisition and regardless of whether the seller or, in the event of a royalty-free transfer, any of the seller's legal predecessors held an interest in the Company of at least 1%. The tax base is 50% of the capital gains from the sale of shares. Generally, only 50% of losses from the sale of shares and 50% of expenses economically connected therewith may be claimed as tax deductions where applicable. Trade tax is, in general, credited against the stockholder's personal income tax liability in accordance with a blanket tax credit method. Provided that certain requirements are satisfied, capital gains from the sale of shares in corporations may, for a limited period of time, be deducted from the acquisition costs of certain other assets up to the amount of €500,000.00.

(iii) If the stockholder is a partnership, personal income tax or corporate income tax is assessed only at the level of each partner. Taxation depends upon whether the partner is a corporation or natural person: if the partner is a corporation, 95% of capital gains are, in general, tax-exempt (see subparagraph (i) above). If the partner is a natural person, 50% of capital gains are subject to income tax, plus solidarity surcharge (see subparagraph (ii) above). If the shares are held as assets of a permanent business establishment maintained in Germany by a trade or business of the partnership, capital gains from the sale of shares are subject to trade tax at the level of the partnership. The personal income tax and corporate income tax exemptions described above (only 50% tax basis for capital gains from the sale of shares or 95% capital gains exemption) also apply accordingly for purposes of trade tax if the partnership is owned by natural persons or corporations. If the partner is a natural person, the trade tax apportionable to that partner and paid by the partnership is generally credited against the partner's personal income tax liability in accordance with a blanket tax credit method.

Non-resident stockholders

If the shares are sold by a natural person who resides abroad but is subject to non-resident taxation in Germany and if (i) such natural person holds the shares as business assets of a permanent German business establishment or fixed base in Germany or as business assets for which a permanent representative in Germany has been appointed or (ii) such natural person or, in the event of a royalty-free transfer of the shares, his or her legal predecessor held, at any point during the five years immediately preceding the sale of the shares, a direct or indirect interest of at least 1% in the Company, 50% of capital gains will be subject to German income tax, plus a 5.5% solidarity surcharge thereon, and, if the shares are held as assets of a permanent business establishment maintained in Germany by a trade or business, 50% of capital gains will also be subject to trade tax. However, except in (i) above, most double taxation treaties provide for full exemption from German taxation.

Subject to certain exceptions for companies in the finance and insurance industry, 95% of capital gains earned by foreign corporations subject to non-resident taxation in Germany are generally exempt from trade and corporate income tax, while the remaining 5% of capital gains are considered non-deductible business expenses and, as such, are subject to corporate income tax (plus solidarity surcharge). Losses from the sale of shares or other reductions of profits related to the sold shares generally do not qualify as tax-deductible business expenses.

Special treatment of companies in the financial and insurance industry as stockholders

If financial institutions or financial services providers, including those domiciled in another member state of the European Community or another contracting state to the EEA Agreement, hold or sell shares which are allocable to the trading book (*Handelsbuch*) pursuant to section 1 (12) of the German Banking Act (*Kreditwesengesetz*), neither the dividends nor capital gains will be subject to the half-income method or the 95% exemption from corporate income tax and from any applicable trade tax, unless the dividends are accorded favourable tax treatment under the so-called Parent-Subsidiary Directive (EC Directive 90/435/EEC of the Council dated 23 July 1990). The foregoing sentence also applies correspondingly to shares, which are acquired by a financial enterprise within the meaning of the German Banking Act for purposes of realising short-term gains from proprietary trading, and to shares, which life insurance or health insurance companies would classify as a capital investment or which are held by pension funds.

Estate and Gift Tax

The transfer of shares to another person by gift or *causa mortis* is generally subject to German estate or gift tax only if:

(i) the decedent, donor, heir, donee or any other transferee maintained a residence or had his or her habitual abode in Germany at the time of the transfer, or is a German citizen who had spent no more than five consecutive years outside Germany without maintaining a residence in Germany; or

(ii) the shares were held by the decedent or donor as business assets for which a permanent business establishment was maintained in Germany or for which a permanent representative in Germany was appointed; or

(iii) the decedent or donor, either individually or collectively with related parties, held, directly or indirectly, at least 10% of the Company's capital stock at the time of the inheritance or gift.

The few German double estate tax treaties currently in force usually provide that German estate or gift tax may be assessed only in the cases described in subparagraph (i) and, subject to some limitations, subparagraph (ii).

Special rules apply to certain German citizens who neither maintain a residence nor have their habitual abode in Germany.

Other Taxes

No German transfer tax, value-added tax, stamp duty or similar taxes are assessed on the purchase, sale or other transfer of shares. In certain circumstances it is possible, however, that business owners may opt for the payment of value-added tax on transactions that are otherwise tax-exempt. No net wealth tax or trade tax on capital is currently assessed in Germany.

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Financial Section

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Combined Financial Statements (IFRS) of the LANXESS Group for the Fiscal Year 2003

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LANXESS Subgroup
Combined Statements of Income

	Note	Dec. 31, 2002	Dec. 31, 2003
		(in € millions)	
Net sales	(1)	6,763	6,315
Cost of goods sold		(5,285)	(5,211)
Gross profit		1,478	1,104
Selling expenses		(985)	(935)
Research and development expenses	(2)	(149)	(168)
General and administrative expenses		(202)	(257)
Other operating income	(3)	76	57
Other operating expenses	(4)	(337)	(1,098)
Operating Result (EBIT)	(5)	(119)	(1,297)
Income (expense) from investments in affiliated companies — net	(6)	0	(15)
Interest expense — net	(7)	(71)	(54)
Other non-operating expenses — net	(8)	(18)	(42)
Non-operating result		(89)	(111)
Income (loss) before income taxes		(208)	(1,408)
Income taxes	(9)	90	412
Income (loss) after taxes		(118)	(996)
Minority stockholders' interest	(11)	(1)	(1)
Net income (loss)		(119)	(997)
Earnings per share (€)	(12)	(1.63)	(13.65)
Diluted earnings per share (€)	(12)	(1.63)	(13.65)

LANXESS Subgroup
Combined Balance Sheets

	Note	Dec. 31, 2002	Dec. 31, 2003
		(in € millions)	
ASSETS			
Noncurrent assets			
Intangible assets	(16)	379	99
Property, plant and equipment	(17)	2,575	1,551
Investments	(18)	67	40
		3,021	1,690
Current assets			
Inventories	(19)	1,094	1,096
Receivables and other assets			
Trade accounts receivable	(20)	1,048	990
Short-term loans	(21)	182	256
Other receivables and other assets	(21)	217	298
		1,447	1,544
Marketable securities and other instruments		0	0
Cash and cash equivalents		10	13
Liquid assets	(22)	10	13
		2,551	2,653
Deferred taxes	(9)	25	170
Deferred charges	(23)	22	18
Total assets		5,619	4,531
STOCKHOLDERS' EQUITY AND LIABILITIES			
Stockholders' equity			
Capital		2,848	2,729
Net income (loss)		(119)	(997)
Currency translation adjustment		(264)	(374)
Miscellaneous items		0	0
	(24)	2,465	1,358
Minority stockholders' interest	(25)	39	43
Liabilities			
Long-term liabilities			
Long-term financial obligations	(28)	446	209
Miscellaneous long-term liabilities	(30)	1	1
Provisions for pensions and other post-employment benefits	(26)	324	408
Other long-term provisions	(27)	171	252
		942	870
Short-term liabilities			
Short-term financial obligations	(28)	974	1.233
Trade accounts payable	(29)	428	574
Miscellaneous short-term liabilities	(30)	212	187
Short-term provisions	(27)	193	153
		1,807	2,147
		2,749	3,017
Deferred taxes	(9)	310	57
Deferred income	(32)	56	56
Total stockholders' equity and liabilities		5,619	4,531

LANXESS Subgroup
Combined Statements of Changes in Stockholders' Equity

	Capital	Net income (loss)	Currency translation adjustment	Miscellaneous items	Total
			(in € millions)		
December 31, 2001	2,848	0	(158)	0	2,690
Dividend payments					0
Allocation to retained earnings					0
Exchange differences			(106)		(106)
Other differences					0
Net income (loss)		(119)			(119)
December 31, 2002	2,848	(119)	(264)	0	2,465
December 31, 2002	2,848	(119)	(264)	0	2,465
Dividend payments					0
Allocation to retained earnings	(119)	119			0
Exchange differences			(110)		(110)
Other differences					0
Net income (loss)		(997)			(997)
December 31, 2003	2,729	(997)	(374)	0	1,358

LANXESS Subgroup
Combined Statements of Cash Flows*

	Note	2002	2003
		(in € millions)	
Operating result (EBIT)		(119)	(1,297)
Income taxes		(70)	12
Depreciation and amortization		626	1,477
Change in provisions for pensions and other post employment benefits		(20)	25
Losses on retirements of noncurrent assets		6	6
Gross cash provided by operating activities		423	223
Increase in inventories		(77)	(55)
Decrease in trade accounts receivable		43	29
Increase in trade accounts payable		130	42
Changes in other working capital		(150)	107
Net cash provided by operating activities	(36)	369	346
Cash outflows for additions to property, plant and equipment		(393)	(312)
Cash inflows from sales of property, plant and equipment		62	65
Cash outflows for investments		(21)	(58)
Cash outflows for acquisitions less acquired cash		0	0
Interest and dividends received		5	5
Net cash inflow (outflow) from marketable securities		0	0
Net cash provided by (used in) investing activities	(37)	(347)	(300)
Changes in stockholders' equity		0	0
Issuances of debt		171	159
Retirements of debt		(120)	(136)
Interest paid		(76)	(69)
Net cash provided by (used in) financing activities	(38)	(25)	(46)
Change in cash and cash equivalents due to business activities		(3)	0
Cash and cash equivalents at beginning of year		13	10
Change in cash and cash equivalents due to changes in scope of consolidation		0	3
Change in cash and cash equivalents due to exchange rate movements		0	0
Cash and cash equivalents at end of year	(39)	10	13
Marketable securities and other instruments		0	0
Liquid assets as per balance sheets		10	13

* In the 2002 Combined Financial Statements contained in the Joint Spin-off Report, a portion of property, plant and equipment already existing as of January 1, 2002 was erroneously reported as additions, thus leading to an error amounting to €94 million in the presentation of 2002 capital expenditures and amounting to €40 million in the presentation of 2002 depreciation and write-downs of property, plant and equipment. This technical error was corrected in the 2002 Combined Financial Statements and did not have an effect on either the 2002 balance sheet and income statement, or on the financial data and financial reports for subsequent periods. The correction of this error led most importantly to a decrease of €40 million in net cash provided by operating activities, a decrease of €94 million in net cash used in investing activities and a decrease of €54 million in net cash provided by (used in) financing activities. Segment data were changed accordingly.

Notes Subgroup LANXESS

Key Data by Segment and Region

Key Data by Segments

Segments	Chemical Intermediates 2002	Chemical Intermediates 2003	Performance Chemicals 2002	Performance Chemicals 2003	Engineering Plastics 2002	Engineering Plastics 2003	Performance Rubber 2002	Performance Rubber 2003	Reconciliation 2002	Reconciliation 2003	LANXESS 2002	LANXESS 2003
	(in € millions)											
Net sales	1,447	1,411	2,055	1,925	1,504	1,401	1,484	1,375	273	203	6,763	6,315
Intersegment sales	105	88	11	7	2	1	1	2	(119)	(98)		
Operating result (EBIT)	5	(344)	67	(176)	(146)	(488)	(2)	(246)	(43)	(43)	(119)	(1,297)
Net cash flow	85	203	98	92	102	80	131	24	(47)	(53)	369	346
Total assets	1,220	900	1,391	1,148	1,353	1,051	1,305	1,030	350	402	5,619	4,531
Capital expenditures	141	79	102	63	72	85	78	78		7	393	312
Amortization and depreciation	149	463	129	272	171	474	163	250	14	18	626	1,477
Liabilities	195	230	353	419	294	348	294	349	1,979	1,784	3,115	3,130
Number of employees (as of Dec. 31)	4,265	4,059	5,129	4,881	3,844	3,658	3,151	2,999	5,071	4,826	21,460	20,423

Key Data by Regions

Regions	Europe 2002	Europe 2003	North America 2002	North America 2003	Asia/Pacific 2002	Asia/Pacific 2003	Latin America/Africa/Middle East 2002	Latin America/Africa/Middle East 2003	Reconciliation 2002	Reconciliation 2003	LANXESS 2002	LANXESS 2003
	(in € millions)											
Net sales by market	3,606	3,565	1,567	1,346	1,019	887	571	517			6,763	6,315
Total assets	3,522	2,977	1,441	879	353	266	189	181	114	228	5,619	4,531
Capital expenditures	289	242	82	47	14	19	8	4			393	312

History of the Spin-off and Spin-off Process

In November 2003, the Board of Management and the Supervisory Board of Bayer AG resolved to demerge major portions of the Bayer Group's chemical and polymer activities, which have since been combined into the LANXESS Subgroup, one demerger option being to transfer the activities concerned to LANXESS AG by way of a spin-off (*Abspaltung zur Aufnahme*) pursuant to the German Transformation Act (*Umwandlungsgesetz*). In July 2004, Bayer's Board of Management decided to pursue the demerger by way of a spin-off. Accordingly, BAYER AG and LANXESS AG intend to enter into a Spin-Off and Acquisition Agreement in September 2004, a draft of which is currently available. This agreement, in order to become effective, must be approved by the stockholders' meetings of both BAYER AG and LANXESS AG.

In contrast to the remaining core business lines of the Bayer Group, the LANXESS portfolio consists primarily of products that have reached a high level of maturity in the market and are therefore exposed to lower barriers to market entry and growth rates. Generally lower margins require the creation of lean management structures with low complexity and a commitment to optimizing equipment and processes. The Board of Management of Bayer AG believes that the spin-off will form the basis for a greater commitment to implementing the necessary courses of action more consistently and establishing optimized structures and processes to account for the special needs of the chemical and polymer activities.

The spin-off of the Bayer Group's chemical and polymer activities, which have been combined in the LANXESS Subgroup, will be conducted in two steps. In a first, preparatory step, the Bayer Group's chemical and polymer activities have been or will be transferred to LANXESS Deutschland GmbH (a wholly-owned subsidiary of BAYER AG) and its subsidiaries. The second step will consist of transferring Bayer AG's shares in LANXESS Deutschland GmbH to LANXESS AG by way of a spin-off pursuant to the German Transformation Act. As between Bayer AG and LANXESS AG, the transfer of the assets subject to spin-off is intended to take economic effect as of July 1, 2004. The spin-off will become legally effective once it has been registered in the commercial register for Bayer AG. As consideration for the transfer, LANXESS AG will grant shares to the stockholders of BAYER AG. These LANXESS AG shares are to be admitted to the official market (*amtlicher Markt*) of the Frankfurt Stock Exchange in Germany with a simultaneous admission to the Prime Standard segment of the official market. Chapter III of the Joint Spin-Off Report prepared by the Boards of Management of both Bayer AG and LANXESS AG contains a description of the spin-off process and a detailed explanation of the reasons for the spinoff. A draft of the Joint Spin-Off Report is available for review.

Corporate Structure and Segmentation

The Bayer Group's chemical and polymer activities that have been combined in the LANXESS Subgroup primarily consist of independently managed strategic business units of the Bayer Group. They specifically include the operations of the former Bayer Chemicals subgroup, with the exception of H.C. Starck GmbH and Wolff Walsrode AG, as well as the polymer business units Rubber Chemicals, Semi-Crystalline Products, Styrenics, BR/Butyl, Technical Rubber Products and Fibers. The ''Blends'' reporting unit within the ''Styrenics'' business unit will not be transferred, but will remain part of the Bayer Group. The equity investments held by Bayer Chemicals AG in DyStar Holding Inc., DyStar Textilfarben GmbH, GE Bayer Silicones GmbH & Co. KG and GE Bayer Silicones Verwaltungs-GmbH, which are reported ''at equity'' in Bayer's consolidated financial statements, have not been included in the chemical and polymer activities combined within the LANXESS Subgroup.

Also included in the LANXESS Subgroup, apart from the operating units assigned to it, are certain cross-subgroup service functions and a self-contained organizational unit of the Bayer Corporate Center comprising functions that perform services for the polymer and chemical businesses.

The principal transfers from Bayer Business Services GmbH consisted of parts of the following functions: Business Consulting, Development of IT-based Systems, Development and Support of Research Systems, Procurement, Law and Patent Services, and HR Recruiting Services. The plant-related Engineering and Maintenance Services department was transferred from Bayer Industry Services GmbH & Co. OHG, and sections of the Engineering, Plant Management, Process Engineering, Construction Management and Construction Planning departments were transferred from Bayer Technology Services GmbH. In addition, certain accounting services attributable to the LANXESS Subgroup were transferred from Euroservices Bayer GmbH, a subsidiary of Bayer Business Services GmbH. Service functions in various foreign countries were also transferred to the LANXESS Subgroup.

The LANXESS Subgroup consists of 17 operating business units which, based on their operational management and internal reporting structures, are grouped into the four segments Performance Chemicals, Chemical Intermediates, Performance Rubber and Engineering Plastics in accordance with the requirements of IFRS. For the sake of comparison, the following diagram shows the future reporting structure of the LANXESS Group with respect to the activities to be transferred, compared with the existing reporting structure of the Bayer Group.

Reporting structure in 2003		Reporting structure in 2004 — SG/Segment	LANXESS			
SG	Segments	Reporting Groups / Business areas (after the spin-off: segments)	Chemical Intermediates	Performance Chemicals	Engineering Plastics	Performance Rubber
Polymers	Plastics/Rubber	Thermoplastic Polymers			Semi-Crystalline Products, Styrenics ABS/SAN) (new: Styrenic Resins)	
Polymers	Plastics/Rubber	Rubber Polymers		Rubber Chemicals (new: Rubber Chemicals and RheinChemie)		BR/Butyl (new: Polybutadiene Rubber, Butyl Rubber), Technical Rubber Products
Polymers	Polyurethane/Coating Materials/Fibers	Coating Materials / Fibers			Fibers	
Chemicals	Chemicals	Industrial Chemicals	Basic Chemicals, Inorganic Pigments	Ionic Exchange Resins		
Chemicals	Chemicals	Custom Manufacturing	Fine Chemicals			
Chemicals	Chemicals	Functional Chemicals		Functional Chemicals (new: Material Protection Products and Functional Chemicals)		
Chemicals	Chemicals	Process Chemicals		Textile Processing Chemicals, Leather, Paper		

Chapter IV of the Joint Spin-Off Report provides a detailed description of the business activities of the LANXESS Subgroup. A draft version of the Joint Spin-Off Report is available for review.

Basis for Financial Statement Reporting

As the Bayer Group did not prepare separate financial statements for the business activities of the LANXESS Subgroup prior to the spin-off and the LANXESS Subgroup did not previously constitute an independent reporting unit, the so-called combined financial statements (hereinafter ''Combined Financial Statements'') of the LANXESS Subgroup for the years 2002 and 2003 have been derived from the consolidated accounts of the Bayer Group. The relevant terms in the agreements concluded for the purpose of establishing the LANXESS Subgroup prescribe which business activities are to be allocated to the LANXESS Subgroup. The assets and liabilities to be transferred to the LANXESS Subgroup were recognized and valued in the Combined Financial Statements in accordance with the standards issued by the International

Accounting Standards Board (''IASB''), London, in effect as of the closing date of the financial statements.

The purpose of the Combined Financial Statements is to reflect the business activities to be spun-off as if the LANXESS Subgroup had already existed in the structure defined for the spin-off. Accordingly, the business activities to be spun off were assumed to have been included in the LANXESS Subgroup for all periods presented, and the financial statements for 2002 and 2003 reflect the assets and liabilities (including income and expenses) which were necessary to conduct these business activities or which were incurred in connection therewith. In this respect, central costs that were not historically allocated to the business units being transferred, but were incurred in connection with the activities of these business units, have been reflected in the Combined Financial Statements. This was also the case for the services provided by BAYER AG's Corporate Center, which housed departments with management and control functions for the LANXESS Subgroup, such as the Board Office, Corporate Development, Industrial & Environmental Affairs, Treasury, Tax, Corporate Controlling, Accounting, Communications, Law & Patents and Human Resources. For this purpose, expenses amounting to € 26 million in 2002 and € 24 million in 2003 were recorded in the Combined Financial Statements. These expenses are based on the LANXESS Subgroup's *pro rata* share of historical costs.

In preparing the Combined Financial Statements, assumptions and projections must be made that have an effect on the amounts and presentation of assets and liabilities, income and expenses and contingent liabilities. Actual results could differ from the estimates. The Combined Financial Statements published here therefore do not necessarily reflect the financial condition and results of operations that would have resulted had the LANXESS Subgroup already existed as an independent group as of January 1, 2002 and the underlying transactions between the LANXESS and Bayer companies had thus been entered into between independent companies. For the reasons set forth herein, the absence of historical unity and independence of the LANXESS Subgroup limits the informative value of the Combined Financial Statements. Therefore, the Combined Financial Statements do not enable reliable forecasts concerning the future development of the businesses combined in the LANXESS Subgroup.

Preparation of the Combined Financial Statements

In principle, the demarcation of the business to be transferred is based on the consolidated reporting structures and, therefore, the reporting units underlying those structures. For this reason, diverging allocations of individual products below this level are not taken into account. However, these deviations are the exception and would, based on current knowledge, not, in the aggregate, result in any materially different statements for the LANXESS Subgroup.

The financial statements of the entities included in the Combined Financial Statements were prepared based on uniform accounting and valuation principles. Values assigned on the basis of tax regulations are not incorporated in the Combined Financial Statements. The statements of the individual consolidated companies were prepared as of the same closing dates as the Combined Financial Statements. The amounts shown in the Combined Financial Statements are in millions of euros (€ in millions). The income statement was prepared using the cost-of-sales method. Individual items have been grouped together in the income statement and balance sheet for the sake of clarity, as explained in the notes. According to IAS 1 (Presentation of Financial Statements), a distinction is made in the balance sheet between long-term and short-term liabilities. Liabilities and provisions are deemed to be short-term if they mature within one year. Income taxes were generally assigned to each reported period on the basis of the respective contributions of the business divisions of the LANXESS Subgroup to be transferred to the results of the LANXESS Subgroup. In the future, the actual tax position of the LANXESS Group will depend on the legal structure and tax strategies of the LANXESS Group as an independent company.

The Combined Financial Statements include all business activities of existing legal entities (share deals) as well as individual groups of assets and liabilities to be transferred (asset deals), including the services to be transferred.

Business Activities of Existing Legal Entities (Share Deals)

The Combined Financial Statements include 34 companies that were exclusively engaged in LANXESS-related business. The shares in these companies have already been or will be transferred to LANXESS Deutschland GmbH or to one of its direct or indirect subsidiaries. Each of these companies was included in the Combined Financial Statements on the basis of its historical financial statements for the years 2002 and 2003. Accordingly, only intra-group transactions between the remaining part of the Bayer Group and the LANXESS Subgroup were examined and, if necessary, reclassified.

Four other companies, which primarily operate businesses allocable to the LANXESS Subgroup, were also included in the Combined Financial Statements on the basis of their historical financial statements, however, the business units or business activities originally contained in these companies which were allocable to the remaining part of the Bayer Group were transferred to a new or existing Bayer company.

Business Activities to be Transferred (Asset Deals)

In the case of an additional 28 companies, which were primarily engaged in business activities that were to remain with the Bayer Group, but whose LANXESS-related business was to be transferred to legally independent units, the respective individual assets were removed from the existing companies in order to reflect the LANXESS-related business. In this respect, the fact that transactions with business units remaining within the Bayer Group now had to be reported as transactions with third parties was specifically taken into account. To this end, separate financial statements were prepared for the business units to be transferred, and then included in the Combined Financial Statements.

The classification of assets and liabilities necessitated by this treatment was based on the following criteria. As a general rule, the assets and liabilities to be transferred pursuant to the relevant agreements were allocated to the various operating activities on the basis of use (assets) or accountability (liabilities). With respect to non-current and current assets, which will not be legally transferred to the LANXESS Subgroup but are nevertheless necessary for the LANXESS Subgroup's business operations to continue, the necessary utilization rights will be granted to the LANXESS Subgroup. Where assets transferred to the LANXESS Subgroup are required in order to continue the business activities remaining with the Bayer Group, the LANXESS Subgroup will grant the Bayer Group the necessary utilization rights; this particularly relates to shared land and buildings.

Liabilities relating to individual business units (such as trade accounts payable, advance payments and debt instruments) were generally allocated on the accountability principle, *i.e.*, liabilities were allocated to the business units in which they arose. Generally, provisions, including reserves for environmental matters and restructuring measures, were also recognized on the basis of accountability. This also applies to provisions for environmental matters and restructuring measures. For pensions and similar obligations, see the section ''*Pensions and other post-employment benefits*'' below. Financial obligations were assigned in the manner described in ''*Capital Structure*''.

Tax receivables and liabilities assessed prior to the spin-off will generally stay with the Bayer Group and were not reported in the Combined Financial Statements of the LANXESS Subgroup, unless the underlying transaction was clearly allocable to a business division of the LANXESS Subgroup and the applicable national tax laws allow the transfer of tax receivables to another taxpayer.

Deferred taxes were determined in the Combined Financial Statements on the basis of the temporary differences between the carrying amounts of assets and liabilities in the accounting and tax balance sheets. The calculation is based on the tax rates anticipated in the individual countries for the time of realization. These tax rates are generally based on the statutory rates in effect or enacted, as the case may be, as of the balance sheet date and may deviate from the actual tax rates that would have applied had the business units of the LANXESS Subgroup in fact been operated as separate entities during the respective periods.

Similar to assets and liabilities, income and expenses were also generally allocated to the business unit responsible for generating the income or incurring the expense. In the case of shared areas such as Distribution and Research and Development, expenses were allocated according to the ‘‘primary use’’ principle. In addition, so-called term sheets govern reporting and accounting for jointly-used services (power plants, laboratories and production and storage facilities). Thus, the so-called ‘‘costs of doing business’’ principle was followed in the preparation of the historical financial data of the LANXESS Subgroup, although it should be noted that the amounts allocated to the LANXESS Subgroup reflect the income and expenses that would have been allocated on the basis of this principle to the LANXESS Subgroup as an entity of the Bayer Group.

Service and Agency Companies

For consolidation purposes, separate financial statements were also prepared for the business divisions to be transferred from seven Bayer service companies that previously provided services to the LANXESS Subgroup.

In countries in which the Bayer Group did not maintain extensive chemical or polymer operations for transfer to the LANXESS Group, the future LANXESS Group is likely to use the existing distribution network of the Bayer Group pursuant to commercial agency agreements and authorized dealer agreements. In these cases, the historical costs were taken into account in the Combined Financial Statements. The so-called agency companies will continue to be included in Bayer AG’s consolidated financial statements.

Pensions and Other Post-Employment Benefits

For the periods ending December 31, 2002 and December 31, 2003, separate actuarial opinions were prepared for the presentation of pension obligations in the Combined Financial Statements and the obligations to be transferred. Each of these opinions was based on personnel lists detailing the employees to be transferred to the LANXESS Subgroup. The obligations were therefore calculated primarily on a person-by-person basis. Only in exceptional cases were obligations allocated proportionately based on the number of employees.

Country or company-specific rules exist in relation to the vested pension claims of employees who had retired or left the organization prior to July 1, 2004. These rules are discussed below insofar as they relate to the pension schemes in Germany, the U.S. and Canada, which are of key relevance to the LANXESS subgroup.

With regard to Germany, the agreements concluded and yet to be concluded in order to establish the LANXESS Subgroup stipulated that all pension obligations to active employees to be transferred to the LANXESS Subgroup as of July 1, 2004 will be transferred to the LANXESS Group. At the same time, the Bayer Group will remain responsible for all obligations owed to ex-employees with vested claims who left the organization prior to July 1, 2004.

By contrast, the pension obligations in the United States were allocated on the basis of the existing pension plans. In the case of plans which give rise to obligations to former employees as well as to active employees and could be allocated to the LANXESS Subgroup for financial reporting purposes, the respective obligations were transferred to the LANXESS Subgroup in full. Furthermore, plans were allocated to the LANXESS Subgroup under which only the obligations to active employees were transferred, while the remaining obligations remain with the Bayer Group, analogous to the arrangement in Germany. The pension obligations under yet another category of plans fully remain with Bayer.

In Canada, obligations to active employees, retirees and ex-employees with vested claims were transferred to the LANXESS Subgroup.

Capital Structure

Liquidity and financial debt are not assigned to existing business units of the Bayer Group, but are instead managed centrally at the company or group level. The liquidity as well as the equity and debt structure shown in the Combined Financial Statements are based on the target net indebtedness level as of the date the spin-off takes effect, with the goal of achieving an investment grade rating. The financing structure for the years 2002 and 2003 was handled accordingly.

The first step was to allocate all directly allocable receivables and financial obligations affecting liquidity. In order to achieve the desired level of financing for the LANXESS Subgroup, an external funding arrangement was assumed to be in place for LANXESS Deutschland GmbH in a second, supplementary step. Interest expenses for 2002 and 2003 are based on market interest rates for industrial bonds at the lower end of the investment grade range. These interest rates were computed by averaging the rates charged on a short-term instrument and on a five-year instrument. A risk premium was added to account for non-euro denominated financing.

Effects of the New Accounting Standards

Since 2002, International Financial Reporting Standards (''IFRS'') is the term used to describe the entire body of accounting standards issued by the IASB, and thereby replaces the earlier term used, ''IAS'' or ''International Accounting Standards.'' With respect to individual accounting standards that the IASB issued prior to this change in terminology, the prefix ''IAS'' continues to be used.

In February 2004, the IASB issued International Financial Reporting Standard (IFRS) 2 — Share-based Payment — which was intended to govern accounting for share-based payments, including employee share purchase plans. IFRS 2 governs the way in which corporations account for share-based payments and requires that such payments be recorded in the corporation's income statement and in the balance sheet. IFRS 2 applies to fiscal years commencing on or after January 1, 2005.

In March 2004, the IASB issued IFRS 3 — Business Combinations — which superseded the previous IAS 22. According to IFRS 3, all business combinations are to be accounted for in accordance with the purchase method of accounting; the pooling of interests method is not to be applied. Identifiable assets and liabilities must be recognized at fair value at the acquisition date. Goodwill may no longer be amortized, but must be tested annually for impairment. IFRS 3 applies to all business combinations for which the agreement date is on or after March 31, 2004. In the case of goodwill or intangible assets that were acquired in connection with a business combination occurring prior to March 31, 2004, the standard must be applied beginning with the fiscal year commencing immediately following March 31, 2004.

In March 2004, the IASB issued IFRS 4 — Insurance Contracts. This standard applies to virtually all insurance contracts that give rise to an insurance obligation on the part of a corporation, as well as to all of a corporation's reinsurance contracts. IFRS 4 applies to fiscal years commencing on or after January 1, 2005.

In March 2004, the IASB issued IFRS 5 — Non-current Assets Held for Sale and Discontinued Operations. According to IFRS 5, assets intended for disposal are to be recorded at the lower of the assets' carrying amounts or fair value less selling costs. The standard also stipulates when certain operating segments of an entity are to be classified as discontinued operations. IFRS 5 applies from January 1, 2005.

In March 2004, the IASB issued an amendment to International Accounting Standard (IAS) 39 — Financial Instruments: Recognition and Measurement — which governs fair value hedge accounting for portfolio hedging of interest rate risks. The amendment simplifies the implementation of IAS 39 by enabling fair value hedge accounting to be used more readily for portfolio hedging of interest rate risk than under previous versions of IAS 39. The corresponding modifications of IAS 39 apply to fiscal years commencing on or after January 1, 2005. However, this amendment should be applied earlier if the revised versions of IAS 39 (as revised in 2003) and IAS 32 — Financial Instruments: Disclosure and Presentation (as revised in 2003) — are applied earlier.

In connection with the issuance of IFRS 3 in March 2004, the IASB also revised IAS 36 (Impairment of Assets) and IAS 38 (Intangible Assets). These standards now require that goodwill and intangible assets with an indefinite useful life be tested for impairment at least annually. If events or changes in circumstances indicate that an impairment could exist, then additional impairment tests must be conducted at any time during the year. In addition, the reversal of an impairment loss recognized for goodwill is prohibited. If there is no foreseeable limit to the period over which intangible assets are expected to generate net cash inflows, the intangible assets will be treated as having an indefinite life. Amortization of such assets is prohibited; instead they must be tested for impairment in the same way as goodwill. The revised standards are effective for goodwill and intangible assets acquired in business combinations for which the completion date is on or after March 31, 2004 and all other goodwill and intangible assets for annual periods beginning on or after March 31, 2004.

The Bayer Group and the LANXESS Subgroup are currently reviewing the effects of the amended standards on the financial condition and results of operations of the LANXESS Subgroup.

Basic Principles of the Consolidated Financial Statements

Consolidation Methods

Capital consolidation is performed according to IAS 22 (Business Combinations) by offsetting investments in subsidiaries against the underlying equity on the dates of acquisition by the Bayer Group. The identifiable assets and liabilities are included at their fair value. The balance is recognized as goodwill. Fair value adjustments of the assets and liabilities concerned are amortized together with the corresponding assets and liabilities in subsequent periods. No additional fair value adjustments are recognized in connection with the transfer of assets and liabilities and of subsidiaries to the LANXESS Subgroup.

Where financial statements of individual consolidated companies reflect write-downs or write-backs of investments in other consolidated companies, these write-downs or write-backs are reversed for purposes of the Group financial statements.

Intragroup sales, profits, losses, income, expenses, receivables and payables are eliminated.

Deferred taxes are recognized for temporary differences related to consolidation entries.

Jointly-managed entities are consolidated *pro rata* according to the same principles.

The Combined Financial Statements include the business transactions and business activities allocable to the LANXESS Subgroup. Subsidiaries and joint ventures that do not have a material impact on the financial condition and results of operations either individually or in the aggregate, are not consolidated. They are presented in the Combined Financial Statements at the lower of cost of acquisition or fair value.

However, investments in associated companies on which the LANXESS Subgroup exerts significant influence, generally through an ownership interest between 20 and 50 percent, are accounted for by the equity method. The cost of acquisition of a company included at equity is adjusted annually by the percentage of any change in its stockholders' equity. Any goodwill arising from the first-time inclusion of these investments at equity is accounted for in the same manner as goodwill relating to fully-consolidated companies. No companies were recorded at equity in the Combined Financial Statements for the years 2002 and 2003.

Foreign Currency Translation

In the financial statements of the individual consolidated companies, which are the basis for the Combined Financial Statements, foreign currency receivables and payables are translated at rates prevailing on the financial statement closing date, irrespective of whether they are exchange-hedged. Forward contracts which, from an economic point of view, serve as a hedge against fluctuations in exchange rates, are recorded at fair value.

The financial statements of entities outside the euro zone are translated into euros in accordance with the concept of ''functional currencies'' pursuant to IAS 21 (The Effects of Changes in Foreign Exchange Rates). The functional currencies are in all cases the respective local currencies, since these entities operate independently from a financial, economic and organizational point of view. Their assets and liabilities are therefore translated at rates prevailing on the financial statement closing date, and income and expense items at the average rates for the year.

Differences arising from the translation of foreign companies' balance sheets as of the financial statement closing date are shown in a separate stockholders' equity item as ''currency translation adjustments''.

In preparing the consolidated financial statements, differences from the currency translation were also determined for the company units being transferred. It was assumed here that the ratio between the assets and liabilities transferable to the LANXESS Subgroup and the net assets of the transferring Bayer company would reflect the *pro rata* share of the currency translation difference.

In case consolidated companies leave the consolidated group, the respective currency translation differences are reversed and recognized in income.

The exchange rates for major currencies against the euro varied as follows:

		Closing Rate		Average Rate	
		2002	2003	2002	2003
			(€1)		
Argentina	ARS	3.53	3.70	2.97	3.33
Brazil	BRL	3.71	3.66	2.78	3.47
United Kingdom	GBP	0.65	0.70	0.63	0.69
Japan	JPY	124.39	135.05	118.06	130.96
Canada	CAD	1.66	1.62	1.48	1.58
Mexico	MXN	10.99	14.18	9.15	12.22
Switzerland	CHF	1.45	1.56	1.47	1.52
USA	USD	1.05	1.26	0.95	1.13

Accounting and Valuation Principles

Net sales and other operating income

Sales are recognized upon delivery of goods or rendering of services to third parties and are reported net of sales taxes and rebates. Revenues from contracts that contain customer acceptance provisions are deferred until customer acceptance occurs or the contractual acceptance period has lapsed. Expenses related to provisions for rebates to customers are recognized in the period in which the related sales are recorded based on contract terms. Payments relating to the sale or outlicensing of technologies or technological expertise are immediately recognized as income once the respective agreements have become effective, if all rights to the technologies and all obligations resulting from them have been relinquished under the terms of the contract. However, if rights to technologies continue to exist or obligations resulting from them have yet to be fulfilled, then the payments received are recorded in line with the actual circumstances. Revenues such as license and rental revenues, and dividend and interest income, are recognized according to the same principles.

Research and development costs

According to IAS 38 (Intangible Assets), research costs cannot be capitalized; development costs must only be capitalized if specific conditions have been fulfilled. Development costs must be capitalized if it is sufficiently certain that the future economic benefits to the company will cover not only the normal operational costs, but also the development costs themselves. There are also several other criteria relating to the development project and the products or processes being developed, all of which have to be met in order to justify asset recognition. As in fiscal year 2002, these conditions have not been satisfied.

Income taxes

Taxes paid or owed on income and other revenues in the individual jurisdictions, as well as any deferred taxes, are reported under income taxes. Taxes were generally allocated according to the respective contributions the transferring business divisions made to the results. Country-specific tax rates were used as the basis for the calculation. Underlying this calculation was an assumption that the German LANXESS companies were not included in Bayer AG's consolidated tax assessment. Under this assumption and in accordance with the fundamental principles observed in the preparation of the Combined Financial Statements, tax loss carry forwards were allocated on a *pro rata* basis. Future actual tax results of the LANXESS Subgroup are dependent on the legal structure and tax strategy of the LANXESS Subgroup as an independent organization. One particular influencing factor will be the domestic tax loss carry forwards, which are expected to pass to the LANXESS Subgroup in accordance with § 15 (4) UmwStG and that may be used subject to the requirements under the general rules of § 8 (4) of the Corporate Income Tax Act (KStG).

Intangible assets

Intangible assets acquired for consideration are recorded at acquisition cost and amortized over their expected useful lives. Acquired intangible assets other than goodwill are amortized by the straight-line method over a period of 4 to 15 years. Permanent impairments are accounted for by impairment charges. If the reasons for the impairment loss cease to apply, it will be reversed. Amortization for the fiscal year was allocated to the relevant operating cost account, *i.e.*, cost of goods sold, selling expenses, research and development expenses or general and administrative expenses.

Goodwill, including that resulting from capital consolidation, is capitalized in accordance with IAS 22 (Business Combinations) and amortized on a straight-line basis over its estimated useful life, not exceeding a maximum period of 20 years. The value of goodwill is reassessed regularly and is written-down, if necessary. In compliance with IAS 36 (Impairment of Assets), such write-downs of goodwill are calculated using an analysis of the future discounted estimated cash flows to be generated by the underlying assets. Amortization and write-downs of capitalized goodwill are recorded as other operating expense.

Self-created intangible assets generally are not capitalized. Certain development costs relating to the application development stage of internally developed software are, however, capitalized. These costs are amortized over the estimated useful life of the software from the date it is placed into service.

Property, plant and equipment

Property, plant and equipment is carried at the cost of acquisition or construction, less scheduled depreciation through actual use. Impairments are recognized for any declines in value expected to be permanent that exceed the depreciation through actual use. In compliance with IAS 36 (Impairment of Assets), such impairment is calculated using an analysis of the future discounted estimated cash flows of the relevant assets. If it is not possible to allocate to the assets in question their own future cash flow, the impairment is calculated on the basis of the cash flow generated by the relevant cash-generating unit. If the reasons for the impairment loss cease to apply, it will be reversed.

The cost of construction of self-constructed property, plant and equipment comprises the direct costs of the materials and direct manufacturing expenses, as well as appropriate allocations of material and manufacturing overheads, an appropriate share of the depreciation and write-downs of assets used in construction and the *pro rata* share of expenses for company pension plans and discretionary employee benefits that are attributable to the construction.

If the construction phase of property, plant or equipment extends over a long period, the interest incurred on borrowed capital up to the date of completion is capitalized as part of the cost of acquisition or construction.

Expenses for the repair of property, plant and equipment are normally charged against income, but they are capitalized if they result in an enlargement or substantial improvement of the respective asset.

Property, plant and equipment is depreciated using the straight-line method, except where the declining-balance method is more appropriate in light of the actual utilization pattern. Depreciation for the fiscal year has been allocated to the relevant operating cost account, *i.e.*, cost of goods sold, selling expenses, research and development expenses or general and administrative expenses.

When property, plant and equipment assets are closed down, sold or abandoned, the difference between the net proceeds and the net carrying amount of the assets is recognized as a gain or a loss in other operating income or expenses, respectively.

The following depreciation periods, based on the estimated useful lives of the respective assets, are applied throughout the Group:

Buildings	20	to	50	years
Outdoor infrastructure	10	to	20	years
Plant installations	6	to	20	years
Machinery and apparatus	6	to	12	years
Laboratory and research facilities	3	to	5	years
Storage tanks and pipelines	10	to	20	years
Vehicles	5	to	8	years
Computer equipment	3	to	5	years
Furniture and fixtures	4	to	10	years

In accordance with IAS 17 (Leases), property, plant and equipment leased on terms equivalent to financing a purchase by long-term loan (finance leases) are capitalized at the lower of their fair value on the date of acquisition of the asset or the present value of the total lease payments. The leased assets are depreciated over their estimated useful lives except where subsequent transfer of title is uncertain, in which case they are depreciated over the shorter of their estimated useful lives or the term of the lease. Future lease payments are recorded as financial obligations.

Investments

Investments in affiliated companies and investments in securities are classified as either held-to-maturity or available-for-sale and recognized in compliance with IAS 39 (Financial Instruments: Recognition and Measurement) at amortized costs or fair value. Where evidence exists that such assets may be impaired, the impairment is recognized as necessary on the basis of an impairment test. If the reasons for the impairment loss lease to apply, it will be reversed.

Loans receivable that are interest-free or bear low rates of interest are carried at present value; other loans receivable are carried at amortized cost.

Financial instruments

Financial instruments represent contractual claims on financial assets. Under IAS 32 (Financial Instruments: Disclosure and Presentation), financial instruments include both primary instruments, such as trade accounts receivable and payable, investments, and financial liabilities; and derivative financial instruments, which are used to hedge risks arising from changes in currency exchange and interest rates. Further details concerning financial instruments are provided in note (35).

Inventories

In accordance with IAS 2 (Inventories), the item inventories encompasses assets (finished goods and goods purchased for resale) held for sale in the ordinary course of business, assets in the process of production for such sale (work in process) or assets to be consumed in the production process or in the rendering of services (raw materials and supplies). Inventories are usually measured at their cost of acquisition or production, using the weighted-average method, or, if lower, at net realizable value, which is the estimated ordinary course selling price less the estimated production costs and selling expenses.

The cost of goods sold comprises the direct cost of materials, direct manufacturing expenses and appropriate allocations of fixed and variable manufacturing overheads, to the extent they are attributable to production.

It also includes the share of expenses for company pension plans and discretionary employee benefits that are attributable to production. Administrative costs are included where they are attributable to production.

In view of the production characteristics of the Lanxess Subgroup, work in process and finished goods are grouped together.

Other receivables and other assets

Other receivables and other assets are recorded at amortized cost. Any necessary valuation allowances are made on the basis of the probability of default.

Deferred taxes

Deferred taxes are calculated in accordance with IAS 12 (Income Taxes). Deferred taxes arise from temporary differences between the carrying amounts of assets or liabilities in the accounting and tax balance sheets, from consolidation measures and from realizable tax loss carry forwards. The calculation is based on the anticipated tax rates in the individual countries at the time of recognition. The tax rates are generally based on the statutory provisions in effect or enacted, as the case may be, as of the balance sheet date.

A valuation allowance is recognized against tax loss carry forwards when it is not sufficiently certain that they will be realized.

Provisions

Other provisions are valued in accordance with IAS 37 (Provisions, Contingent Liabilities and Contingent Assets) and, where appropriate, IAS 19 (Employee Benefits), using the best estimate of the extent of the obligation. Long-term portions of provisions are discounted to their present value insofar as the extent and timing of the obligation can be assessed with a reasonable degree of certainty. Details on pension provisions are provided in note (26).

If the projected extent of obligation declines as a result of a change in the estimate, the provision is reversed by the corresponding amount and the resulting income recognized in the appropriate operating cost account, *i.e.*, cost of goods sold, selling expenses, research and development expenses or general and administrative expenses.

Personnel commitments mainly include annual bonus payments, service awards and other personnel costs. Reimbursements to be received from the German Government under the pre-retirement part-time work program are recorded as receivables and recognized as income as soon as the criteria for such reimbursements have been fulfilled. Provisions for trade-related commitments mainly include rebates.

The LANXESS Subgroup also sets up provisions for ongoing or probable litigation where reasonable estimates are possible. These provisions include all estimated legal fees and expenses and costs of potential settlements. The amounts are based on information and cost estimates provided by the Subgroup’s attorneys. The provisions are reviewed and updated together with the Group’s attorneys at regular intervals not exceeding three months.

Liabilities

Short-term liabilities are recognized at payment or redemption amounts. Long-term liabilities and financial obligations that do not represent an item hedged in a permissible hedge accounting relationship are carried at amortized cost. Liabilities relating to finance leases are carried at the present value of the future lease payments.

Deferred income

In accordance with IAS 20 (Accounting for Government Grants and Disclosure of Government Assistance), grants and subsidies that serve to promote investment are reflected on the balance sheet as deferred income. The amounts are reversed to income over the useful lives of the respective assets.

Cash Flow Statement

The cashflow statement shows how the liquidity of the LANXESS Subgroup was affected by the inflow and outflow of cash and cash equivalents during the course of the reporting year. The effects of acquisitions, divestitures or other changes in the scope of consolidation are eliminated. Cash flows are classified by operating, investing and financing activities in accordance with IAS 7 (Cash Flow Statements). Cash and cash equivalents shown in the balance sheet comprise cash, checks, balances with banks and securities with original maturities of up to three months. An adjustment is shown to reconcile cash and cash equivalents at the end of the year to the liquid assets reflected in the balance sheet.

The amounts reported by consolidated companies outside the euro zone are translated at average exchange rates for the year, with the exception of cash and cash equivalents, which are translated at rates prevailing on the financial statement closing date as in the balance sheet. The effects of changes in the exchange rates on cash and cash equivalents are shown separately.

Global Impairment Testing Procedures and Impact

In the fourth quarter of 2003, the Bayer Group considered it necessary to review the carrying amount of its global assets as part of an impairment test conducted pursuant to IAS 36. This impairment test also affected business areas allocable to the LANXESS Subgroup. These developments were caused primarily by a number of anticipated adverse external factors such as sustained unfavorable price trends, especially higher raw material costs, that could only be passed on to customers to a limited extent. An additional underlying cause was lower sales volume growth as a result of tougher competition caused partially by global overcapacities. Moreover, lower macroeconomic growth forecasts and continued unfavorable currency exchange trends played a role.

Assets were tested for impairment by comparing the residual carrying amount of each cash-generating unit (CGU) to the recoverable amount, which is the higher of the net selling price or value in use.

In line with the definition of cash generating units, those units were generally identified as being the strategic business entities. They represent the financial reporting level immediately below the segments.

The following business units comprising all segments of the LANXESS Subgroup were affected by the 2003 impairments:

Chemical Intermediates	Performance Chemicals	Engineering Plastics	Performance Rubber
Fine Chemicals	Textile Processing Chemicals	Styrenics Resins	Technical Rubber Products
Inorganic Pigments	Paper	Fibers	Polybutadiene Rubber
	Rubber Chemicals		

Where the carrying amount of a cash generating unit exceeded the recoverable amount, an impairment loss was recognized covering the difference. First, the goodwill of the relevant strategic business entity was written down. Any remaining impairment loss was allocated *pro rata* among the other assets of the strategic business entity, based on the net carrying amount of each asset on December 31, 2003.

The value in use was determined from the present value of expected future cash flows, based on the continuing use of the asset by the strategic business entity and its retirement at the end of its useful life. The cash flow forecasts were derived from the long-term planning of the Bayer Group.

The discount rate was determined based on in-house analyses of the weighted average cost of capital (WACC). The model used for determining the cost of capital for these analyses is based on the option pricing theory and takes into account country, credit and additional risks arising from the volatility of the business operations as well as the capital structure.

A capital structure was computed for each Bayer subgroup by deriving its theoretical stockholders' equity from the market capitalization of Bayer AG, while taking into account industry-specific financing structures. For the global strategic business entities of the LANXESS Subgroup subjected to impairment testing, the WACC used to discount the estimated cash flows varied between six and seven percent, depending on a specific risk intrinsic to the respective assets.

The following impairment losses were recognized with regard to the LANXESS Subgroup's noncurrent assets for 2003:

	2003 (in € millions)
Goodwill	80
of which Chemical Intermediates	8
of which Performance Chemicals	72
of which Engineering Plastics	—
of which Performance Rubber	—
Intangible assets, excluding goodwill	84
of which Chemical Intermediates	1
of which Performance Chemicals	26
of which Engineering Plastics	54
of which Performance Rubber	3
Property, plant and equipment	824
of which Chemical Intermediates	322
of which Performance Chemicals	70
of which Engineering Plastics	302
of which Performance Rubber	130
Total	988
of which Chemical Intermediates	331
of which Performance Chemicals	168
of which Engineering Plastics	356
of which Performance Rubber	133

In fiscal year 2002, impairment losses on property, plant and equipment (totaling € 84 million) were recognized solely in Engineering Plastics.

Changes in the Group

Since in the past only a portion of the business of the LANXESS Subgroup had been conducted by independent legal entities, while the majority of the business had been conducted by shared legal entities engaged in other Bayer Group business as well, the consolidated financial statements were derived from the Bayer Group's consolidated accounts.

The Combined Financial Statements include 38 companies that were exclusively engaged in LANXESS-related business. They were included in the LANXESS Subgroup on the basis of their historical financial statements for the years 2002 and 2003.

Former (transferred) Bayer company	Future LANXESS company
Germany	
GVW Garnveredelungswerke GmbH, Goch	GVW Garnveredelungswerke GmbH, Goch
Bayer Distribution Service GmbH, Cologne	LANXESS Distribution GmbH, Cologne
RheinChemie Rheinau GmbH, Mannheim	RheinChemie Rheinau GmbH, Mannheim
Bayer Faser GmbH, Dormagen	Dorlastan Fibers & Monofil GmbH, Dormagen
Bayer Kautschuk Gesellschaft mit beschränkter Haftung, Dormagen	LANXESS Kautschuk GmbH, Dormagen
Bayer Buna GmbH, Marl	LANXESS Buna GmbH, Marl
Borchers GmbH, Langenfeld	Borchers GmbH, Langenfeld
IAB Ionenaustauscher GmbH Bitterfeld, Greppin	IAB Ionenaustauscher GmbH Bitterfeld, Greppin
Bayer Industrieprodukte GmbH & Co. KG, Leverkusen	LANXESS Europe GmbH & Co. KG, Leverkusen
ISL-Chemie GmbH & Co. KG, Kürten	ISL-Chemie GmbH & Co. KG, Kürten
DUBAY Polymer GmbH, Hamm (beginning 2003)	DUBAY Polymer GmbH, Hamm (beginning 2003)
PharmAgro GmbH, Leverkusen (beginning 2003)	PharmAgro GmbH, Leverkusen (beginning 2003)
Other Europe	
Bayer Rubber N.V., Belgium	LANXESS Rubber N.V., Belgium
Bayer Elastomeres S.A., France	LANXESS Elastomeres S.A.S, France
Borchers France S.A., France	Borchers France S.A., France
Sybron Chemical Industries Nederland B.V., Netherlands	Sybron Chemical Industries Nederland B.V., Netherlands
EUROPIGMENTS S.L., Spain	EUROPIGMENTS S.L., Spain
Bayer Chemicals S.L., Spain	LANXESS Chemicals S.L., Spain
Novochem 2000 S.A., Spain (beginning 2003)	Novochem 2000 S.A., Spain (beginning 2003)
W. Hawley & Son Ltd., Great Britain	LANXESS Limited, Great Britain
Bayer Tanatex B.V., Netherlands	LANXESS B.V., Netherlands
Sybron Chemicals Holdings B.V., Netherlands	Sybron Chemicals Holdings B.V., Netherlands
Sybron Chemicals International Holdings Ltd., Great Britain	Sybron Chemicals International Holdings Ltd., Great Britain
Sybron Kimyasal Ürünler Ticaret Limited Sirketi, Turkey	Sybron Kimyasal Ürünler Ticaret Limited Sirketi, Turkey
North America	
Rhein Chemie Corporation, USA	Rhein Chemie Corporation, USA
Sybron Chemicals Inc., USA	Sybron Chemicals Inc., USA
Sybron Chemical Holdings Inc., USA	Sybron Chemical Holdings Inc., USA
Asia/Oceania	
Bayer Chemicals Pty. Ltd., Australia	LANXESS Pty. Ltd., Australia
Bayer Shanghai Pigments Co. Ltd., China	LANXESS Shanghai Pigments Co. Ltd., China
Bayer International Trading (Shanghai) Co. Ltd., China	LANXESS International Trading (Shanghai) Company Limited, China
Bayer Wuxi Leather Chemical Co. Ltd., China	LANXESS (Wuxi) Chemical Co. Ltd., China
Rhein Chemie (Qingdao) Co. Limited, China	Rhein Chemie (Qingdao) Co. Limited , China
Bayer Speciality, India	LANXESS India Private Limited, India
Bayer ABS Limited, India	LANXESS ABS Limited, India
Rhein Chemie Japan Ltd., Japan	Rhein Chemie Japan Ltd., Japan
Bayer Chemicals Japan Ltd., Japan (Spin-off in 2003)	LANXESS K.K., Japan
Latin America/Africa/Middle East	
Bayer Holding (Pty) Ltd., South Africa	LANXESS Mining (Proprietary) Limited, South Africa
Chrome International South Africa (Pty) Ltd., South Africa	Chrome International South Africa (Pty) Ltd., South Africa

Four of the listed companies, which operate businesses primarily allocable to the LANXESS Subgroup, were also included in the Combined Financial Statements on the basis of their historical financial statements, although the business units or business activities allocable to the remaining part of the Bayer Group were transferred to a new or existing Bayer company.

Former (transferred) Bayer Company	Future LANXESS Company
Bayer Chemicals Pty. Ltd., Australia	LANXESS Pty. Ltd., Australia
Bayer ABS Limited , India	LANXESS ABS Limited, India
Sybron Chemicals Inc., USA	Sybron Chemicals Inc., USA
Bayer International Trading (Shanghai) Co. Ltd., China	LANXESS International Trading (Shanghai) Co. Ltd., China

In the case of an additional 35 companies, which were primarily engaged in business activities that were to remain with the Bayer Group but whose LANXESS-related business was to be transferred to legally independent units, individual assets were removed from the existing companies in order to reflect the LANXESS-related business. Also included in this number of companies are seven Bayer service companies, which had previously provided services to the LANXESS Subgroup.

For purposes of consolidation, financial statements were prepared for the following divisions in the Combined Financial Statements:

Bayer company (transferring entity)	Future LANXESS company
Germany	
Bayer MaterialScience AG, Leverkusen	LANXESS Deutschland GmbH, Leverkusen
Euroservices Bayer GmbH, Leverkusen	LANXESS Accounting GmbH, Leverkusen
Bayer Polymers Customer Services GmbH, Neuss	LANXESS Europe GmbH & Co. KG, Leverkusen
Bayer Chemicals AG, Leverkusen	LANXESS Deutschland GmbH, Leverkusen
Bayer Business Services GmbH, Leverkusen	LANXESS Deutschland GmbH, Leverkusen
Bayer Technology Services GmbH, Leverkusen	LANXESS Deutschland GmbH, Leverkusen
Other Europe	
Bayer Antwerpen N.V., Belgium	LANXESS N.V., Belgium
Bayer International Comm. V., Belgium	LANXESS N.V., Belgium
Bayer S.A.-N.V., Belgium	LANXESS N.V., Belgium
Bayer B.V., Netherlands	LANXESS B.V., Netherlands
Bayer S.A.S., France	LANXESS S.A.S., France
Bayer S.P.A., Italy	LANXESS S.r.l., Italy
Bayer MaterialScience S.r.l., Milan	LANXESS Deutschland GmbH, Leverkusen
Bayer International S.A., Belgium	LANXESS N.V., Belgium
Bayer International, Switzerland	LANXESS International S.A., Switzerland
Bayer Hispania, S.A., Spain	LANXESS Holding Hispania, S.L., Spain
Bayer Polimeros S.L., Barcelona	LANXESS Styrenics S.L., Barcelona, Spain
Bayer UK Limited, Great Britain	LANXESS Limited, Great Britain
North America	
Bayer Inc., Canada	LANXESS Inc., Canada
Bayer Polymers LLC, USA	LANXESS Corp., USA
Bayer Chemicals Corporation, USA	LANXESS Corp., USA
Bayer Corporate and Business Services LLC, USA	LANXESS Corp., USA

Bayer company (transferring entity)	Future LANXESS company
Asia/Oceania	
Bayer Australia Limited, Australia	LANXESS Pty. Ltd., Australia
Bayer China Company Limited, Hong Kong	LANXESS Hong Kong Ltd., Hong Kong
Bayer China Ltd., China	LANXESS Chemical (Shanghai) Company Limited, China
Bayer Polymers, Hong Kong	LANXESS Hong Kong Ltd., Hong Kong
Bayer (India) Limited, India	LANXESS India Private Limited, India
Bayer Polychem India Limited, India	LANXESS India Private Limited, India
Bayer Ltd., Japan	LANXESS K.K., Japan
Bayer South East Asia Pte. Ltd., Singapore	LANXESS Pte. Ltd., Singapore
Bayer Thai Company Limited, Thailand	LANXESS (Thailand) Co., Ltd., Thailand
Latin America/Africa/Middle East	
Bayer S.A., Argentina	LANXESS S.A., Argentina
Bayer de Mexico, S.A. de C.V., Mexico	LANXESS, S.A. de C.V., Mexico
Bayer S.A., Brazil	LANXESS Industria de Produtos Quimicos e Plasticos Ltda., Brazil
Bayer (Proprietary) Limited, South Africa	LANXESS (Pty) Ltd., South Africa

Eleven additional subsidiaries were not consolidated because in aggregate they are of minor importance to the Group's financial condition and results of operations. The following is a list of these companies:

LANXESS company	Percentage ownership [%]
Suberit Kork GmbH, Mannheim	100
LANXESS Europe Geschäftsführungs GmbH, Leverkusen	100
ISL-Chemie Geschäftsführungs GmbH, Leverkusen	100
Mineracao Comisa Ltda., Brazil	100
Comercial Andinas Ltda., Chile	99.5
Mineracao Cromina Ltda., Brazil	100
Sybron Chemicals UK Ltd., Great Britain	100
Sybron Chemicals (Shanghai) Ltd., China	100
Sybron Chemicals (South Africa) (Pty) Ltd., South Africa	100
Sybron Quimica Iberica S.A., Barcelona	100
1. BCh eV GmbH, Leverkusen (beginning 2003)	100

Furthermore, there are eight (2002: nine) associated or other companies deemed to be of minor importance to the Group's financial condition and results of operations. The following is a list of these companies:

LANXESS company	Percentage ownership [%]
ARG Verwaltungs GmbH, Duisburg	16.67
ARG mbH & Co. KG, Duisburg	16.90
Treuhandgemeinschaft Deutscher Chemiefasererzeuger GmbH, Frankfurt	12.60
Studiengesellschaft Kohle mbH, Mülheim	4.50
Quimidroga Plasticos, S.A., Barcelona	40.00
Indaver N.V., Antwerp	0.50
Elemica Inc., Delaware, USA	9.48
Hidrax Ltda., Brazil	39.00
Elemica, Dublin (only in 2002; merged into Elemica Inc., Delaware, in 2003)	9.00

In the years 2002 and 2003, Bayer Chrome International, South Africa, was included as a joint venture in accordance with IAS 31 (Financial Reporting of Interests in Joint Ventures) by proportionate consolidation. The joint venture had the following effect on the Group's assets and liabilities as well as on its income and expenses:

	2002 (in € millions)		2002 (in € millions)
Noncurrent assets	31	Income	20
Current assets	3	Expenses	(19)
Provisions for pensions	0		
Other provisions	(1)		
Financial obligations	(36)		
Remaining liabilities	(1)		
Net assets	(4)	**Income after taxes**	1

	2003 (in € millions)		2003 (in € millions)
Noncurrent assets	30	Income	17
Current assets	5	Expenses	(21)
Provisions for pensions	0		
Other provisions	(1)		
Financial obligations	(39)		
Remaining liabilities	(1)		
Net assets	(6)	**Income after taxes**	(4)

No acquisitions were made in the years 2002 and 2003. In 2003, the organic pigments business was sold to Sun Chemicals Group (USA) for €46 million, which was offset against asset disposals totaling €41 million and transaction and other costs in the amount of €5 million.

NOTES TO THE STATEMENTS OF INCOME

(1) Net sales

Net sales in 2003 decreased by €448 million (or 6.6 percent) compared with 2002 to €6,315 million. The effect of negative changes in the currency exchange rates was €353 million or –5.2 percent. Furthermore, divestitures reduced sales by €58 million; a development that may be traced primarily to the divestiture of the Organic Pigments product group.

The Combined Financial Statements generally reflect the target structure of the LANXESS Group. However, transactions completed after January 1, 2002 with respect to individual product groups — primarily the sale of Organic Pigments — are included in the Combined Financial Statements as of the date on which they took economic effect.

Sales and their breakdown by segment are presented in the summary on page F-9.

(2) Research and development costs

Because of their importance to the LANXESS Subgroup, research and development expenses are reported separately from the cost of goods sold, selling expenses and general administration expenses.

(3) Other operating income

	2002	2003
	(in € millions)	
Reversal of unutilized provisions	21	11
Recognition of exchange rate hedges	13	11
Gains from sales of property, plant and equipment	1	0
Write-backs of receivables and other assets	1	1
Other operating income	40	34
	76	57

(4) Other operating expenses

	2002	2003
	(in € millions)	
Amortization and write-downs of acquired goodwill	(19)	(97)
Write-downs of trade account receivables	(8)	(3)
Losses from sales of property, plant and equipment	(6)	(5)
Impairment write-downs, excluding goodwill	(84)	(908)
Other operating expenses	(220)	(85)
	(337)	(1,098)

In fiscal year 2003, the need for worldwide impairments led to €988 million in additional charges reported under other operating expenses.

In 2002, a special charge against property, plant and equipment in the fibers business, in particular, increased other operating expenses by €84 million.

€48 million was spent on restructuring in 2003 (2002: €144 million). Further details on the restructuring measures are set forth on page F-45.

(5) Operating result (EBIT)

The breakdown of operating results by segment and by region is set forth on page F-9.

As part of the accounting for ''defined benefit plans'', all expenses and income items included in net pension cost as of December 31, 2003 were recognized in the operating result in the Bayer consolidated financial statements through December 31, 2003. Consequently, interest costs for funded pension obligations representing the increase in present value of the defined benefit obligation during the reporting period as well as the expected return on plan assets were included in the operating result. Only the interest costs for unfunded pension obligations were recorded as other non-operating expense.

All interest costs (*i.e.*, even those involving funded pension obligations) were reported retroactively under non-operating result in the LANXESS Combined Financial Statements using the same approach applied by the Bayer Group starting in 2004. The same applies to the return on plan assets. Regarding the amortization of any actuarial gains or losses, a distinction must be made as to whether the expense resulted from changes in the actuarial assumptions regarding pension obligations or from changes in plan assets. If the assumptions regarding the pension obligations change (such as due to rising salaries and wages), the relevant expense or income must be allocated to the respective operating cost account (such as selling expenses, research and development expenses, general and administrative expenses, etc), thereby increasing or decreasing the operating result. Income or expenses that resulted from changes in the actual values as to opposed to changes in the actuarial assumptions made in connection with valuing the plan assets, continued to be recorded under non-operating result.

(6) Income (expense) from investments in affiliated companies — net

This comprises the following items:

	2002	2003
	(in € millions)	
Dividends and similar income	0	0
Income from profit and loss transfer agreements	0	2
• *of which €0 million from subsidiaries (2002: €0 million)*		
Write-downs of investments in affiliated companies	0	(17)
	0	(15)

(7) Interest income and expense — net

Interest income and expense consists of:

	2002	2003
	(in € millions)	
Income from other securities and loans included in investments	0	0
Other interest and similar income	11	12
• *of which €0 million (2002: €0 million) from subsidiaries*		
Interest and similar expenses	(82)	(66)
• *of which –€1 million (2002: €3 million) to subsidiaries*		
	(71)	(54)

Finance leases are capitalized under property, plant and equipment in compliance with IAS 17 (Leases). The interest portion of the lease payments, amounting to €5 million (2002: €5 million), is reflected under interest expense.

Interest, which is incurred to finance the construction phase on larger investment projects, did not arise.

(8) Other non-operating income and expenses — net

Other non-operating income and expenses consist of the following:

	2002	2003
	(in € millions)	
Interest portion of interest-bearing provisions	(13)	(23)
Net exchange loss	(4)	(18)
Miscellaneous non-operating expenses	(1)	(2)
Miscellaneous non-operating income	0	1
	(18)	(42)

(9) Income taxes

The income taxes item reflects the taxes on income owed or paid in the individual countries as well as the deferred tax accruals. Taxes were generally allocated according to the contributions the transferring business divisions made to the results. Country-specific tax rates were used as the basis for the calculation. Underlying this calculation was an assumption that the German LANXESS companies were not included in Bayer AG’s consolidated tax assessment. Under this assumption and in accordance with the fundamental principles observed in the preparation of the Combined Financial Statements, tax loss carry forwards were allocated on a *pro rata* basis.

The absence of historical unity and independence of the LANXESS Subgroup limits the informative value of the taxes reported here. Future actual tax results of the LANXESS Subgroup are dependent on the legal structure and tax strategy of the LANXESS Subgroup as an independent organization. One significant influencing factor will be the domestic tax loss carry-forwards, which are expected to pass to the LANXESS Subgroup in accordance with § 15

(4) UmwStG and which may be used subject to the requirements under the general rules of § 8 (4) of the Corporate Income Tax Act (KStG).

The breakdown of income tax expenses by origin is as follows:

	2002	2003
	(in € millions)	
Income/loss before income taxes		
— Germany	(136)	(816)
— Other countries	(72)	(592)
	(208)	(1,408)
Income taxes paid or accrued		
— Germany	(11)	(11)
— Other countries	(59)	23
	(70)	12
Deferred taxes		
— from temporary differences	136	258
— from tax loss carry forwards	24	142
	160	400
	90	412

In 2003, deferred tax expenses declined by €10 million as a result of changes in tax rates, while increasing by €3 million in 2002.

The deferred tax assets and liabilities are allocable to the various balance sheet items as follows:

	December 31, 2002		December 31, 2003	
	Deferred tax assets	Deferred tax liabilities	Deferred tax assets	Deferred tax liabilities
	(in € millions)			
Intangible assets	29	1	45	1
Property, plant and equipment	1	408	129	300
Investments	—	—	—	—
Inventories	20	14	12	13
Receivables	4	13	3	14
Other current assets	2	24	0	17
Pension provisions	25	11	26	14
Other provisions	64	2	52	2
Other liabilities	18	1	42	0
Tax loss carry forwards	29	—	167	—
Valuation allowance for tax loss carry forwards	(3)	—	(2)	—
	189	474	474	361
of which long-term	81	420	364	316
Set-off*	(164)	(164)	(304)	(304)
	25	310	170	57

* According to IAS 12 (Income Taxes), deferred tax assets and deferred tax liabilities should, under certain conditions, be offset, if they relate to income taxes levied by the same tax authority.

Due to changes in scope of consolidation, deferred tax assets increased by €2 million in 2003. The existing tax loss carry forwards may continue to be used as follows:

	December 31, 2002	December 31, 2003
	(in € millions)	
Within one year	—	4
Within two years	—	—
Within three years	—	—
Within four years	—	—
Within five years or more	78	416
	78	420

Deferred tax assets totaling €165 million (2002: €26 million) are recognized on the €420 million (2002: €74 million) in tax loss carry forwards that represent income likely to be realized in the future. This resulted in deferred tax income of €142 million (2002: €24 million). The actual utilization of domestic tax loss carry forwards is governed by the general provisions of § 8 (4) KStG.

The actual tax income for 2003 is €412 million (2002: tax income of €90 million). This amount differs by €105 million (2002: €18 million) from the anticipated tax income of €517 million (2002: €72 million), which would result from applying to the pre-tax loss of the legal entities and the spun-off business activities a 2003 tax rate of 36.7 percent (2002: 34.8 percent), which is the weighted average of the theoretical tax rates for the individual consolidated companies.

The reconciliation of theoretical to actual income tax (income) expense in the Group is as follows:

	2002		2003	
	(in € millions)	%	(in € millions)	%
Theoretical tax income (+)	72	100	517	100
Increase in taxes due to non-tax-deductible expenses				
— amortization of goodwill	(7)	(10)	(6)	(1)
— non-scheduled amortization of goodwill based on impairment	—	—	(29)	(6)
Other expenses relating to impairment	—	—	(57)	(11)
Other tax effects	25	35	(13)	(2)
Actual tax income (+)	90	125	412	80
Effective tax rate in %	43.3		29.3	

(10) Other taxes

Other taxes amounting to €70 million (2002: €46 million) are included in the cost of goods sold, selling expenses, research and development expenses and general and administrative expenses. These are mainly taxes related to property, as well as taxes on electricity and other utilities.

(11) Minority stockholders' interest

Minority interests in income are €2 million (2002: €2 million), while minority interest in losses amounted to €1 million (2002: €1 million).

(12) Earnings per share

Since there were no issued and outstanding options, the earnings per share were not diluted in either 2002 or 2003. The ordinary and diluted earnings per share were calculated for 2002 and 2003 on the basis of the annual net income (net loss) divided by the assumed number of shares after completion of the Spin-off. The Board of Management at Bayer AG assumes that 73,034,192 shares of LANXESS AG stock will be issued to implement the Spin-off.

(13) Cost of materials

The cost of materials was €2,434 million (2002: €2,841 million). Since the Bayer Group had not prepared separate annual financial statements with respect to the businesses of the LANXESS Subgroup businesses prior to the decision to spin-off that subgroup, the cost of materials was computed on the basis of the consolidated accounts of the Bayer Group. The cost of materials shown here do not necessarily reflect the expenditures that would have arisen had the LANXESS Subgroup maintained a separate reporting program as of January 1, 2002. In particular, the group-wide service functions, which were transferred to the operating units, could cause future distortions between primary and secondary costs.

(14) Personnel expenses

Personnel expenses declined by €3 million to €1,277 million in 2003; changes in exchange rates reduced this expense by €13 million (2002: €40 million). Personnel expenses consist of wages and salaries totaling €932 million (2002: €993 million) and social expenses totaling €345 million (2002: €287 million), of which €141 million (2002: €99 million) were pension expenses. The limitation on the informative value of the cost of materials also applies accordingly to personnel expenses.

(15) Employees

The number of employees, classified by corporate functions, was as follows:

	2002	2003
Marketing	3,867	3,648
Technology	14,048	14,213
Research	1,316	887
Administration	2,229	1,675
	21,460	20,423

Included in this number is the LANXESS Subgroup's *pro rata* share of joint venture employees. The total number of persons employed by joint ventures of the LANXESS Subgroup was 65 (2002: 66).

Notes to the Balance Sheets

(16) Intangible assets

Changes in intangible assets in 2002 were as follows:

	Acquired concessions, industrial property rights, similar rights and assets, and licenses thereunder	Acquired goodwill	Advance payments	Total
		(in € millions)		
Gross carrying amounts, Dec. 31, 2001	339	236	9	584
Exchange differences	(28)	(33)	(1)	(62)
Changes in scope of consolidation	—	—	—	—
Acquisitions	—	—	—	—
Capital expenditures	45	14	32	91
Retirements	(5)	—	—	(5)
Transfers	1	—	(1)	0
Gross carrying amounts (Dec. 31, 2002)	352	217	39	608
Accumulated amortization and write-downs, Dec. 31, 2001	(122)	(63)	—	(185)
Exchange differences	15	15	—	30
Changes in scope of consolidation	—	—	—	—
Amortization and write-downs in 2002	(59)	(19)	—	(78)
• *of which write-downs*	(8)	—	—	(8)
Write-backs	—	—	—	—
Retirements	4	—	—	4
Transfers	—	—	—	—
Accumulated amortization and write-downs, Dec. 31, 2002	(162)	(67)	—	(229)
Net carrying amounts, Dec. 31, 2002	190	150	39	379

Changes in intangible assets in 2003 were as follows:

	Acquired concessions, industrial property rights, similar rights and assets, and licenses thereunder	Acquired goodwill	Advance payments	Total
		(in € millions)		
Gross carrying amounts, Dec. 31, 2002	352	217	39	608
Exchange differences	(21)	(15)	(2)	(38)
Changes in scope of consolidation	2	—	—	2
Acquisitions	—	—	—	—
Capital expenditures	41	0	8	49
Retirements	(124)	(65)	—	(189)
Transfers	18	—	(30)	(12)
Gross carrying amounts, Dec. 31, 2003	268	137	15	420
Accumulated depreciation and write-downs, Dec. 31, 2002	(162)	(67)	—	(229)
Exchange differences	19	0	—	19
Changes in scope of consolidation	—	—	—	—
Amortization and write-downs in 2003	(202)	(97)	(1)	(300)
• *of which write-downs*	(89)	(80)	(1)	(170)
Write-backs	0	—	—	0
Retirements	122	65	—	187
Transfers	2	—	—	2
Accumulated amortization and write-downs, Dec. 31, 2003	(221)	(99)	(1)	(321)
Net carrying amounts, Dec. 31, 2003	47	38	14	99

The assets of the companies outside the euro zone at the beginning and at the end of each year are translated at the exchange rates prevailing on the financial statement closing date, while intra-year changes in assets are translated at the average rate for that year. This translation method generally also applies to acquisition-related goodwill and remeasurement amounts reflected in the statements of companies outside the euro zone. The differences resulting from currency translation are presented separately in the table above.

(17) Property, plant and equipment

Changes in property, plant and equipment in 2002 were as follows:

	Land and buildings	Technical equipment and machinery	Furniture, fixtures and other equipment	Advance payments to vendors and contractors and construction in progress	Total
			(in € millions)		
Gross carrying amounts, Dec. 31, 2001	1,366	6,253	194	241	8,054
Exchange differences	(73)	(378)	(12)	(11)	(474)
Changes in scope of consolidation	—	—	—	—	—
Acquisitions	—	—	—	—	—
Capital expenditures	9	107	9	177	302
Retirements	(23)	(294)	(18)	(1)	(336)
Transfers	67	143	5	(215)	0
Gross carrying amounts, Dec. 31, 2002	1,346	5,831	178	191	7,546
Accumulated depreciation and write-downs, Dec. 31, 2001	(821)	(4,003)	(140)	—	(4,964)
Exchange differences	22	241	8	0	271
Changes in scope of consolidation	—	—	—	—	—
Depreciation and write-downs in 2002	(47)	(482)	(19)	0	(548)
• *of which write-downs*	(5)	(78)	(1)	—	(84)
Write-backs	—	—	—	—	—
Retirements	18	235	17	—	270
Transfers	(22)	22	—	—	0
Accumulated depreciation and write-downs, Dec. 31, 2002	(850)	(3,987)	(134)	0	(4,971)
Net carrying amounts, Dec. 31, 2002	496	1,844	44	191	2,575

Changes in property, plant and equipment in 2003 were as follows:

	Land and buildings	Technical equipment and machinery	Furniture, fixtures and other equipment	Advance payments to vendors and contractors and construction in progress	Total
			(in € millions)		
Gross carrying amounts, Dec. 31, 2002	1,346	5,831	178	191	7,546
Exchange differences	(40)	(191)	(7)	(4)	(242)
Changes in scope of consolidation	6	22	—	24	52
Acquisitions	—	—	—	—	—
Capital expenditures	10	97	4	152	263
Retirements	(28)	(304)	(13)	(3)	(348)
Transfers	69	74	22	(153)	12
Gross carrying amounts, Dec. 31, 2003	1,363	5,529	184	207	7,283
Accumulated depreciation and write-downs, Dec. 31, 2002	(850)	(3,987)	(134)	0	(4,971)
Exchange differences	19	114	5	—	138
Changes in scope of consolidation	—	—	—	—	—
Depreciation and write-downs in 2003	(195)	(942)	(39)	(1)	(1,177)
• *of which write-downs*	(160)	(640)	(23)	(1)	(824)
Write-backs	—	—	—	—	—
Retirements	14	254	12	—	280
Transfers	(29)	40	(13)	—	(2)
Accumulated depreciation and write-downs, Dec. 31, 2003	(1,041)	(4,521)	(169)	(1)	(5,732)
Net carrying amounts, Dec. 31, 2003	322	1,008	15	206	1,551

The guidelines for currency translation described under ''Intangible Assets'' also apply here.

Capitalized property, plant and equipment includes assets held under finance leases having a total net value of €53 million (2002: €60 million). The gross carrying amounts of these assets as of the financial statement closing date total €126 million (2002: €132 million).

These assets are mainly technical equipment and machinery with a carrying amount of €38 million and a gross carrying amount of €107 million (2002: carrying amount of €53 million and gross carrying amount of €122 million) and buildings having a carrying amount of €13 million and a gross carrying amount of €18 million (2002: carrying amount of €6 million and gross carrying amount of €8 million). In the case of buildings, either the present value of the minimum lease payments covers substantially all of the costs of the acquisition or title passes to the lessee on expiration of the lease.

Also included are products of minor significance leased to other parties under operating leases, where — under the relevant agreements — the lease does not constitute a finance lease within the meaning of IAS 17 (Leases). However, if the lessee is to be regarded as the economic owner of the assets, a receivable is recognized in the balance sheet in the amount of the discounted future lease payments.

(18) Investments

Changes in investments in 2002 were as follows:

	Investments in subsidiaries	Loans to subsidiaries	Investments in affiliated companies		Loans to other affiliated companies	Other securities	Other loans	Total
			Associated companies	Other companies				
				(in € millions)				
Gross carrying amounts, Dec. 31, 2001	11	—	5	18	38	5	—	77
Exchange differences	—	—	—	0	—	—	—	0
Changes in scope of consolidation	—	—	—	—	—	—	—	—
Changes in fair value	—	—	—	—	—	—	—	—
Acquisitions	—	—	—	—	—	—	—	—
Other additions	—	—	—	—	1	0	—	1
Retirements	—	—	—	—	(5)	(3)	—	(8)
Transfers	—	—	—	—	—	—	—	—
Gross carrying amounts, Dec. 31, 2002	11	—	5	18	34	2	—	70
Accumulated write-downs, Dec. 31, 2001	(3)	—	—	—	0	—	—	(3)
Exchange differences	—	—	—	—	—	—	—	—
Changes in scope of consolidation	—	—	—	—	—	—	—	—
Write-downs in 2002	—	—	—	—	0	—	—	0
Write-backs	—	—	—	—	0	—	—	0
Retirements	—	—	—	—	0	—	—	0
Transfers	—	—	—	—	—	—	—	—
Accumulated write-downs, Dec. 31, 2002	(3)	—	—	—	0	—	—	(3)
Net carrying amounts, Dec. 31, 2002	8	—	5	18	34	2	0	67

Changes in investments in 2003 were as follows:

	Investments in subsidiaries	Loans to subsidiaries	Investments in affiliated companies		Loans to other affiliated companies	Other securities	Other loans	Total
			Associated companies	Other companies				
				(in € millions)				
Gross carrying amounts, Dec. 31, 2002	11	—	5	18	34	2	—	70
Exchange differences	—	—	—	—	—	—	—	—
Changes in scope of consolidation	(12)	—		—	—	—	—	(12)
Changes in fair value	—	—	—	—	—	—	—	—
Acquisitions	—	—	—	—	—	—	—	—
Other additions	1	—	—	0	0	1	—	2
Retirements	—	—	—	—	0	0	—	0
Transfers	5	—	(5)	—	—	—	—	—
Gross carrying amounts, Dec. 31, 2003	5	—	0	18	34	3	—	60
Accumulated write-downs, Dec. 31, 2002	(3)	—	—	—	0	—	—	(3)
Exchange differences	—	—	—	—	—	—	—	—
Changes in scope of consolidation	—	—	—	—	—	—	—	—
Write-downs in 2003		—	—	(17)	—	—	—	(17)
Write-backs	—	—	—	—	0	—	—	0
Retirements	—	—	—	—	0	—	—	0
Transfers	—	—	—	—	—	—	—	—
Accumulated write-downs, Dec. 31, 2003	(3)	—	0	(17)	0	—	—	(20)
Net carrying amounts, Dec. 31, 2003	2	—	0	1	34	3	—	40

The guidelines for currency translation described under ''Intangible Assets'' also apply here.

(19) Inventories

Of the €1,096 million in inventories carried as of December 31, 2003 (2002: €1,094 million), €25 million (2002: €24 million) represent inventories carried at net realizable value.

Inventories consist of the following:

	Dec. 31, 2002	Dec. 31, 2003
	(in € millions)	
Raw materials and supplies	183	185
Work in process, finished goods and goods purchased for resale	909	909
Advance payments	2	2
	1,094	1,096

The changes in inventory write-downs are as follows:

	Dec. 31, 2002	Dec. 31, 2003
	(in € millions)	
Balance at beginning of year	(25)	(62)
Additions charged to expense	(44)	(34)
Exchange differences	2	1
Changes in scope of consolidation	0	0
Deductions due to utilization	5	39
Balance at end of year	(62)	(56)

(20) Trade accounts receivable

Trade accounts receivable include write-downs of €22 million (2002: €25 million) for amounts unlikely to be collected.

The total amount of trade accounts receivable, which is due within one year, is €990 million (2002: €1,048 million). Trade accounts receivable from other affiliated companies totaled €3 million (2002: €6 million) and trade accounts receivable from other customers amounted to €987 million (2002: €1,042 million). Trade accounts receivable from other companies within the Bayer Group, which represent third parties to the LANXESS Subgroup, totaled €75 million (2002: €63 million). No trade accounts receivable from subsidiaries existed either in 2002 or 2003.

Changes in write-downs of trade accounts receivable are as follows:

	Dec. 31, 2002	Dec. 31, 2003
	(in € millions)	
Balance at beginning of year	(25)	(25)
Additions charged to expenses	(8)	(3)
Exchange differences	5	1
Changes in scope of consolidation	0	0
Deductions due to utilization	3	5
Balance at end of year	(25)	(22)

(21) Other receivables and other assets

Other receivables and other assets are generally carried at amortized cost, less write-downs totaling €3 million (2002: €0 million).

They are comprised as follows:

	Dec. 31, 2002	Dec. 31, 2003
	(in € millions)	
Short-term loans	182	256
Pension assets in excess of obligations	72	89
Claims for tax refunds	22	28
Lease payments receivable	21	20
Receivables from derivative financial instruments	0	4
Interest receivable on loans	1	0
Payroll receivables	1	2
Other receivables	100	155
	399	554

Interest receivables on loans consist mainly of interest earned in the fiscal year, but not due to be received until after the balance sheet date.

Total other receivables include €1 million (2002: €0 million) of receivables from other affiliated companies. Other receivables from Bayer Group companies, which the LANXESS Subgroup classifies as third party receivables, totaled €332 million (2002: €214 million). There are no receivables from subsidiaries. Total other receivables and other assets totaling €107 million (2002: €80 million) have maturities of more than one year.

Receivables under leases in which the customers are considered to be economic owners of the leased property (finance leases), totaled €20 million (2002: €21 million).

The lease payments are due as follows:

	Lease payments	Of which interest	Account receivable
		(in € millions)	
2004	1	0	1
2005	1	0	1
2006	1	0	1
2007	1	0	1
2008	1	0	1
After 2008	15	0	15
	20	0	20

(22) Liquid assets

	Dec. 31, 2002	Dec. 31, 2003
	(in € millions)	
Marketable securities and other instruments	0	0
Cash and cash equivalents	10	13
	10	13

Financial instruments with original maturities of up to three months are recognized as cash equivalents in view of their high liquidity and are reported under ''Cash and cash equivalents''.

(23) Deferred charges

Total deferred charges include €13 million (2002: €12 million) expected to be used in 2004.

(24) Stockholders' equity

As previously explained in the section entitled ''Basis of Financial Statement Reporting'', the Combined Financial Statements of the LANXESS Subgroup for 2002 and 2003 have been derived from the consolidated accounts of the Bayer Group, allocating the relevant activities to the LANXESS Subgroup for 2002 and 2003. On the basis of the above and of assumptions made, the liquidity and the equity and debt structure shown in the combined financial statements of the LANXESS Subgroup are based on the net indebtedness allocated to the LANXESS Subgroup as of June 30, 2004.

Thus, in accordance with the assumptions made, the total stockholders' equity represents the difference between total assets and total liabilities included in the spun-off businesses combined in the LANXESS Subgroup, taking into account the allocation of net indebtedness for 2002 and 2003. This amount also includes any accumulated gains or losses incurred in these years as well as any other changes in stockholders' equity incurred by the businesses combined in the LANXESS Subgroup.

(25) Minority stockholders' interest

Minority stockholders' interest in 2002 consisted primarily of third parties' shares in the equity of LANXESS ABS Ltd. of India, EUROPIGMENTS S.L. of Spain, LANXESS Shanghai Pigments Co. Ltd. and RheinChemie of China. In 2003, minority stockholders' interest comprised mostly third parties' shares in the equity of LANXESS ABS Ltd. of India, Novochem of Alcantarilla, DUBAY GmbH of Hamm, EUROPIGMENTS S.L. of Spain, and RheinChemie of China.

(26) Provisions for pensions and other post-employment benefits

The LANXESS Subgroup provides retirement benefits for most of its employees, either directly or by contributing to independently-administered funds.

The manner in which these benefits are provided varies according to the legal, fiscal and economic conditions of each country, the benefits generally being based on the employees' remuneration and years of service. The obligations relate both to existing retirees' pensions and to pension entitlements of future retirees.

The basis for presenting the pension obligations in the Combined Financial Statements and the obligations to be transferred were separate actuarial opinions covering the periods ending December 31, 2002 and December 31, 2003, which in turn were based on the lists of employees transferred as of the financial statement closing date. The obligations were therefore calculated primarily on a person-by-person basis. Only in exceptional cases were obligations allocated proportionately based on the number of employees.

Country- or company-specific rules govern the vested pension claims of employees who had retired or left the organization prior to July 1, 2004.

Retirement benefits are provided under both defined contribution and defined benefit plans.

In the case of **defined contribution plans**, the company pays contributions to publicly- or privately-administered pension insurance plans on a mandatory, contractual or voluntary basis. Once the contributions have been paid, the company has no further payment obligations.

The regular contributions constitute net periodic costs for the year in which they are due, and are included in the relevant operating cost account, *i.e.*, cost of goods sold, research and development expenses or general and administrative expenses, and thus in the operating result. In 2003, these payments totaled €51 million (2002: €56 million) for the group.

All other retirement benefit plans are **defined benefit plans**, which may be either unfunded (*i.e.*, financed by provisions or accruals), or funded (*i.e.*, financed through pension funds). In 2003, expenses for defined benefit plans totaled €58 million (2002: €46 million), which, except for the interest costs incurred, the expected return on plan assets and that share of the amortized actuarial gains or losses that is attributable to the plan assets, are generally included in the relevant operating cost account, *i.e.*, cost of goods sold, selling expenses, research and development expenses, general and administrative expenses or other operating income and expenses.

Provisions are also set up under this item for the obligations of Group companies, particularly in the United States, to provide health care to their retirees. For health care costs, the valuation is based on the assumption that they will increase at an annual rate of 5 percent in the long term. Early retirement and certain other benefits to retirees are also included to the extent these obligations are similar in character to pension obligations. Like pension obligations, they are valued in accordance with international standards. These obligations, which are similar to pension obligations, totaled €129 million (2002: €79 million). Expenses for 2003 amounted to €63 million (2002: €22 million). This comprises €57 million (2002: €14 million) for service costs incurred in 2003, €5 million (2002: €5 million) for interest costs as well as €1 million (2002: €1 million) for the amortization of actuarial losses. In 2002, this item included an additional €2 million expense arising from plan curtailments and settlements.

The costs for the plans comprise the following:

	Pension obligations		Other post-employment benefit obligations	
	Dec. 31, 2002	Dec. 31, 2003	Dec. 31, 2002	Dec. 31, 2003
	(in € millions)			
Service cost	35	38	14	57
Past service cost	—	2	—	—
Interest cost	59	61	5	5
Expected return on plan assets	(56)	(51)	—	—
Amortization of actuarial amounts	2	8	1	1
Plan curtailments and settlements	6	—	2	—
	46	58	22	63

The pension provisions for defined benefit plans are calculated in accordance with IAS 19 (Employee Benefits) using the project unit credit method. Under this approach, the future benefit obligations are valued using actuarial methods on the basis of the appropriate assessment of the relevant parameters. Funds and benefit obligations are valued on a regular basis at least every three years. For all major funds, comprehensive actuarial valuations are performed annually.

Benefits expected to be payable after retirement are spread over each employee's entire period of employment, allowing for future changes in remuneration.

The legally independent fund ''Bayer Pensionskasse VvaG'' (Bayer Pensionskasse) is a private insurance company and is therefore subject to the German Act on the Supervision of Private Insurance Companies *(Versicherungsaufsichtsgesetz)*. Since Bayer guarantees the commitments of the Bayer Pensionskasse, it is classified as a defined benefit plan for IFRS purposes.

In addition to complying with regulatory provisions, the investment policy of Bayer Pensionskasse is geared toward managing the risk structure arising from its obligations. In light of capital market movements, the Bayer Pensionskasse has therefore developed a target strategic investment portfolio aligned to an appropriate risk structure. Its investment strategy focuses principally on stringent management of downside risks rather than on maximizing absolute returns. It is anticipated that this investment policy can generate a return that enables it to meet its long-term commitments.

All defined benefit plans necessitate actuarial computations and valuations. These are based not only on life expectancy, but also on the following parameters, which vary from country to country according to economic conditions:

	Parameters used	
	Dec. 31, 2002	Dec. 31, 2003
Discount rate	5.75% to 7.00%	5.50% to 6.25%
Projected future remuneration increases	3.00% to 4.75%	2.75% to 4.25%
Projected future pension increases	1.44% to 2.25%	1.25% to 2.75%
Projected employee turnover (according to age and gender)	Empirical data	
Expected return on plan assets	6.50% to 8.50%	6.25% to 8.25%

Obligations relating to early retirement benefits are calculated on the basis of the expected medium-term utilization using a discount rate of 3.5% (2002: 3.75%).

	Pension obligations		Other post-employment benefit obligations	
	Dec. 31, 2002	Dec. 31, 2003	Dec. 31, 2002	Dec. 31, 2003
	(in € millions)			
Defined benefit obligation				
Benefit obligation at start of year	992	1,007	91	90
Service cost	35	38	14	57
Interest cost	59	61	5	5
Employee contributions	9	10	—	—
Plan changes	2	2	—	—
Plan settlements	(21)	—	0	—
Net actuarial (gain) loss	2	31	(2)	8
Translation differences	(48)	(3)	(14)	(7)
Benefits paid	(28)	(28)	(6)	(7)
Mergers and acquisitions	—	—	—	—
Divestitures	—	—	—	—
Plan curtailments	5	—	2	—
Benefit obligation at year end	1,007	1,118	90	146
Fair value of plan assets				
Plan assets at start of year	844	748	—	—
Actual return on plan assets	(42)	42	—	—
Mergers and acquisitions	—	—	—	—
Divestitures	—	—	—	—
Plan settlements	(16)	0	—	—
Translation differences	(39)	1	—	—
Employer contributions	20	39	6	7
Employee contributions	9	10	—	—
Benefits paid	(28)	(28)	(6)	(7)
Plan assets at year end	748	812	0	0
Funded status	(259)	(306)	(90)	(146)
Unrecognized past service cost	2	1	—	—
Unrecognized transition obligation	—	—	—	—
Unrecognized actuarial (gain) loss	213	243	11	17
Asset limitation due to uncertainty of future benefits	(129)	(128)	—	—
Net recognized liability at year end	(173)	(190)	(79)	(129)
Amount recognized in the balance sheet				
Prepaid benefit assets	72	89	—	—
Provisions for pension and other post-employment benefits	(245)	(279)	(79)	(129)
Net recognized liability	(173)	(190)	(79)	(129)

Of the defined benefit obligations for pensions, €283 million (2002: €245 million) relates to unfunded benefit obligations, while €835 million (2002: €762 million) relates to funded benefit obligations. The defined benefit obligation for other post-employment benefits is completely unfunded at €146 million (2002: €90 million).

Of the funded pension plans, total overfunding of individual plans amounts to €60 million (2002: €67 million), while underfunding amounts to €83 million (2002: €79 million).

The adjustments, as yet unrecognized in the income statement, represent the difference between the defined benefit obligation — after deducting the fair value of plan assets — and the net liability recognized in the balance sheet. They arise mainly from actuarial gains or losses caused by differences between actual and previously assumed trends in employee turnover, income and development of plan assets. Pension assets in excess of the obligation are reflected in other receivables on the balance sheet, subject to the asset limitation specified in IAS 19 (Employee Benefits). In accordance with IAS 19, the amounts reflected on the balance sheet will be recognized in the income statement over the expected average remaining working lives of active employees. The portion of the net actuarial gain or loss to be recognized on the income statement is determined by the corridor method.

The net recognized liability is reflected in the following balance sheet items:

	2002	2003
	(in € millions)	
Provisions for pension and other post-employment benefits	(324)	(408)
Other assets	72	89
Net recognized liability	(252)	(319)

Provisions for pension and other post-employment benefits changed as follows in 2002 and 2003:

	Jan. 1, 2002	Changes in scope of consolidation	Currency effects	Allocations	Utilization	Reversal	Dec. 31, 2002
				(in € millions)			
Provision for pensions and other post-employment benefits	345	—	(12)	18	(27)	—	324

	Jan. 1, 2003	Changes in scope of consolidation	Currency effects	Allocations	Utilization	Reversal	Dec. 31, 2003
				(in € millions)			
Provision for pensions and other post-employment benefits	324	—	(5)	135	(46)	—	408

(27) Other provisions

The breakdown of other provisions is as follows:

	Dec. 31, 2002		Dec. 31, 2003	
	Total	Maturing within one year	Total	Maturing within one year
		(in € millions)		
Provisions for personnel commitments	173	53	234	73
Provisions for trade-related commitments	69	69	40	32
Provisions for environmental remediation	46	6	42	4
Provisions for taxes	17	7	22	11
Provisions for restructuring	18	18	21	21
Other provisions	41	40	46	12
	364	193	405	153

Changes in provisions in 2002 were as follows:

	Jan. 1, 2002	Changes in scope of consolidation	Currency effects	Allocations	Utilization	Reversal	Dec. 31, 2002
				(in € millions)			
Provisions for personnel commitments	162	—	(7)	37	(19)	—	173
Provisions for trade-related commitments	79	—	(4)	43	(41)	(8)	69
Provisions for environmental remediation	51	—	(8)	7	(4)	0	46
Provisions for taxes	22	—	(1)	24	(27)	(1)	17
Provisions for restructuring	38	—	(10)	15	(25)	—	18
Other	34	—	(2)	27	(18)	0	41
Total	386	—	(32)	153	(134)	(9)	364

Changes in provisions in 2003 were as follows:

	Jan. 1, 2003	Changes in scope of consolidation	Currency effects	Allocations	Utilization	Reversal	Dec. 31, 2003
				(in € millions)			
Provisions for personnel commitments	173	—	(4)	113	(42)	(6)	234
Provisions for trade-related commitments	69	—	(3)	37	(48)	(15)	40
Provisions for environmental remediation	46	—	(4)	2	(2)	0	42
Provisions for taxes	17	—	0	23	(17)	(1)	22
Provisions for restructuring	18	—	(3)	15	(9)	0	21
Other	41	—	0	38	(31)	(2)	46
Total	364	—	(14)	228	(149)	(24)	405

Participation programs

The Bayer Group's three-tier participation program for different classes of employees was launched in 2000. The program consists of a Stock Option Program for members of the Board of Management and other Group Executives, a Stock Incentive Program for other senior management and a Stock Participation Program for other managers and non-managerial staff. To be eligible for the Stock Option Program, Stock Incentive Program or Module 1 of the Stock Participation Program, participants must place Bayer AG shares of their own into a special deposit account.

Provided participants hold these shares for the full term of the Stock Incentive Program or the Stock Participation Program, they will receive specific payments from the company after defined retention periods. Under Module 2 of the Stock Participation Program, employees have the opportunity to purchase shares at a discounted price. To the extent that obligations under the employee participation programs exist toward employees of the LANXESS Subgroup, such obligations will have been or will be transferred to the LANXESS Subgroup.

Environmental provisions

The LANXESS Subgroup's activities are subject to extensive laws and regulations in the jurisdictions in which it does business or maintains properties. Its compliance with environmental laws and regulations may require it to remove or mitigate the effects of the disposal or release of chemical substances at various sites. Under some of these laws and regulations, a current or previous owner or operator of property may be held liable for the costs of removal or remediation of hazardous substances on, under, or in its property, without regard to whether the owner or operator knew of, or caused the presence of the contaminants, and regardless of whether the practices that resulted in the contamination were legal at the time they occurred. As many of its production sites have an extended history of industrial use, it is impossible to predict precisely what effects these laws and regulations will have on the LANXESS Subgroup in the future.

As is typical for companies involved in the chemical or related industries, soil and groundwater contamination has occurred in the past at some of the sites, and might occur or be discovered at other sites. The LANXESS Subgroup is subject to claims brought by federal and state regulatory agencies in the United States and other private entities and individuals regarding the remediation of sites and parcels, which the LANXESS Subgroup has purchased or will purchase from Bayer AG, on which materials were produced specifically for the LANXESS Subgroup by contract manufacturers or on which waste from the LANXESS Subgroup's operations was treated, stored or disposed of.

In particular, the LANXESS Subgroup may be exposed to potential liability under the U.S. Federal Comprehensive Environmental Response, Compensation and Liability Act, commonly known as ''Superfund'', the U.S. Resource Conservation and Recovery Act and related state laws for investigation and remediation costs at a number of sites. At most of these sites, numerous companies, including the LANXESS Subgroup, have been notified that the U.S. Environmental Protection Agency (EPA), state government regulators or private persons consider such companies to be potentially responsible parties under Super-fund and similar laws. At other U.S. sites, the LANXESS Subgroup is the sole responsible party. The proceedings relating to these sites are in various stages. In most cases, remediation measures have already been initiated.

As of December 31, 2003, the LANXESS Subgroup had set aside €42 million in provisions for environmental remediation (2002: €46 million). The main components of the provisions for environmental remediation costs relate primarily to land reclamation, rehabilitation of contaminated sites, recultivation of landfills, and redevelopment and water protection measures. The provisions for environmental remediation costs are recorded on a discounted basis where environmental inquiries or remediation measures are probable, the costs can be sufficiently reliably estimated and no future benefits are expected from such measures. Significant factors in estimating the costs include previous experiences in similar cases, expert opinions regarding environmental programs, current costs and new developments affecting costs, our interpretation of current environmental laws and regulations, the number and financial condition of third parties that may become obligated to participate in any remediation costs at the various sites on the basis of joint liability, and the remediation methods which are likely to be deployed.

It is difficult to estimate the future costs of environmental protection and remediation because of the many uncertainties, particularly with regard to the status of laws, regulations and information available about conditions in the various countries and at the individual sites. Subject to these factors, but taking into consideration its experience to date regarding environmental matters of similar nature, the LANXESS Subgroup believes that the provisions are adequate based on currently available information. However, given the inherent difficulties in estimating liabilities in this area, it cannot be guaranteed that additional costs will not be incurred beyond the amounts accrued. It is possible that a final resolution of these matters may require expenditures in excess of the established provisions, over an extended period of time and in a range of amounts that cannot be reasonably estimated. Nevertheless, management believes that such additional amounts, if any, would not have a material adverse effect on the Group’s financial position or results of operation.

Litigation risks

The LANXESS Subgroup or LANXESS Group, as the case may be, is involved in a number of legal proceedings, either directly or indirectly by way of indemnity claims Bayer has against it. As a global chemical company, it is currently exposed to, and may in the future become involved in proceedings in the ordinary course of its business relating to such matters as competition or antitrust law or its past waste disposal practices and release of chemicals into the environment.

The outcome of current and future litigation cannot be predicted with certainty. Thus, an adverse decision in a lawsuit could result in additional costs that are not covered, either wholly or partially, under insurance policies and that could significantly impact the business and results of operations of the LANXESS Subgroup or LANXESS Group, as the case may be. If the LANXESS Subgroup or LANXESS Group, as the case may be, loses a case in which it seeks to enforce its patent rights, a decrease in future earnings could result as other manufacturers could be permitted to begin to market products that the LANXESS Group or its predecessors had developed.

Litigation and other judicial proceedings as a rule raise difficult and complex legal issues and are subject o t many uncertainties and complexities including, but not limited to, particularities regarding the facts and circumstances of each particular case, issues regarding the jurisdiction in which each suit is brought and applicable law. Upon resolution of a pending legal matter, the future LANXESS Subgroup or LANXESS Group may be forced to incur charges in excess of the presently established provisions and related insurance coverage. It is possible that the results of operations and cash flows could be materially affected by an ultimately unfavorable outcome of litigation.

Regarding the current antitrust litigation risks, see the Note on commitments and contingencies (Note (33)).

Expenses for restructuring

Restructuring charges totaling €144 million were incurred in 2002 for the shutdown of sites and relocation of business operations, including €15 million in provisions that are expected to be utilized as the respective restructuring measures are implemented. The total charges include accelerated amortization/depreciation and write-downs of property, plant and equipment and intangible property totaling €74 million, severance payments totaling €7 million and other expenditures totaling €63 million. The majority of the severance payments and other expenses incurred in 2002 resulted in disbursements in 2003.

In connection with the restructuring of the Canadian production facility for rubber in Sarnia, Ontario, special charges totaling €41 million were incurred as well as severance payments of €7 million and other expenditures totaling €19 million.

In 2002, €36 million in restructuring charges were incurred in connection with the partial closing and sale of the organic pigments production facility in Bushy Park, South Carolina. Of this amount, €23 million relate to write-downs and €13 million were used to cover other expenses.

Other restructuring related to the closing of a production line for ferric-oxide in New Martinsville involving write-offs totaling €10 million and other expenses totaling €20 million, with the restructuring of the Technical Rubber Products segment in Leverkusen (€11 million charge). The provisions and expenses for restructuring changed in 2002 as follows:

	Severance payments	Other costs	Total
	(in € millions)		
Status Jan. 1, 2002	11	27	38
Additions	0	15	15
Utilization	(6)	(19)	(25)
Exchange differences	(1)	(9)	(10)
Status Dec. 31, 2002	4	14	18

In 2003, total expenses for restructuring measures were €48 million. Of this amount, €15 million was set aside as restructuring provisions and €12 million as other provisions. The total expenses include severance payments and other pre-retirement part-time work benefits made in connection with the restructuring and totaled €37 million, as well as accelerated depreciation/amortization and write-down of property, plant and equipment and intangible assets totaling €11 million. The majority of the severance payments and other expenses incurred in 2003 are to be disbursed in 2004.

In connection with the closing of the Goch and Marl production sites, expenses totaling €12 million and €11 million, respectively, were incurred for severance payments and other write-offs.

As part of a global reorganization, personnel changes were made at several sites, costing a total of €25 million.

Changes in provisions for restructuring in 2003 were as follows:

	Severance payments	Other costs	Total
	(in € millions)		
Status Jan. 1, 2003	4	14	18
Additions	15	0	15
Utilization	(3)	(6)	(9)
Exchange differences	0	(3)	(3)
Status Dec. 31, 2003	16	5	21

Other costs are mainly demolition expenses and other charges relating to the abandonment of production facilities.

(28) Financial obligations

Financial obligations comprise the following:

	Dec. 31, 2002		Dec. 31, 2003	
	Total	Maturing in 2002	Total	Maturing in 2003
	(in € millions)			
Liabilities to banks	25	25	41	3
Liabilities under lease agreements	104	11	86	9
Other financial obligations	1,291	938	1,315	1,221
	1,420	974	1,442	1,233

The maturities of financial obligations existing as of December 31, 2003 were as follows:

Maturing in	In € millions
2004	1,233
2005	23
2006	36
2007	5
2008	42
2009 or later	103
	1,442

On the basis of the net indebtedness targeted at the time the Spin-off becomes legally effective, all financial obligations directly allocable to the LANXESS Subgroup and included in the historical financial statements of the so-called share deal companies were allocated to the LANXESS Subgroup. In order to achieve the targeted overall indebtedness for the LANXESS Subgroup, some external debt was assumed o t exist, which currently is classified as a short-term financial obligation. Short-term financial obligations totaled €1,233 million (2002: €974 million). Their weighted average interest rate was 4.6 percent (2002: 5.8 percent). The financial obligations allocable to the LANXESS Subgroup are mostly unsecured and of equal priority.

Liabilities under finance leases are recognized as financial obligations if the leased assets are capitalized under property, plant and equipment as the group is deemed the economic owner of the leased property (finance leases). They are stated at their present value. Future lease payments amount to €116 million (2002: €134 million). The interest component contained in such lease payments is €30 million (2002: €30 million).

The liabilities associated with finance leases mature as follows:

	Lease payments	Of which interest	Lease liability
		(in € millions)	
2004	13	4	9
2005	13	4	9
2006	18	5	13
2007	8	3	5
2008	5	2	3
After 2008	59	12	47
	116	30	86

Lease payments in 2003 in connection with operating leases amounted to €29 million (2002: €10 million). No other financial obligations to subsidiaries or to companies of the Bayer Group were reported.

(29) Trade account payables

Trade accounts payables were mainly to third parties. As in the previous year, the total amount of €574 million (2002: €428 million), is due within one year. Trade accounts payable to other affiliated companies totaled €7 million (2002: €2 million), and trade accounts payable to other suppliers totaled €567 million (2002: €426 million). There were no trade accounts payable to subsidiaries. Trade accounts payable to companies belonging to the Bayer Group, which the LANXESS Subgroup classifies as third parties, totaled €142 million (2002: €20 million).

(30) Miscellaneous liabilities

Miscellaneous liabilities are carried at amortized cost.

They are comprised as follows:

	Dec. 31, 2002		Dec. 31, 2003	
	Total	Maturing in 2002	Total	Maturing in 2003
	(in € millions)			
Payroll liabilities	49	48	40	39
Tax liabilities	33	33	32	32
Liabilities for social expenses	17	17	15	15
Accrued interest on liabilities	3	3	2	2
Advance payments received	2	2	3	3
Liabilities from the acceptance of drafts	11	11	12	12
License liabilities	2	2	—	—
Other miscellaneous liabilities	96	96	84	84
	213	212	188	187

Tax liabilities include not only the Group companies' own tax liabilities, but also taxes withheld on behalf of third parties.

Liabilities for social expenses include, in particular, social insurance contributions that have not yet been paid by the closing date.

The other miscellaneous liabilities comprise mainly guarantees, commissions to customers and expense reimbursements.

Total miscellaneous liabilities include €2 million (2002: €1 million) to subsidiaries and €38 million to companies belonging to the Bayer Group (2002: €22 million), which the LANXESS Subgroup classifies as third parties. Miscellaneous liabilities to other affiliated companies did not exist.

(31) Further information on liabilities

Other liabilities include €104 million (2002: €205 million) with maturities of more than five years.

Liabilities totaling €189 million (2002: €1 million) were secured, of which €22 million (2002: €1 million) were secured by mortgages.

The total amount of liabilities includes €2 million (2002: €3 million) in accrued interest, representing expenses attributable to the fiscal year, but not due for payment until after the closing date.

(32) Deferred income

Deferred income as of December 31, 2003, includes €56 million (2002: €56 million) in grants and subsidies received from government. The amount reversed and recognized in income in 2003 was €9 million (2002: €10 million).

(33) Commitments and contingencies

Contingent liabilities as of December 31, 2003 — all of which existed toward third parties — amounted to €13 million (2002: €14 million). They resulted from:

	Dec. 31, 2002	Dec. 31, 2003
	(in € millions)	
Issuance and endorsement of bills	1	0
Guarantees	10	8
Warranties	3	5
	14	13

These items refer to potential future obligations where the occurrence of future events would create an obligation, the existence of which is uncertain as of the balance sheet date. Companies often enter into warranty obligations related to business transactions. These mainly comprise commitments undertaken by subsidiaries for a defined level of performance or the rendering of specific services that go beyond the degree of liability ordinarily assumed in the respective industry. Guarantees comprise mainly bank guarantees where subsidiaries guarantee third parties' liabilities to banks resulting from contractual agreements of those third parties with the LANXESS Subgroup. A liability to perform under the guarantee arises if the debtor is in arrears on payments or is insolvent.

In addition to provisions, other liabilities and contingent liabilities, there are also other financial commitments, including those arising under lease and long-term rental agreements.

The minimum non-discounted future payments relating to operating leases total €67 million (2002: €43 million). The respective payment obligations mature as follows:

Maturing in	In € millions
2004	11
2005	10
2006	9
2007	9
2008	8
2009 or later	20
	67

Financial commitments resulting from orders already placed under purchase agreements related to planned or ongoing capital expenditure projects totaled €37 million (2002: €37 million). The respective payments are due in full in 2004.

In addition, research agreements have been concluded with a number of third parties under which various research projects are funded or commitments are assumed subject to certain agreed conditions. The total amount of such funding and other commitments is €2 million (2002: €5 million). As of December 31, 2003, the remaining payments expected to be made to these parties, assuming the agreed conditions are met, were as follows:

Maturing in	In € millions
2004	2
2005	0
2006	0
2007	0
2008	0
2009 or later	0
	2

Section 133 (1) sentence 1 of the German Transformation Act states that all legal entities involved in a spin-off will be jointly and severally liable for all of the transferring entity's debts and liabilities existing at the time that the spin-off takes effect. This means that Bayer AG and LANXESS AG will be jointly and severally liable for all liabilities of Bayer AG existing at the time that the LANXESS Subgroup was spun off. In accordance with Section 133 (3) of the German Transformation Act, the period of liability for the company to which the liabilities were not assigned under the Spin-Off and Acquisition Agreement, will be limited to five years.

The Spin-Off and Acquisition Agreement provides that Bayer AG will indemnify LANXESS AG against statutory joint liability pursuant to Section 133 of the German Transformation Act for obligations and liabilities that were not transferred to LANXESS AG pursuant to the Spin-Off and Acquisition Agreement.

Additional details on the topic of liability are contained in Chapter VIII of the Joint Spin-Off Report.

Description of the Master Agreement

In the Master Agreement to be entered between Bayer AG and LANXESS AG contemporaneously with the Spin-Off and Acquisition Agreement, Bayer AG and LANXESS AG will agree, among other things, on how to apportion general liability and liabilities arising specifically under environmental, product liability and antitrust law. The following is a description of the key provisions of the Master Agreement related to these liabilities.

Apportionment of liability

Bayer AG and LANXESS AG will agree in the Master Agreement that LANXESS AG and its affiliates will be responsible only for the liabilities assigned to them and that conversely Bayer AG and its affiliates will be responsible for the liabilities not assigned to the future LANXESS Group. To achieve this goal, the Master Agreement contains corresponding indemnity obligations of Bayer AG and LANXESS AG.

Environmental liability

The Master Agreement governs how liability will be shared among the contracting parties on any environmental contamination of real estate, which was caused or arose prior to the Spin-off Economic Effective Date (July 1, 2004). The legal consequence of any liability of a contracting party is as a rule that such party will be obligated to indemnify the other contracting party and its affiliates to the full extent with respect to any and all public or private liability to government agencies or to other third parties for environmental contamination on the relevant real estate. The provision concerning the apportionment of liability for environmental contamination essentially establishes a liability of each contracting party based on the condition of the properties that such party and its affiliates used on the Spin-Off Economic Effective Date. In addition, the liability provision also contains individual elements of causation-based liability. Consequently, liability attaches to the affected property as follows (in simplified terms):

LANXESS AG will generally be, subject to certain opportunities for exoneration, liable for any and all environmental contamination of the so-called ''LANXESS properties''. ''LANXESS properties'' consist primarily of real estate, which the LANXESS Subgroup uses both in Germany and abroad as of the SpinOff Economic Effective Date and which the companies of the future LANXESS Group have either already purchased from Bayer AG (primarily the properties located abroad) or will still purchase from Bayer AG under land purchase contracts (for example, in Germany). In contrast, Bayer AG will generally be liable for any and all environmental contamination of the so-called ''BAG-properties'', likewise subject to certain opportunities for exoneration. This real estate involves primarily the real property owned or used by Bayer AG or its affiliates (excluding the LANXESS properties). With respect to any liability for environmental contamination of real estate owned by third parties, the contracting parties agree that LANXESS AG will be liable for such environmental contamination, if the environmental contamination was caused by a LANXESS-property (*via* the groundwater), and Bayer AG will be liable if the environmental contamination was caused by a BAG-property (*via* the groundwater). In addition, the Master Agreement also provides special rules regarding the apportionment of liability with respect to the environmental contamination of certain properties (including landfills) as well as environmental liability based on certain acquisition contracts.

The Master Agreement will cap liability of LANXESS AG and its affiliates for environmental contamination at €350 million. However, in simplified terms, this liability cap relates only to remedial action ordered, agreed upon or actually carried out before the end of 2009. Otherwise, LANXESS AG and its affiliates shall bear unlimited liability for environmental contamination.

Product liability

The Master Agreement governs the apportionment of product liability among the contracting parties, but only in respect of claims brought by third parties and not by the contracting parties against one another. The contracting parties agreed to waive the enforcement of such latter claims against one another. If one contracting party is held liable for product liability, it will be obligated to indemnify the other contracting party and its affiliates with respect to the relevant product liability claim. Following are the key provisions of the Master Agreement regarding the apportionment of liability:

The LANXESS Subgroup, on the one hand, and the future Bayer Group, on the other hand, will generally each be responsible for any and all product liability claims arising out of or connected with defective products, which their respective units (active as of the Spin-Off Economic Effective Date) introduced to the market or which they will have introduced to the market prior to the consummation date. The products introduced to the market by the relevant unit are identified, among other things, on the basis of so-called ''UVP numbers'' assigned to each product. The Master Agreement does not contain separate provisions governing product liability arising out of or connected with defective products introduced to the market on or after the consummation date and instead references the rules of the applicable legal system. In addition, the Master Agreement contains special provisions regarding defective products introduced to the market by certain sold companies, business units, production facilities and plants, and allocates such product liability to LANXESS AG. In addition, the Agreement also contains a special provision, pursuant to which product liability for certain products — specifically products which have been produced by discontinued business units and business groups at the Bayer Group that are allocable to the LANXESS Subgroup — is assigned to LANXESS AG.

Antitrust violations

The Master Agreement governs the apportionment of liability for violations of antitrust laws as between the contracting parties. Antitrust liabilities are obligations or liabilities to pay fines, pecuniary and other (additional) penalties relating to damage claims of third parties including payment of criminal sanctions, third party claims for the transfer of surplus proceeds or advantages arising out of antitrust violations.

The future LANXESS Subgroup will be liable to the Bayer Group for liabilities arising out of antitrust violations committed by the LANXESS Subgroup. Conversely, the Bayer Subgroup will be liable for any liabilities arising out of antitrust violations it commits. The liable party will be responsible for reimbursing the other party for any expenses incurred as necessary to fulfill the antitrust liabilities.

In addition to these general principles, there are special provisions for antitrust proceedings and civil litigation in connection with certain products sold by the former Rubber business division that are assigned to the LANXESS Subgroup. With respect to these products, Bayer AG and a number of its affiliates are involved in criminal or civil investigations, particularly in the United States, Canada and Europe. Where, in each case before July 1, 2004, regulatory proceedings have been at least commenced or if a company has taken steps before an antitrust authority with a view to commencing proceedings, any liability arising is to be apportioned as between the parties, so that the LANXESS Group assumes 30 percent of the liabilities and the Bayer Group 70 percent.

The reimbursement obligation of the LANXESS AG is generally limited to €100 million. Any tax disadvantages arising out of the non-deductibility or limited deductibility must be reimbursed and will not count towards the cap. In addition to the liability cap, there is a €50 million cap for payments per calendar year; any balance will be carried forward to the subsequent year.

Also subject to the reimbursement provision is a proceeding arising out of allegations concerning antitrust violations in the Rubber Chemicals business unit between 1995 and 2001, in respect of which Bayer AG announced on July 14, 2004 that it had reached a settlement with the U.S. Department of Justice. Bayer AG agreed to plead guilty and to pay $66 million. A provision was set aside for this purpose during the second quarter of 2004.

Costs for external assistance in these proceedings are likewise shared between the parties on a 30:70 basis. These amounts will not, however, count towards the liability cap.

Any antitrust obligations and environmental contamination attributable to the divisions of the LANXESS Group based or operating in the United States will be included in the calculation of the relevant liability cap. In light of the special legal situation in the United States, contracts have already been executed with respect to such LANXESS Group divisions, containing provisions that are not always congruent with the provisions of the Master Agreement. Bayer AG and LANXESS AG have undertaken to ensure that the agreements entered into in the United States would be modified, in case of material discrepancies, in accordance with the fundamental rules of the Master Agreement.

(34) Related Parties

In the course of its operations, the LANXESS Subgroup sources its materials, inventories and services from a large number of business partners. These include companies in which Bayer AG holds an interest, and companies with which members of the Supervisory Board of Bayer AG are associated.

Business and legal relations exist between the remaining Bayer Group and the LANXESS Group. These relationships will continue to exist after the Spin-off enters into effect. These relationships include contracts for the delivery of goods and services between the Bayer subgroups and the Bayer service companies, on the one hand, and the LANXESS Subgroup, on the other hand.

On the basis of these goods and service contracts, the companies of the Bayer Group supplied approximately €0.5 billion worth of goods and other services to companies of the LANXESS Group in 2003. Most of these services relate to the supply of products such as chlorine and sodium hydroxide, the majority of these goods being supplied by the Bayer MaterialScience Subgroup. Services will also be provided t o the LANXESS Group (excluding services provided by Bayer Industry Services GmbH & Co. OHG). The majority of these services are rendered by Bayer Business Services GmbH in the fields of IT Systems Development & Application Support, IT Infrastructure, Human Resource Payroll & Pensions and Customs & Excise. The LANXESS Group will procure engineering services from Bayer Technology Services GmbH. Moreover, various goods and services will be purchased in different countries, including custom manufacturing and other services.

In addition, the LANXESS Group purchased €0.5 billion of on-site services from Bayer Industry Services GmbH & Co OHG in the areas of energy, infrastructure and waste disposal. The companies of the LANXESS Group supplied goods and other services totaling approximately €0.7 billion to companies of the Bayer Group in 2003. Most of the goods and services were supplied to the subgroups Bayer MaterialScience and Bayer CropScience.

To the extent the chemicals or polymer businesses to be transferred to the LANXESS Group did not have the necessary presence in a given country, distributions totaling €0.8 billion in sales were consummated primarily on the basis of commercial agency and, in some cases, on the basis of exclusive dealer arrangements with Bayer companies. In contrast, the use of the LANXESS organization for purposes of selling Bayer products was only of minor significance.

Once the Spin-off becomes effective and the transfer of the LANXESS Subgroup is thereupon complete, Bayer AG will no longer hold any ownership interests in LANXESS Subgroup companies and will therefore no longer be able to exercise any ownership control over such companies. The relationship between the Bayer Group and the LANXESS Group will correspond to that between two independent companies pursuing their own business interests.

(35) Financial instruments

Primary financial instruments are reflected in the balance sheet. In accordance with IAS 39 (Financial Instruments: Recognition and Measurement), financial assets are categorized as either ''held for trading'', ''held to maturity'', or ''available for sale'' and, accordingly, recognized at fair value or amortized cost. Changes in the fair value of available-for-sale securities are recognized in stockholders' equity. In the event of impairment losses, the assets are written down and the write-downs are recognized in income. Financial instruments constituting liabilities are carried at amortized cost.

a) Risks and risk management

The global nature of the LANXESS Subgroup's business exposes its operations, financial results and cash flows to a range of risks. Such risks include the following:

- Currency risks:
  The LANXESS Subgroup is exposed to exchange rate fluctuations between the euro and other major currencies.
- Interest rate risks:
  The LANXESS Subgroup is exposed to changes in interest rates.
- Credit risks:
  The LANXESS Subgroup is subject to credit risks with respect to the counterparties in its transactions.
- Raw material and energy price risks:
  The LANXESS Subgroup is subject to possible increases in raw material prices and energy prices.

The risks mentioned above could adversely affect the results of operations and financial condition of the LANXESS Subgroup. The description below focuses on the individual risks and on the LANXESS Subgroup's risk management.

Currency risk

Since the LANXESS Subgroup transacts business in many different currencies, it is exposed to a variety of risks associated with fluctuations in the relative values of these currencies.

Transaction risk

Currency risks (i.e., the potential depreciation in the value of a financial instrument as a result of changes in the exchange rate) arise especially when receivables or payables are denominated in a currency other than the company's local currency.

The risks from the operating activities are systematically recorded and analyzed. Decisions about the scope of hedging of such risks are taken regularly. Such hedging may also cover anticipated transactions. A material portion of the contractual and foreseeable currency risks are hedged by using derivative instruments. Changes in the fair value of these instruments are recognized in the income statement or, in the case of cash flow hedges, under ''other changes in stockholders' equity''. Since the LANXESS Subgroup enters into derivative transactions for a significant portion of its currency risks, the Subgroup believes that a significant increase or decrease in the exchange rate of the euro relative to other major currencies would not, in the short term, materially affect its future cash flow. Over time, however, to the extent the LANXESS Subgroup is unable to reflect exchange rate movements in, for example, the pricing of its products in the local currency, they could adversely affect its cash flows.

Currency risks from financial transactions, including interest, are generally hedged at 100 percent. Cross-currency interest rate swaps and forward exchange contracts are the main hedging instruments used.

Investments in long-term securities and other loans are made primarily in the currency zone of the group company making the investment in order to minimize the currency risk.

Translation risk

Many of the companies within the LANXESS Subgroup are located outside the euro zone. Since the euro is the Subgroup's financial reporting currency, the annual financial statements of these subsidiaries were translated into euro for inclusion in the Combined Financial Statements. Period-to-period changes in the average exchange rate for a particular country's currency can significantly affect the translation into euro of both revenues and operating income denominated in that currency. Unlike transaction risk, translation risk exposure does not affect the Subgroup's local currency cash flows.

Outside the euro zone, the LANXESS Subgroup holds significant assets, liabilities and operations denominated in local currencies. Although the long-term currency risk inherent in these investments is regularly assessed and evaluated, the Subgroup generally only enters into foreign exchange transactions covering this type of risk when it is considering withdrawal from a specific venture and repatriation of the funds that the withdrawal generates. Nevertheless, the Subgroup recognizes in equity the effects of currency fluctuations on the translation of net asset amounts into euro.

Interest rate risk

Interest rate risk — i.e., the possibility that the total return of a financial instrument will change due to movements in market interest rates — primarily affects financial assets and liabilities.

Where the LANXESS Subgroup does not completely abstain from hedging against interest rate fluctuations due to favorable fixed interest rates, it primarily uses derivative financial instruments to hedge interest rate risk, including interest and interest currency swaps.

The targeted net indebtedness of the future LANXESS Group is presented by means of centralized external borrowings. Interest expense computed for these purposes is based on the market interest rates for industrial bonds at the lower end of the investment grade range. These interest rates were computed by averaging the rates charged on a short-term instrument and a five-year term instrument. A risk premium was added to account for non-euro denominated financing. Based on this assumption, the Combined Financial Statements do not include any interest rate derivative instruments.

Other loans primarily consist of loans to employees, most of which have been issued at market-oriented, fixed interest rates. Due to their fixed interest rates, these loans are generally subject to interest rate risk, which, because it is assumed for overriding reasons, is not hedged. More than three quarters of the employee loans have terms of over five years.

Credit risk

Credit risk is the risk that counterparties cannot meet their obligations to the LANXESS Subgroup in transactions involving financial instruments. Since the LANXESS Subgroup does not conclude master-netting arrangements with its transaction partners, the total of the amounts recognized in assets represents its maximum exposure to credit risk.

Raw material risks

The LANXESS Subgroup is exposed to market price risks with regard to commodities used in its operating business. In connection with the spin-off, the LANXESS Subgroup is in the process of developing a comprehensive strategy for minimizing these risks through financial measures, including the use of derivative financial instruments. In 2003, based on the Subgroup's own market assessment, certain financial instruments were executed in order to factor in anticipated or actual price developments during the year. Fair value changes in the derivative financial instruments used to hedge commodity prices are recognized in the income statement.

b) Derivative financial instruments

Only derivate instruments used by existing legal entities that conducted solely LANXESS-related business were included in the Combined Financial Statements. In this context, fair values totaling

€4 million were recognized on the balance sheet in 2003. ''Regular-way'' purchases and sales of financial assets were recognized using settlement date accounting in accordance with IAS 39.

NOTES TO THE CASH FLOW STATEMENT

(36) Cash inflow from operating activities

The cash flow statement begins with the operating result (EBIT). The gross cash flow totaling €223 million (2002: €423 million) shows the cash surplus from operating activities before any changes in working capital. It is broken down on page F-9 according to reporting unit. The net cash generated (cash inflow) from operating activities equaled €346 million (2002: €369 million) and was included under changes in working capital.

(37) Cash inflow/outflow from investing activities

A cash amount totaling €370 million (2002: €414 million) was used to purchase property, plant and equipment in 2003. Cash totaling €65 million (2002: €62 million) was generated from the sale of property, plant and equipment, as well as other assets, whereas cash generated from interest and dividend income totaled €5 million (2002: €5 million). Investing activities produced a net cash outflow of €300 million (2002: €347 million).

(38) Cash inflow/outflow from financing activities

Financing activities generated a net cash outflow of €46 million in 2003 (2002: €25 million outflow). Net borrowings produced €23 million in cash inflow (2002: €51 million). Interest expenses led to a €69 million cash outflow (2002: €76 million).

(39) Cash and cash equivalents

Cash and cash equivalents included checks, petty cash and accounts at financial institutions and totaled €13 million (2002: €10 million). In accordance with IAS 7 (Cash Flow Statements), this item also includes financial securities with original maturities of up to three months.

NOTES ON SEGMENT REPORTING

In accordance with IAS 14 (Segment Reporting), a breakdown of certain data by segment and geographical region is provided in the financial statements. The segments and regions are the same as those used for internal reporting, allowing a reliable assessment of the Group's risks and returns. The aim is to provide transparency on the profitability and future prospects of the Group's various activities.

The LANXESS Subgroup comprises a number of strategic business entities, which are grouped together into reporting segments according to the economic characteristics of the business, types of products, production processes and customer relationships, and methods of distribution. As of December 31, 2003, the LANXESS Subgroup comprised the following four reporting segments:

Segments	Activities
Chemical Intermediates	Basic chemicals as leading global commodity supplier, fine chemicals as raw materials and intermediates for pharmaceutical, agricultural and specialty chemicals, as well as inorganic pigments for coloring concrete, emulsion paints and other coatings
Performance Chemicals	Material protection products, additives for the leather, textile and paper industries, ion exchange resins for water treatment, synthetic elastic fibers for fashion apparel, as well as additives for plastics, such as flame retardants and plasticizers
Engineering Plastics	Thermoplastics for high-tech applications for the automotive, household goods, leisure and electronics industries
Performance Rubber	Specialty rubbers and rubber chemicals for high-end rubber products, such as those used in automobiles, construction and footwear

The **reconciliation** eliminates inter-segment items and reflects income, expenses, assets and liabilities not directly allocable to segments. These include, in particular, the Corporate Center, the service companies and sideline operations.

Auditor's Report

We have audited the combined financial statements of the LANXESS Group, comprising the balance sheet, the income statement, the statement of changes in stockholders' equity and the statement of cash flows as well as the notes to the combined financial statements for the period from January 1, 2003 to December 31, 2003. The preparation and the content of the combined financial statements according to the International Financial Reporting Standards of the IASB (IFRS) under consideration of the included business and business-partitions as explained in the notes to the combined financial statements are the responsibility of the Board of Management of Bayer AG, Leverkusen. Our responsibility is to express an opinion, based on our audit, on the combined financial statements.

We conducted our audit in accordance with the International Standards on Auditing (ISA). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the combined financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the combined financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Board of Management, as well as evaluating the overall presentation of the combined financial statements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, based on our audit, the combined financial statements give a true and fair view of the financial position of the LANXESS Group as of December 31, 2003, and of the results of its operations and its cash flows for the period from January 1, 2003 to December 31, 2003 in accordance with IFRS.

Without qualifying our opinion we refer to the specific definitions and valuations on which the preparation of the combined financial statements are based and which are summarized in the notes to the combined financial statements. Furthermore, we draw your attention to the note to the cash flow statement, in which the revision of the previously-issued combined financial statements audited by us with report dated September 20, 2004 is described. The revision relates to an overstatement of cash flows from investing activities by €94 million and an overstatement of depreciation in the combined financial statements by €40 million and affects solely the period ended December 31, 2002.

Essen Januar 17, 2005

PwC Deutsche Revision
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

(P. Albrecht)	(V. Linke)
Certified Public Accountant	Certified Public Accountant

Unaudited Interim Combined Financial Statements (IFRS) of the LANXESS Group as of September 30, 2004

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LANXESS
Combined Statements of Income

	September 30, 2003	September 30, 2004
	(in € millions)	
Net sales	4,828	5,047
Cost of goods sold	(3,919)	(3,937)
Gross profit	909	1,110
Selling expenses	(683)	(638)
Research and development expenses	(118)	(95)
General administration expenses	(162)	(196)
Other operating income	41	97
Other operating expenses	(64)	(202)
Operating Result [EBIT]	(77)	76
Income (expense) from investments in affiliated companies — net	(17)	2
Interest expense — net	(43)	(37)
Other non-operating expenses — net	(32)	(23)
Non-operating result	(92)	(58)
Income (loss) before income taxes	(169)	18
Income taxes	60	(21)
Income (loss) after taxes	(109)	(3)
Minority stockholders' interest	(4)	(5)
Net income (loss)	(113)	(8)
Earnings per share (€)	(1.55)	(0.11)
Diluted earnings per share (€)	(1.55)	[1]

1) In connection with the issuance of the convertible bond within the 3rd Quarter 2004 the diluted EPS will not correspond with the EPS. A calculation of the diluted EPS is not feasible due to the fact that the spin-off of Lanxess has not yet become effective.

LANXESS
Combined Balance Sheets

	September 30, 2003	September 30, 2004
	(in € millions)	
ASSETS		
Noncurrent assets		
Intangible assets	285	69
Property, plant and equipment	2,387	1,510
Investments	52	96
	2,724	1,675
Current assets		
Inventories	1,187	1,204
Receivables and other assets		
Trade accounts receivable	1,049	1,217
Short-term loans	243	0
Other receivables and other assets	256	351
	1,548	1,568
Marketable securities and other instruments	0	0
Cash and cash equivalents	14	80
Liquid assets	14	80
	2,749	2,852
Deferred taxes	17	143
Deferred charges	27	13
Total assets	5,517	4,683
STOCKHOLDERS' EQUITY AND LIABILITIES		
Stockholders' equity		
Capital	2,729	1,732
Net income (loss)	(113)	(8)
Currency translation adjustment	(322)	(358)
Miscellaneous items	0	0
	2,294	1,366
Minority stockholders' interest	41	34
Liabilities		
Long-term liabilities		
Long-term financial obligations	173	336
Miscellaneous long-term liabilities	1	2
Provisions for pensions and other post-employment benefits	361	412
Other long-term provisions	186	226
	721	976
Short-term liabilities		
Short-term financial obligations	1,297	1,059
Trade accounts payable	484	652
Miscellaneous short-term liabilities	177	238
Short-term provisions	231	286
	2,189	2,235
	2,910	3,211
Deferred taxes	218	28
Deferred income	54	44
	5,517	4,683

LANXESS
Combined Statements of Changes in Stockholders' Equity

	Capital	Net income (loss)	Currency translation adjustment	Miscellaneous items	Total
			(in € millions)		
December 31, 2002	2,848	(119)	(264)	0	2,465
Dividend payments					0
Allocation to retained earnings	(119)	119			0
Exchange differences			(58)		(58)
Other differences					0
Net income (loss)		(113)			(113)
September 30, 2003	2,729	(113)	(322)	0	2,294
December 31, 2003	2,729	(997)	(374)	0	1,358
Dividend payments					0
Allocation to retained earnings	(997)	997			0
Exchange differences			16		16
Other differences					0
Net income (loss)		(8)			(8)
September 30, 2004	1,732	(8)	(358)	0	1,366

LANXESS Combined Statements of Cash Flows

	September 30, 2003	September 30, 2004
	(in € millions)	
Operating result (EBIT)	(77)	76
Income taxes	5	(52)
Depreciation and amortization	377	249
Change in provisions for pensions and other post employment benefits	9	(27)
Losses on retirements of noncurrent assets	2	6
Gross cash provided by operating activities	316	252
Increase in inventories	(91)	(142)
Increase in trade accounts receivable	(24)	(184)
Increase (decrease) in trade accounts payable	(11)	26
Changes in other working capital	15	88
Net cash provided by operating activities	205	40
Cash outflows for additions to property, plant and equipment	(193)	(158)
Cash inflows from sales of property, plant and equipment	65	29
Cash inflows (outflows) for investments	(23)	208
Cash outflows for acquisitions less acquired cash	0	0
Interest and dividends received	3	6
Net cash inflow (outflow) from marketable securities	0	0
Net cash provided by (used in) investing activities	(148)	85
Changes in stockholders' equity	0	0
Issuances of debt	109	570
Retirements of debt	(107)	(581)
Interest paid	(58)	(48)
Net cash used in financing activities	(56)	(59)
Change in cash and cash equivalents due to business activities	1	66
Cash and cash equivalents at beginning of year	10	13
Change in cash and cash equivalents due to changes in scope of consolidation	3	1
Change in cash and cash equivalents due to exchange rate movements	0	0
Cash and cash equivalents September 30	14	80
Marketable securities and other instruments	0	0
Liquid assets as per balance sheets	14	80

Notes Subgroup LANXESS

Key Data by Segment and Region

Key Data by Segments

Segments	Chemical Intermediates 9 months 2003	Chemical Intermediates 9 months 2004	Performance Chemicals 9 months 2003	Performance Chemicals 9 months 2004	Engineering Plastics 9 months 2003	Engineering Plastics 9 months 2004	Performance Rubber 9 months 2003	Performance Rubber 9 months 2004	Reconciliation 9 months 2003	Reconciliation 9 months 2004	LANXESS 9 months 2003	LANXESS 9 months 2004
						(in € millions)						
Net sales	1,080	1,102	1,501	1,459	1,060	1,281	1,038	1,046	149	159	4,828	5,047
Intersegment sales	61	70	5	12	2	15	3	3	(71)	(100)		
Operating result [EBIT]	33	46	51	(8)	(57)	16	(51)	42	(53)	(20)	(77)	76
Net cash flow	127	47	7	12	41	(16)	88	7	(58)	(10)	205	40
Total assets	1,182	916	1,392	1,194	1,330	1,080	1,289	1,062	324	431	5,517	4,683
Amortization and depreciation	106	86	80	76	89	22	88	55	14	10	377	249
Liabilities	213	265	380	484	316	402	319	402	1,954	1,730	3,182	3,283

Key Data by Regions

Regions	Europe 9 months 2003	Europe 9 months 2004	North America 9 months 2003	North America 9 months 2004	Asia/Pacific 9 months 2003	Asia/Pacific 9 months 2004	Latin America/ Africa/ Middle East 9 months 2003	Latin America/ Africa/ Middle East 9 months 2004	Reconciliation 9 months 2003	Reconciliation 9 months 2004	Lanxess 9 months 2003	Lanxess 9 months 2004
						(in € millions)						
Net sales by market	2,720	2,804	1,053	1,058	672	750	383	435			4,828	5,047
Total assets	3,615	2,957	1,256	985	345	304	205	184	96	253	5,517	4,683

Notes to the Interim Report for the Period ending September 30, 2004

The unaudited Combined Financial Statements of the LANXESS Subgroup for the period ending September 30, 2004 were prepared according to the same principles as the LANXESS Subgroup's Combined Financial Statements for the year 2003. The Notes to the Combined Financial Statements of the LANXESS Subgroup for the year 2003 therefore apply accordingly.

In particular, preparation of these interim Combined Financial Statements also demands the making of supplementary assumptions and projections that affect the amounts and presentation of assets and liabilities, income and expenses and contingent liabilities. Actual figures could differ from the estimates. The Combined Financial Statements published here therefore do not necessarily reflect the financial condition and results of operations that would have resulted had the LANXESS Subgroup already existed as an independent group as of January 1, 2002 and the underlying transactions between the LANXESS and Bayer companies thus been entered into as between independent companies. For the reasons set forth herein, the absence of historical unity and independence of the LANXESS Group limits the informative value of the Combined Financial Statements. Therefore, the Combined Financial Statements do not enable reliable forecasts concerning the future development of the businesses combined in the LANXESS Subgroup.

Material Events since September 30, 2004

- Extraordinary stockholders' meeting of Bayer AG

At the extraordinary stockholders' meeting of Bayer AG on November 17, 2004, the stockholders approved the Spin-Off and Acquisition Agreement between Bayer AG and Lanxess AG, Leverkusen dated September 22, 2004. The Spin-Off will become effective with its registration in the Commercial Register for Bayer AG. At the time the Spin-Off takes effect, each stockholder of Bayer AG will receive one additional LANXESS share for every ten shares in Bayer AG.

- Recourse to a syndicated line of credit

In connection with the formation of the LANXESS Subgroup, financial debt was concentrated within LANXESS AG or LANXESS GmbH to the extent possible and economically practicable. Once the spin-off takes effect, the LANXESS Group will refinance itself, in particular by means of a syndicated credit line, to enable it to redeem the financial liabilities toward the Bayer Group that were transferred to the LANXESS Subgroup upon its formation. The syndicated line of credit is expected to consist of a short-term and a long-term tranche totalling between €1 and 1.5 billion. In addition, up to €200 million of financing capacity is expected to be created by way of an asset-backed commercial paper program. The loan terms and conditions will be determined during the fourth quarter of 2004. In countries with heavily regulated capital markets, such as China, the LANXESS Group will also finance itself using local bank loans. A further component of the LANXESS Group's financing is the convertible bond.

- Transfer of real property from Bayer AG to LANXESS GmbH

Before the spin-off of the LANXESS Group takes effect, Bayer AG and LANXESS GmbH will — probably in the fourth quarter of 2004 — enter into a land purchase agreement, subject to the condition subsequent that the spin-off process continues as planned. Pursuant to this agreement, LANXESS GmbH will purchase virtually all of the real property it currently uses as well as additional real property in Germany (together with any fixtures and accessories). The areas of land to be sold relate almost exclusively to areas of as yet unsurveyed land on the chemical park sites at Leverkusen, Dormagen, Krefeld-Uerdingen and Brunsbüttel. The land areas to be sold appear on the land survey plan (Grundstücksflächenplan) that has been attached to the master agreement as an appendix. Title to the real property as well as the benefits and burdens associated therewith will immediately pass to LANXESS GmbH once the land purchase agreement takes effect. The purchase price for the real property will be determined on the basis of a valuation that has yet to be completed by an expert appraiser, and will become due and payable immediately upon the land purchase agreement taking effect. Based on initial estimates, the purchase price will amount to approximately €265 million. Consummation *in rem* of the agreement for the sale of real property will take place as soon as the relevant land register requirements have been met.

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LANXESS AG (formerly SIFRI Beteiligungs AG)
Three-year Overview, Annual Financial Statements (HGB)
as of December 31, 2003 and Excerpts
from the Annual Financial Statements (HGB)
for the Fiscal Years 2002 and 2001

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SIFRI Beteiligungs Aktiengesellschaft, Frankfurt am Main
Balance Sheets as of December 31, 2003, 2002 and 2001

	Dec. 31, 2003	Dec. 31, 2002 (€)	Dec. 31, 2001
Assets			
A. Current assets			
I. Receivables and other assets (thereof from affiliated companies: 2003: €78.28; 2002: €23.00; 2001: €85.50)	401.91	490.89	718.49
II. Cash in banks (thereof at affiliated companies: 2003: €48,703.75; 2002: €48,743.95; 2001: €48,702.53)	48,703.75	48,743.95	48,702.53
Total assets	**49,105.66**	**49,234.84**	**49,421.02**
Stockholders' Equity and Liabilities			
A. Stockholders' equity			
I. Subscribed capital	50,000.00	50,000.00	50,000.00
II. Unappropriated loss	(1,914.34)	(1,765.16)	(1,548.98)
	48,085.66	48,234.84	48,451.02
B. Accruals and Provisions	1,020.00	1,000.00	970.00
Total stockholders' equity and liabilities	**49,105.66**	**49,234.84**	**49,421.02**

SIFRI Beteiligungs Aktiengesellschaft

Income Statements for the Fiscal Years 2003, 2002 and 2001 (January 1 to December 31)

		2003	2002	2001
			(€)	
1.	Other operating income	7.34	10.34	9.79
2.	Other operating expenses	1,235.00	1,643.09	1,744.81
3.	Other interest and similar income	1,078.07	1,416.34	1,950.78
	(thereof from affiliated companies: 2003: €1,078.07; 2002: €1,416.34; 2001: €1,950.78)			
4.	Result from ordinary operations	(149.59)	(216.41)	215.76
5.	Refunded taxes on income	0.41	0.23	0.10
6.	Loss/Profit for the year	(149.18)	(216.18)	215.86
7.	Loss carried forward from prior year	(1,765.16)	(1,548.98)	(1,764.84)
8.	**Unappropriated loss**	**(1,914.34)**	**(1,765.16)**	**(1,548.98)**

SIFRI Beteiligungs Aktiengesellschaft, Frankfurt am Main

Balance Sheet as of December 31, 2003

			-€-	Prior year -€k-
Assets				
A.	**Current assets**			
	I.	Receivables and other assets (thereof from affiliated companies: €78.28 (prior year: €0.1k))	401.91	0.5
	II.	Cash in banks (thereof at affiliated companies: €48,703.75 (prior year: €48.7k))	48,703.75	48.7
Total assets			**49,105.66**	**49.2**
Stockholders' Equity and Liabilities				
A.	**Stockholders' equity**			
	I.	Subscribed capital	50,000.00	50.0
	II.	Unappropriated loss	(1,914.34)	(1.8)
			48,085.66	48.2
B.	**Accruals and Provisions**		1,020.00	1.0
Total stockholders' equity and liabilities			**49,105.66**	**49.2**

SIFRI Beteiligungs Aktiengesellschaft, Frankfurt am Main

Income Statement for the Fiscal Year from January 1 to December 31, 2003

		-€-	Prior year -€k-
1.	Other operating income	7.34	< 0.0
2.	Other operating expenses	1,235.00	1.6
3.	Other interest and similar income (thereof from affiliated companies €1,078.07 (prior year: €1.4k))	1,078.07	1.4
4.	Result from ordinary operations	(149.59)	(0.2)
5.	Refunded taxes on income	0.41	0.0
6.	Loss for the year	(149.18)	(0.2)
7.	Loss carried forward from prior year	(1,765.16)	(1.6)
8.	**Unappropriated loss**	**(1,914.34)**	**(1.8)**

SIFRI Beteiligungs Aktiengesellschaft, Frankfurt am Main

Notes for the Fiscal Year 2003

1. Accounting and valuation methods

Current assets are stated at acquisition costs/nominal value.

Accruals and provisions are recognised for uncertain liabilities and are stated at the amounts required based on sound business judgement.

The income statement has been prepared using the cost summary method.

The facilitation rules in accordance with the regulations of §§ 266 (1) sentence 3, 288 HGB (German Commercial Code) for small corporations according to § 267 (1) HGB have been used in preparing the financial statements.

2. Cash in banks

The cash account is kept at an affiliated company.

3. Subscribed capital

The share capital of the company is divided into 50,000 non par value bearer shares with an equitable interest in the share capital of €1.00 each. It is fully paid in. Deutsche Bank AG, Frankfurt/Main has informed the company about the existence of a majority investment in accordance with § 20 (4) AktG (German Stock Corporation Act).

4. Unappropriated loss

The unappropriated loss of €1,914.34 includes a loss carried forward from the prior year of €1,765.16.

5. Executive bodies

Supervisory board

— Jens Bischoff, Dipl.-Wirtschaftsingenieur, Frankfurt am Main
– Chairman –

— Dr. Karsten Munscheck, Dipl.-Kaufmann, Eppstein
– Vice Chairman –

— Dr. Henning Schröer, Syndicus, Königstein

The members of the supervisory board are all employees of Deutsche Bank AG.

Management board

— Bernd Amlung, Frankfurt am Main

— Till Staffeldt, Frankfurt am Main

6. Other information

Deutsche Bank AG, Frankfurt/Main is sole stockholder of the company. The announcement in accordance with § 42 AktG has been made. The exempting group financial statements (§ 292a HGB) prepared by Deutsche Bank in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP), and in which the company is not included, are published in the Federal Gazette and filed with the Commercial Register of the Local Court in Frankfurt am Main (HRB 30000).

Frankfurt am Main, April 14, 2004

SIFRI Beteiligungs Aktiengesellschaft

The Management Board

SIFRI Beteiligungs Aktiengesellschaft
Frankfurt am Main

Management Report for the Fiscal Year 2003

In 2003, the business activity of our company was, once again, limited to the investment of short term funds with financial institutions. Due to the administrative costs of the company, which were set off only in part by a smaller amount of interest income, the resultant loss for the year amounted to approximately €149. As a result, stockholders' equity declined to approximately €49,086. Also, compared to the previous year, in 2003 the short term funds declined by approximately €40 to approximately €48,704.

For the fiscal year 2004 we expect a balanced result from the management of the company's assets. At present, a future engagement in other business activities is not foreseeable. Therefore, there are at present no risks in evidence that could have a material effect on the net assets, financial position and results of operations of our company.

SIFRI Beteiligungs Aktiengesellschaft is a subsidiary of Deutsche Bank AG. Because of the close relationship between the company and Deutsche Bank AG, the board has issued a report detailing the business transactions with related parties. That report ends with the following conclusion:

''To the best of our knowledge at the time when completed, all transactions with related parties were carried out such that the company received adequate remuneration in every such transaction. Other than those transactions mentioned, which were carried out by our company on behalf or in the interest of related parties, there were no transactions during the fiscal year 2003. Furthermore, the company did not undertake or omit to undertake any other actions on behalf or in the interest of any related parties within the same period.''

Frankfurt am Main, April 14, 2004

SIFRI Beteiligungs Aktiengesellschaft
The Management Board

Auditor's Report

I have audited the annual financial statements, together with the bookkeeping system and the management report of SIFRI Beteiligungs Aktiengesellschaft for the fiscal year from January 1, 2003 to December 31, 2003. The maintenance of the books and records and the preparation of the annual financial statements and management report in accordance with German commercial law are the responsibility of the Company's Board of Management. My responsibility is to express an opinion on the annual financial statements, the bookkeeping system, and the management report based on my audit. I conducted my audit of the annual financial statements in accordance with § 317 HGB (*Handelsgesetzbuch*, German Commercial Code) and the German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (IdW).

Those standards require that I plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the annual financial statements in accordance with German principles of proper accounting and in the management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Company and expectations of possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the books and records, the annual financial statements and the management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the accounting principles used and significant estimates made by the Company's Management Board, as well as evaluating the overall presentation of the annual financial statements and management report. I believe that my audit provides a reasonable basis for my opinion.

My audit has not led to any reservations.

In my opinion, the annual financial statements give a true and fair view of the net assets, financial position and results of operations of the Company in accordance with German principles of proper accounting. On the whole the management report provides a suitable understanding of the Company's position and suitably presents the risks of future development.

Bad Homburg, May 28, 2004

Sell
Wirtschaftsprüfer
(German Public Auditor)

SIFRI Beteiligungs Aktiengesellschaft,
Frankfurt am Main

Notes for the Fiscal Year 2002

1. Accounting and valuation methods

Current assets are stated at acquisition costs/nominal value.

Accruals and provisons are recognised for uncertain liabilities and are stated at the amounts required based on sound business judgement.

2. Cash in banks

The current and the fixed deposit-accounts of the company are kept at an affiliated company.

3. Subscribed capital

The share capital of the company is divided into 50,000 non par value bearer shares with an equitable interest in the share capital of €1.00 each. It is fully paid in. Deutsche Bank AG, Frankfurt am Main has informed the company about the existence of a majority investment in accordance with § 20 (4) AktG (German Stock Corporation Act).

4. Unappropriated loss

The unappropriated loss of €1,765.16 includes a loss carried forward from the prior year of €1,548.98.

5. Executive bodies

Supervisory board

— Jens Bischoff, Dipl.-Wirtschaftsingenieur, Frankfurt am Main – Chairman –

— Dr. Karsten Munscheck, Dipl.-Kaufmann, Eppstein – Vice Chairman –

— Dr. Henning Schröer, Syndicus, Königstein

The members of the supervisory board are all employees of Deutsche Bank AG.

Management board

— Bernd Amlung, Frankfurt am Main

— Onder Unsal, Frankfurt am Main (until August 14, 2002)

— Till Staffeldt, Frankfurt am Main (effective August 14, 2002)

6. Other information

Deutsche Bank AG, Frankfurt/Main is sole stockholder of the company. The announcement in accordance with § 42 AktG has been made. The exempting group financial statements (§ 292a HGB (German Commercial Code)) prepared by Deutsche Bank in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP), and in which the company is not included, are published in the Federal Gazette and filed with the Commercial Register of the Local Court in Frankfurt am Main (HRB 30000).

Frankfurt am Main, Mai 28, 2003

SIFRI Beteiligungs Aktiengesellschaft
The Management Board

SIFRI Beteiligungs Aktiengesellschaft
Frankfurt am Main

Management Report 2002

In 2002, the business activity of our company was, once again, limited to the investment of short term funds with financial institutions. Due to the administrative costs of the company, which were set off only in part by a smaller amount of interest income, the resultant loss for the year amounted to €216.18, and stockholders' equity declined by the same amount. Compared to the previous year, in 2002 the short term funds changed only marginally.

For the fiscal year 2003 we expect a balanced or slightly positive result from the management of the company's assets. At present, a future engagement in other business activities is not foreseeable. Therefore, there are at present no risks in evidence that could have a material effect on the net assets, financial position and results of operations of our company.

SIFRI Beteiligungs Aktiengesellschaft is a subsidiary of Deutsche Bank AG. Because of the close relationship between the company and Deutsche Bank AG, the board has issued a report detailing the business transactions with related parties. That report ends with the following conclusion:

''To the best of our knowledge at the time when completed, all transactions with related parties were carried out such that the company received adequate remuneration in every such transaction. Other than the those mentioned, which were carried out by our company on behalf or in the interest of related parties, there were no transactions during the fiscal year 2002. Furthermore, the company did not undertake or omit to undertake any other actions on behalf or in the interest of any related parties within the same period.''

Frankfurt am Main, May 28, 2003

SIFRI Beteiligungs Aktiengesellschaft
The Management Board

Auditor's Report

I have audited the annual financial statements together with the bookkeeping system and the management report of SIFRI Beteiligungs Aktiengesellschaft for the fiscal year from January 1, 2002 to December 31, 2002. The maintenance of the books and records and the preparation of the annual financial statements and management report in accordance with German commercial law are the responsibility of the Company's Board of Management. My responsibility is to express an opinion on the annual financial statements, together with the bookkeeping system, and the management report based on my audit. I conducted my audit of the annual financial statements in accordance with § 317 HGB (*Handelsgesetzbuch*, German Commercial Code) and the German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (IdW).

Those standards require that I plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the annual financial statements in accordance with German principles of proper accounting and in the management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Company and expectations of possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the books and records, the annual financial statements and the management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the accounting principles used and significant estimates made by the Company's Management Board, as well as evaluating the overall presentation of the annual financial statements and management report. I believe that my audit provides a reasonable basis for my opinion.

My audit has not led to any reservations.

In my opinion, the annual financial statements give a true and fair view of the net assets, financial position and results of operations of the Company in accordance with German principles of proper accounting. On the whole the management report provides a suitable understanding of the Company's position and suitably presents the risks of future development.

Eschborn, July 9, 2003

Sell
Wirtschaftsprüfer
(German Public Auditor)

SIFRI Beteiligungs Aktiengesellschaft,
Frankfurt am Main

Notes for the Fiscal Year 2001

1. Accounting and valuation methods

Current assets are stated at acquisition costs/nominal value.

Sufficient accruals and provisions are recognised for uncertain liabilities. Liabilities are stated at redemption amounts.

2. Cash in banks

The company's cash account is kept at an affiliated company.

3. Subscribed capital

The fully paid up share capital of the company is divided into 50,000 non par value bearer shares with an equitable interest in the share capital of €1.00 each. Deutsche Bank AG, Frankfurt/Main has informed the company about the existence of a majority investment in accordance with § 20 (4) AktG (German Stock Corporation Act).

4. Unappropriated loss

The unappropriated loss of €1,548.98 includes a loss carried forward from the prior year of €1,764,84.

5. Executive bodies

Supervisory board

Jens Bischoff, Dipl.- Wirtschaftsingenieur, Frankfurt am Main – (effective August 29, 2001) – Chairman

Dr. Holger Lindner, Dipl.-Volkswirt, Frankfurt am Main – Chairman – (effective January 17, 2001 until August 29, 2001)

Onder Unsal, Dipl.-Kaufmann, Frankfurt am Main – Chairman – (until January 17, 2001)

Dr. Karsten Munscheck, Dipl.- Kaufmann, Eppstein – Vice Chairman – (effective January 17, 2001)

Hans-Hermann Lotter, Dipl.- Wirtschaftsmathematiker, Frankfurt am Main – Vice Chairman – (until January 17, 2001)

Dr. Henning Schröer, Syndicus, Königstein

The members of the supervisory board are all employees of Deutsche Bank AG.

Management board

Bernd Amlung, Frankfurt am Main

Onder Unsal, Frankfurt am Main (effective January 17, 2001)

Dr. Markus Weber, Oberursel (until February 14, 2001)

6. Other information

Deutsche Bank AG, Frankfurt am Main is sole stockholder of the company. The announcement in accordance with § 42 AktG has been made. The group financial statements prepared by Deutsche Bank, and which do not include the company in accordance with § 296 (2) HGB (German Commercial Code), are published in the Federal Gazette and filed with the Commercial Register for the Local Court in Frankfurt am Main (HRB 30000).

Frankfurt am Main, July 18, 2002

SIFRI Beteiligungs Aktiengesellschaft
The Management Board

SIFRI Beteiligungs Aktiengesellschaft
Frankfurt am Main

Management Report for 2001

In 2001, the business activity of our company, which was founded on 28th October 1999, was, once again, limited to the investment of short term funds with financial institutions. Due to the interest income of the invested funds, set off in part by administrative costs of the company, the annual income amounted to €215.76, and stockholders' equity increased by the same amount. Compared to the previous year, in 2001 the short term funds changed only marginally.

For the fiscal year 2002 we expect a balanced or slightly positive result from the management of the company's assets. At present, a future engagement in other business activities is not foreseeable. Therefore, there are at present no risks in evidence that could have a materiel effect on the net assets, financial position and results of operations of our company.

SIFRI Beteiligungs Aktiengesellschaft is a subsidiary of Deutsche Bank AG. Because of the close relationship between the company and Deutsche Bank AG, the board has issued a report detailing the business transactions with related parties. That report ends with the following conclusion:

''To the best of our knowledge at the time when completed, all transactions with related parties were carried out such that the company received adequate remuneration in every such transaction. Other than the those mentioned, which were carried out by our company on behalf or in the interest of related parties, there were no transactions during the fiscal year 2001. Furthermore, the company did not undertake or omit to undertake any other actions on behalf or in the interest of any related parties within the same period.''

Frankfurt am Main, July 18, 2002

SIFRI Beteiligungs Aktiengesellschaft
The Management Board

Auditor's Report

I have audited the annual financial statements, together with the bookkeeping system and the management report of SIFRI Beteiligungs Aktiengesellschaft, Frankfurt am Main, for the fiscal year from January 1, 2001 to December 31, 2001. The maintenance of the books and records and the preparation of the annual financial statements and management report in accordance with German commercial law are the responsibility of the Company's Board of Management. My responsibility is to express an opinion on the annual financial statements, together with the bookkeeping system, and the management report based on my audit. I conducted my audit of the annual financial statements in accordance with § 317 HGB (*Handelsgesetzbuch*, German Commercial Code) and the German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (IdW).

Those standards require that I plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the annual financial statements in accordance with German principles of proper accounting and in the management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Company and expectations of possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the books and records, the annual financial statements and the management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the accounting principles used and significant estimates made by the Company's Management Board, as well as evaluating the overall presentation of the annual financial statements and management report. I believe that my audit provides a reasonable basis for my opinion.

My audit has not led to any reservations.

In my opinion, the annual financial statements give a true and fair view of the net assets, financial position and results of operations of the Company in accordance with German principles of proper accounting. On the whole the management report provides a suitable understanding of the Company's position and suitably presents the risks of future development.

Eschborn, August 12, 2002

Sell
Wirtschaftsprüfer
(German Public Auditor)

Information Relating to Recent Business Developments and Outlook for LANXESS

Group sales increased in the first nine months of fiscal year 2004 compared to the prior-year period as a result of increases in both sales volume and prices, despite negative currency effects resulting from the weakness of the U.S. dollar, which once again came under pressure particularly in the fourth quarter of fiscal year 2004. The Engineering Plastics and Chemical Intermediates segments reported the strongest increase in sales in the first nine months of fiscal year 2004. The increase in the cost of raw materials could to some extent be passed on to customers by means of price increases, particularly beginning in the third quarter. In October and November 2004, the positive sales trend of the preceding months continued in the Performance Rubber, Engineering Plastics and Chemical Intermediates segments, while sales of the Performance Chemicals segment stagnated because of negative currency effects. From a regional perspective, substantial sales increases were reported in the dynamic economic environments of Asia and North America. The economic upturn also reached Europe, such that sales increased there as well.

Compared to the prior year period, operating result (EBIT) increased significantly in the first nine months of fiscal year 2004 as a result of volume growth, price increases and cost savings. All of the segments contributed to the increase with the exception of Performance Chemicals, where operating result in the first nine months of fiscal year 2004 was substantially affected by exceptional items.

The Company expects a negative operating result (EBIT) in the fourth quarter 2004 as a result of the somewhat lower sales volume anticipated for December, the normally higher expenses in the fourth quarter and exceptional items. Nevertheless, based on the positive development in the first three quarters of fiscal year 2004, LANXESS currently anticipates that operating result (EBIT) before exceptional items in fiscal year 2004 exceeds that of the prior year.

The international chemicals and polymers markets are currently experiencing a general upward trend which the Company expects to peak in 2006 or 2007. The LANXESS portfolio includes operations in the basic chemicals and fine and specialty chemicals sectors. The latter two typically exhibit less pronounced economic cycles. The Company believes that the basic chemicals business is currently benefiting disproportionately from recovery potential in terms of price and volume trends.

Against this background, the Company expects that demand for chemical and polymer products will increase further in fiscal year 2005 and that this will result in positive effects on volume and price for a large portion of its product portfolio. However, should the cost of raw materials and energy prices rise again, this could have a negative effect on the economy and thus on business development. The continuing strength of the euro could also negatively affect exports.

The Company is targeting an improvement in its operating result (EBIT) adjusted for exceptional items. This expected improvement will, in the view of the Board of Management, be considerably influenced by the generally favourable business trend.

Leverkusen, 18 January 2005

LANXESS AG

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Glossary

Acrylonitrile-butadiene-styrene (ABS)	Polymer blend of acrylonitrile-styrene-copolymers and 1, 3-butadiene. ABS belongs to the group of elastomer-modified thermoplastics, possesses a high impact strength and heat resistance, and is used primarily for the manufacture of high-quality technical components.
Acrylonitrile	Also known as vinyl cyanide; is used, for example, as a raw material for the manufacture of homo- and copolymers in the fibre, plastic and synthetic rubber sectors.
Acrylonitrile-styrene-acrylic ester (ASA)	This impact-resistant copolymer has similar properties to ABS, but is more weather-resistant. In the case of ASA, the acrylic ester is distributed uniformly in an SAN (styrene-acrylonitrile) polymer and is linked by grafted SAN chains. ASA forms high-quality, semi-matt and scratchproof surfaces, and is resistant to water-based chemicals.
Adipic acid	Colourless solid that is used as an key raw material for the manufacture of PA 6.6 and as an intermediate during the manufacture of plasticisers, polyesters and polyurethanes, etc.
Adsorbers...................	Adsorption agents are usually solid substances whose large surface areas enable them to concentrate (adsorb) certain substances from gaseous or liquid mixtures selectively at their interface.
Amines	Nitrogen-containing gases, liquids or solids that can be regarded as substitution products of ammonia. They serve, for example, as starting materials for the manufacture of surfactants, process chemicals and dyestuffs, and also as bases in chemical reactions.
Amino alcohols	Chemical compounds that contain both amino (nitrogen-containing) and hydroxyl or ether (oxygen-containing) groups.
Ammonia	Nitrogen-containing base product used in the chemical industry as the starting material for the manufacture of, for example, urea, sulphonamides, and synthetic fibres or in the form of ammonium salts for fertilisers.
Aniline......................	Liquid aromatic amine that is used as one of the most important key substances in aromatic chemistry.
Aromatics network	Production network that manufactures intermediates based on simple aromatic raw materials such as benzene or toluene for — among other things — the subsequent synthesis of agrochemicals or plastics.
Azodicarbonamide...........	Azodicarbonamide, which decomposes at 190 °C to nitrogen, carbon monoxide, carbon dioxide and traces of ammonia, is used as a blowing agent for thermoplastics and elastomers.
B2B (Business-to-business) ..	Electronic commerce, the trading of goods and services using electronic communications, e.g., via the Internet. Commercial relationships between commercial undertakings are referred to as ''business-to-business''.
Benzene	Colourless liquid, a key aromatic product that is recovered from oil or coal and serves as the basis for numerous aromatic intermediates.

Benzyl chloride	Benzyl chloride is produced by the chlorination of toluene and is used, for example, for the manufacture of dyestuffs, pharmaceuticals, synthetic resins, perfumes and vulcanisation accelerators.
Benzyl products	Collective name for compounds that contain the benzyl group, an aromatic hydrocarbon group, as part of the molecule.
Biocides	Active ingredients and preparations that serve to deter, disarm or destroy harmful organisms, such as bacteria and fungi, by chemical or biological means.
Blend	Generally, a mixture of two or more substances. In particular, different polymers are mixed together to selectively modify specific properties of the individual components, e.g., to increase the impact resistance of a brittle polymer by adding rubbers.
Blowing agent	Collective term for blowing gases or substances that develop blowing gases under the influence of heat or chemicals.
Bromobutyl rubber	See butyl rubber.
Butadiene	Colourless, easily liquefied gas that is used, for example, as the raw material for the manufacture of synthetic rubbers (e.g., polybutadiene rubber) and thermoplastic copolymers (e.g., ABS).
Butyl rubber	Butyl rubbers are copolymers of isobutylene and isoprene. Vulcanised butyl rubber is characterised by very low gas permeability and high stability. The property profile can be modified selectively by halogenation of butyl rubber to form bromobutyl or chlorobutyl rubber.
C4 raffinate 1	Cleaned mineral oil product; it consists mainly of isobutylene, butylene and butane.
Caprolactam	An intermediate obtained from cyclohexane for the manufacture of polyamide.
Chloroaromatics	Collective term for chlorinated aromatic compounds that are used for various applications, e.g., as intermediates for the manufacture of pharmaceuticals, pesticides, crop protection agents and preservatives.
Chlorobenzenes	These belong to the group of chloroaromatics.
Chlorobutyl rubber	See butyl rubber.
Chlorination	Introduction of chlorine into a chemical compound by addition or substitution. Chlorination is frequently performed using chlorine itself or a chlorine carrier such as thionyl chloride.
Chloroprene	2-chloro-1, 3 butadiene; chloroprene is polymerised almost completely to chloroprene rubber (CR) (Neopren®, Baypren®).
Chlorotoluenes	These belong to the group of chloroaromatics.
Chromium (VI)	Hexavalent oxidation state of chromium.
Chromium oxide pigments ...	Powders that are stable in the presence of light, air, acid and alkaline materials, and which are used for coatings, building materials, plastics, enamels and ceramics.
Commoditisation	Describes the process in a product's life-cycle whereby it becomes a ''commodity'', *i.e.*, the product is present in mature, price-driven markets with standardised product characteristics.

Cresols .... Cresols are basic aromatic chemicals used, for example, in the production of antioxidants.

Cyclohexane .... Colourless liquid that is normally produced by hydrogenating benzene and is used, for example, in the manufacture of caprolactam and adipic acid.

Dichromates .... Salts of dichromic acid, which are used especially as raw materials for chrome tanning agents and chromic acid.

Elastane fibres .... Also known as spandex; extremely expandable synthetic elastomer fibres.

Emulsifiers .... Additives for the manufacture and stabilisation of emulsions, which can be more accurately described as surface-active substances or surfactants, and mostly exist as oily or waxy substances, but also as powders.

Ethylene-propylene-copolymers .... General term for the products generated during the vulcanisation of copolymers from ethylene and propylene (ethylene-propylene rubbers).

EPDM .... Abbreviation for ethylene-propylene-diene terpolymers.

Ethylene-propylene rubber ... See ethylene-propylene copolymers.

Ethylene-vinyl acetate copolymers .... Abbreviation EVA; EVAs are copolymers of ethylene and vinyl acetate. They are used, for example, for the manufacture of heat-and weather-resistant technical rubber goods, such as sealing gaskets, or as additives for natural rubber and SBR vulcanisates to improve ageing and ozone resistance; EVAs are also used as hot-melt, solvent or dispersion adhesives.

Fine chemicals .... Term for chemicals that are produced in small quantities (on laboratory scale up to approximately 5,000 tonnes) and in various degrees of purity for a variety of applications.

Flame retardant .... Collective term for materials that impart flame-retarding properties especially to wood and wood composites, plastics and textiles.

Fluorescent whitening agents . . Chemical compounds that prevent greying or yellowing of textiles, paper, plastics, etc., by producing a brightening effect and simultaneously simulating bleaching by converting ultraviolet radiation into visible light.

Functional chemicals .... Substances that selectively influence one or more properties of products, e.g., additives for paper manufacture or textile processing.

Functional polymers .... Serve one single purpose in contrast to general-purpose plastics or engineering/high-performance plastics.

Glass fibres .... Fibres manufactured from glass that can be used as reinforcements in polymers.

Hexanediol .... Colourless solid for the manufacture of hexanediamine, polyesters, polyurethanes and other materials.

High impact polystyrene (HIPS) .... Polystyrene, which is relatively brittle as a pure compound, can be converted to high impact polystyrene by copolymerisation, e.g., with acrylonitrile and butadiene.

Hybrid technology .... For the production of plastic/metal composites.

Hydrazine hydrate	Aqueous solution of hydrazine (diamide) for use as a corrosion inhibitor, dechlorination agent for water and as an intermediate for the synthesis of pharmaceutical compounds and crop protection agents.
Hydrocarbons	Common abbreviation used by the chemical industry for the aromatics benzene, toluene, xylene and ethyl benzene.
Hydrofluoric acid	Colourless liquid that is used to etch glass and metals, manufacture printed-circuit boards and chips, in façade cleaners, to remove enamels, to de-sand metal castings and in electroplating processes.
Hydrogenated nitrile-butadiene rubber (HNBR)	A specific improvement of the characteristics of nitrile-butadiene rubber, e.g., temperature stability, achieved by hydrogenation.
Hydrogenation	Term for the usually catalytic introduction of hydrogen into organic compounds, generally by means of the addition of hydrogen.
Hydrolysis protection	Protection against the influence of water.
Ion exchanger	Collective term for solid materials or liquid solutions that are able to take up charged particles from an aqueous electrolyte solution by releasing equivalent quantities of other particles.
Iron oxide pigments	Collective term for a large group of natural or synthetic yellow, red, brown and black iron pigments, which contain iron oxides as the main colouring components.
Isobutylene	Colourless gas, used as the raw material for the manufacture of butyl rubber and other products.
Isocyanate	Organic compounds with at least one isocyanate group (nitrogen-, carbon-, oxygen-containing molecule group). Isocyanates are widely used in the chemical industry due to their reactivity, especially for the manufacture of polyurethane plastics.
Isomer separation	Isomer is the chemical term for compounds that consist of an identical number of the same atoms, which can differ in their configuration, however. There are numerous, sometimes very complex processes, to separate such isomers.
‘‘Kautschuk’’ (Rubber)	The German term ‘‘Kautschuk’’ (Rubber) is used to define non-crosslinked but vulcanisable polymers with rubber-elastic properties at 20 °C. These serve as raw materials for the manufacture of elastomers and (vulcanised) rubber. Rubbers are classified systematically into natural and synthetic rubbers.
Landfill leachate	Water originating from precipitation or waste that flows through landfill bodies and absorbs water soluble materials contained in the waste.
Latex	The term ‘‘latex’’ was originally restricted to the chyle of plants supplying rubber. Today, the term latex is used to describe very general dispersions of polymers in aqueous media.
Leather finishing auxiliaries . .	Substances used to improve leather quality after tanning.
Lösungs-Styrol-Butadien-Kautschuk.	German term for SSBR (solution styrene-butadiene rubber).

Maleic anhydride .... Colourless solid that is mainly used for the manufacture of unsaturated polyester resins and for the modification of alkyd resins.

Merchant producer .... Manufacturers not manufacturing for their own production, e.g., synthetic rubbers for tyre production.

Monoisocyanates .... Organic compounds comprising an isocyanate group and an organic residue. In contrast to diisocyanates, they are used for the synthesis of agrochemicals and/or biocides and other products.

Monofilament fibres .... Engineering fibres, often based on polyamides or polyesters.

Monomers .... Compounds whose molecules can form one or more recurrent units during polymerisations.

Nitration .... Introduction of nitro groups (nitrogen and oxygen-containing groups) into organic compounds.

Nitrile-butadiene rubber ..... Term for a synthetic rubber that is produced by the copolymerisation of acrylonitrile and butadiene.

Nitrotoluenes .... Fluid or solid materials, aromatic compounds that contain at least one nitro group. They serve as intermediates for pigments, plastics, pharmaceuticals, fragrances, explosives (TNT) or polyurethane starting products (isocyanates).

Phosgenation .... Phosgenation is the reaction of phosgene with organic molecules, e.g. for the manufacture of isocyanates. Gaseous phosgene is used for organic syntheses, e.g., for chlorination, dehydration or introduction of CO groups.

Phosphorous chlorides ...... Fluids for the manufacture of organic phosphorous compounds and as chlorination agents.

Phthalic anhydride .... A solid that belongs to the technically most important aromatic compounds and is used during the manufacture of plasticisers, alkyd and polyester resins, dyestuffs and numerous fine chemicals.

Pigments .... Latin: *pigmentum* = artists' colour. A coloured or achromatic colouring agent, which is virtually insoluble in the application medium, used for the manufacture of printing ink, the colouring of paints, surface coatings, plastics, paper, textiles, cement, etc.

Plastic additives .... Additives that influence the properties of a plastic.

Polyacrylates .... Polymers based on esters of acrylic acid.

Polyamide (PA) .... Collective term for polymers whose basic units are held together by amide bonds. The abbreviation PA is frequently used in association with numerals that represent the number of carbon atoms in the starting material from which the polyamides were manufactured, e.g. PA 6 for polyamides based on ε-caprolactam (C6), PA 6.6 for those based on hexamethylenediamine (C6) and adipic acid (C6) or PA 6/12 for copolymers of ε-caprolactam (C6) and ώ-dodecanolactam (C12).

Polyamide 6 .... See polyamide (PA).

Polyamide 6.6 .... See polyamide (PA).

Polyamide-acrylonitrile-butadiene styrene .... Blend of polyamide and acrylonitrile-butadiene styrene.

Polyamide monofilament .... See monofilament fibres.

Polybutadiene rubber	Synthesised rubber based on polymerised 1, 3-butadiene.
Polybutylene terephthalates (PBT)	Thermoplastic polymer with high strength, stiffness, hardness, toughness at low temperatures and heat resistance.
Polychloroprene hard rubber	See chloroprene.
Polyester monofilament	See monofilament fibres.
Polymer	A substance that is constructed from numerous molecules characterised by the multiple repetition of constitutive units or building blocks.
Polymer dispersions	A dispersion is defined as a two- or multi-phase system in which a finely-divided material, e.g., a polymer, is distributed in another material.
Polyols	Collective term for molecules that contain several alcohol groups.
Polycyclic aromatic hydrocarbons	Polycyclic aromatic hydrocarbons are manufactured for the production of pigments, herbicides and pesticides, are contained in coal tar and crude oil, and are produced during all incomplete combustion processes and the decomposition of organic materials.
Pooling	The combination of items, receivables, and similar things.
Process chemicals	Process-supporting chemicals, e.g., during paper manufacture.
REACh	Planned EU Regulation for the registration, evaluation, authorisation and restriction of chemicals.
Retanning materials	Materials used for the retannage of animal hides.
Retention agent	Filter agent for the retention of the dispersed phase, e.g., during paper manufacture as a fibre and filler retention agent on the paper machine screen.
Reverse osmosis	Osmosis is the diffusion of solvent molecules through a semi-permeable membrane. Reverse osmosis is a form of membrane microfiltration. The reversal of normal osmosis is forced by applying an increased hydrostatic pressure.
SCALE Initiative	A ''Strategy for Environment and Health'' proposed by the European Commission.
Semi-crystalline polymer	Semi-crystalline signifies that the polymer contains both crystalline and amorphous domains side by side. The nature, size, proportion and orientation of the crystals contained in a semi-crystalline polymer have a decisive influence on the chemical and, particularly, on the physical and mechanical properties of the material.
Solvent-based finishing chemicals	Term originating from the textile and leather finishing industry in the context of the treatment of textile materials with finishing agents to influence the feel and appearance of textiles and leather.
Styrene	Aromatic base chemical widely used as a solvent and reaction partner, mainly in the manufacture of polystyrene or styrene copolymers.
Styrene-acrylonitrile (SAN)	Abbreviation for styrene-acrylonitrile copolymers

Styrene-butadiene	Collective term for copolymers of styrene and butadienes, the properties and applications of which are determined by the ratio of the two comonomers. Small butadiene quantities (approx. 5-20%, relative to the copolymer) are used to improve the impact strength of polystyrene. Copolymers with a high butadiene ratio (approx. 70-75%) in the form of styrene-butadiene rubbers are technically very important synthetic rubbers.
Sulfuryl chloride	Colourless liquid that is used as a dehydrating agent, to chlorinate organic compounds and for introducing the nitrogen dioxide group into carbon compounds.
Sulphuric acid	Clear, oily liquid which is corrosive depending on the concentration, with numerous applications, e.g. for the manufacture of fertilisers and numerous applications in organic synthesis.
Tanning auxiliaries	Materials that serve the treatment of animal hides in the tanning process.
Tanning agents, vegetable . . .	Tanning agents of vegetable origin, e.g., from tree bark.
Thionyl chloride	(Sulphurous dichloride) Colourless liquid used as chlorination agent, e.g., during the manufacture of organic intermediates and crop protection products and during the synthesis of pharmaceuticals.
Thio products	Collective term for sulphurous substances.
Toluidines	Aminotoluenes, manufactured by hydrogenation of the corresponding nitrotoluenes; pale yellow liquids used for the manufacture of pigments, vulcanisation accelerators, textile processing chemicals, etc.
Toluene	Liquid, aromatic chemical that is used as the base product for the manufacture of numerous compounds, such as chlorotoluenes and nitrotoluenes.
Triacetine	Glycerine triacetat; a colourless liquid, used among other things as solvent or carrier agent for aromas.
Trimethylol propane	Colourless, hygroscopic solid for the manufacture of protective coatings, polyethers, polyurethanes, foamed plastics, alkyd resins, plasticisers, lubricants, finishing chemicals, surfactants, elastomers, etc. and as a substitute for glycerine.
Vulcanisation	Conversion of rubber polymers into the rubber-elastic state by means of crosslinking.

Based on the foregoing Listing Memorandum,
application is hereby made to admit

73,034,192 (€73,034,192.00) no par value ordinary bearer shares
(total capital stock)

consisting of

50,000 (€50,000.00) no par value ordinary bearer shares
(existing capital stock)

and

72,984,192 (€72,984,192.00) no par value ordinary bearer shares
issued in connection with the capital increase in exchange for a contribution in kind, which was approved by resolution on 21 December 2004 and was registered on 10 January 2005,

each such share currently representing a €1.00 portion of the capital stock and carrying full dividend rights from 1 January 2004

International Securities Identification Number (ISIN): DE0005470405
German Securities Identification Code: 547040
Common Code: 020904992

of

LANXESS Aktiengesellschaft
Leverkusen

for trading on the official market segment (*amtlicher Markt*) and,
simultaneously, the official market sub-segment entailing
additional post-admission obligations (Prime Standard).

Leverkusen and Frankfurt am Main, the 18th of January 2005

Deutsche Bank
Aktiengesellschaft

Morgan Stanley Bank AG